DOCTOR OF PHILOSOPHY

Consideration of Islamic insurance, takaful for development, by re-examining and analysing existent takaful models vis-à-vis relevant English marine insurance law.

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"Consideration of Islamic insurance, *takaful* for development, by re-examining and analysing existent *takaful* models vis-à-vis relevant English marine insurance law."

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Abstract

For a prolonged period of time, there has been a long of confusion existed among the Muslim community about utilisation of insurance in Islam and that confusion was aggravated further by the existent western traditional insurance that are in use. The reason behind this is because traditional insurance contains elements of *riba* (usury), *gharar* (uncertainty) and *maisir* (game of chance), which are restrictions that hindering traditional insurance to be acceptable in Islam.

Therefore, the Muslim community came up with *takaful* which is a cooperative and mutual scheme to assist each other as brethren in matters of catastrophe. The scheme was to be managed by a *takaful* operator and as such for the management of the scheme various models have been developed. These models included *mudarabah* (investor-entrepreneur), *wakala* (principal-agent) and *waqf* (endowment) along with their hybrids. The problem that rose is that none of the models appear to be suitable or even to an extent *Sharia* compliant in them. The models lack important components such as premium, risks, excess and compensation and the models tried to balance off by making it a mutual model. Unfortunately, the models does not appear to have been analysed from all prospective including advancement in the western community and thus, hampering economic development of the Islamic finance.

This lead to the Muslim community being in chaos and ended up with a situation, worse than it was previously. The Muslims not only, do not have an appropriate model to replace the traditional insurance but also, the *takaful* models that presently in existence are in conflict. This is leading to a loss of confidence among Muslims and questioning about the validity of insurance in itself under Islamic law. There is a significant cry in the air for an innovative model which not only meets the *Sharia* requirements but also, help in advancement into the developed western community for commercial advancement. The aim of this thesis has been exactly that, in eliciting the concerns and creating the same for the assistance of not just the Muslims but also the traditional insurance market e.g. marine insurance, to progress the same and future development to bring the platforms closer.

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Glossary of common Arabic terms

Takaful: Alternative created to traditional insurance on the idea of mutuality and cooperativeness of participants coming together to help each other and the scheme being managed by an operator known as *takaful* operator.

Retakaful: An alternative created under Islamic law to traditional reinsurance, whose working idea is similar to that of *takaful* except that it is designed for indemnity cover for *takaful* operators.

Sharia: It is a system of rule that is set in Islam for Muslims to follow.

Halal: A thing or act which is allowed under the Islamic law.

Haram: This is the opposite of *halal* and as such a thing or act which is not allowed under the Islamic law.

Tabarru: A donation, gift or contribution given as a charity.

Quad Hasan: A benevolent loan provided to relieve hardship and to be returned within a time period the same principal amount without any increase.

Darura: Necessity.

Riba: Usury. It is one of the major restriction in Islamic law where loosely speaking refers to unjust enrichment without putting any effort in return e.g. in bank loan the interest is *riba* as no risk was taken in return to earn the interest.

Gharar: Uncertainty. This is another restriction in Islamic law where uncertainty in relation to the contract e.g. as in insurance where it is uncertain if and when the catastrophe will take place and if so, the extent of the obligations which party have to bear.

Maisir: Game of chances. This is another restriction in Islamic law where obligation cannot be left to chance rather needs to be clear between the parties e.g. in a poker or betting, the party is unaware whether he would lose or win the next hand or event and the consequence is left to chance rather than hard work.

Quran: The most Holy book in Islam which the Muslims consider it as a commandments of God, Allah.

Hadith: This refers to the narrations of an act or approval of the Prophet Mohammed (pbuh). There are four different *hadiths* that are well-known which are *Sahih Al-Bukhari*, *Sahih Muslim*, *Sunan Anu-Dawud* and *Malik's Muwatta* and the texts from these books are mainly considered in this thesis.

Sunnah: It is the way of life that the Prophet Mohammed (pbuh) has showed to the Muslims how to lead their lives in compliance with God's laws.

Mudarabah: An investor and entrepreneur relationship which is allowed in Islamic law.

Musaharaka: A partnership relationship where all parties contribute. Also, diminishing *musaharaka* relating to reducing partnership where one party keeps on buying off the partners shares in the partnership as such the partnership keeps on reducing.

Wakala: A principal and agent relationship which is allowed in Islamic law.

Waqf: A type of *sadaqah* i.e. voluntary charity, of an asset or cash which is an inalienable endowment for religious or charitable purposes.

Ijarah: Generally refers to a lease contract where the owner transfers the usufruct to another for use for time and price determinate. *Ijarah* also covers situation where an individual's service is rendered in consideration for a price.

Bai Salaam: This refers to a forward selling contract where payment is made at present time for goods which are to be delivered in future, where goods and time are determinate.

Ordinarily, in such cases, the buyer making the payment in present time asks the seller to provide something as surety.

Bai Mujjal: This refers to a deferred payment selling contract where goods are provided at present time whilst payment is provided at a later date, where time and price are determinate.

Ummah: Nation or community.

Aqad: A contract between the parties based on trust or utmost good faith.

Najsh: A form of fraud in a transaction to mislead another.

*Aqila: A*micable moral support and assistance

Diyya: Blood money paid as compensation to the victim's family on behalf of the murderer to avoid vengeance conflicts.

Tawakkul: Reliance of God

Fuqaha: Islamic scholars

Zakat: Compulsory charity that every Muslim has to pay every annum which is currently set at 2.5% of the total disposable asset and cash

Sadaqah: Voluntary charity.

Kafala: Guaranteeing such as standing as surety for someone else undefined matter.

Jiala: An incentive payment by someone to another as a reward for a task successfully carried out

Muwalat: Giving ones estate to another on the condition that receiver would satisfy any *diyya* that may arise against the transferor

Masalahah: Public interest

Ikhtiar i.e. preventative steps for the avoidance of possible hazards

Dhulum i.e. injustice

Inah: Refers to situation where there is a deferred payment transaction followed by another buy back transaction between same parties for lower sum or deferred payment on less time.

Acknowledgement

Bismillahir Rahmaneer Rahim

(In the name of Allah, the Beneficent, the Merciful)

Very first and foremost, I thank Allah for giving me the *hidayah* (guidance) to do this amazing project, for giving me the knowledge, for allowing me to engage with everything relevant in discovering and writing this work. I am very grateful to Allah for bestowing His mercy on me and for giving me the patience to write this thesis.

I am thankful to my supervisors, Dr. Zhen Jing and Mr. Gwilym Owen for their wonderful support and direction in helping me to write this thesis. They have been kind with me and gave me enough space to think creatively. They have been patient with me during the research process and even at times when I was feeling lost, they were generous enough to assist me to look into the big picture. I am forever indebted to them.

Also, it goes without saying, I am grateful to my wife, Kasia who has been by my side through this tough journey and inspiring me through the constant hardship, by giving me hope whenever I felt lost. She had been my constant beacon of optimism and has always been there to help me with the numerous hurdles that came along the way. Finally, this acknowledgement would be incomplete without thanking my partners, Abdur and Jaaba, whose motivation have pushed me into embarking on this adventure.

Summary

Redesigning and improvising of *takaful* model in light of English marine insurance

This thesis considers Islamic laws on traditional insurance, which generally is considered unacceptable due to its nature and presence of the aspects of *riba* (usury), *gharar* (uncertainty) and *maisir* (game of chances) in such contracts. An Islamic alternative called *takaful* has been created but is found not to be fully appropriately modelled and uncut to exist in traditional insurance markets such as English marine insurance, due to the absence of essential materials of contract construction of insurance namely premium, risks, excess and compensation. There are gaps in both practice and literatures' regarding *takaful* as it is uprising concept so it has become important to consider its credibility for advancement to avoid interrupting the ethos of English marine insurance.

This research considers the underlying structure of various *takaful* models that are existent using Islamic instruments of *mudarabah* (investor-entrepreneur), *wakala* (principal-agent) and *waqf* (endowment). It is analysed that such models, not only contradicts themselves in following the Islamic laws, but are inflexible and cumbersome to be utilized in light of traditional English marine insurance as all of these models lack the vital materials of premium, risks, excess and compensation. The aim is to redesign and create an innovative model of *takaful, which* not only will avoid malfunction in itself with Islamic laws but also would be consistent to operate alongside English marine insurance by carefully covering the four crucial concepts mentioned above. This would be done by utilization of new *Sharia* acceptable instruments as *Ijarah* (remuneration / leasing), *Bai Mujjal* (deferred sale) and *Bai Salaam* (forward sale with securitisation), which includes qualitative research including consideration of primary sources of Holy *Quran* and *hadiths.*

The proposed *takaful* model focus on of how best the basic concepts of premium, risks, excess and compensation can be implemented in *halal* manner in line with traditional marine insurance without allowing the aspects of *riba*, *gharar* and *maisir.* An insurance contract is defined as a contract of indemnification i.e. it is an instrument which is a creation from the elements of Contract and Tort. If the element of Contract is broken down, it will contain basic atoms of offer, acceptance, consideration and intention to create legal relations. Similarly, if the element of Tort is broken down, it will contain basic atoms of duty of care, breach of that duty and causation. If these basics are viewed from the marine insurance prospective, that the derivatives would form the essences of premium, risks, excess and compensation that are in play in these circumstances. The idea of the proposed *takaful* model has been quite a simple one, cautiously satisfy these derivatives with *Sharia* compliant tools being the end result is a *Sharia* compliant marine insurance model, as everything is *halal* all through the way.

The proposed model named as "*X3-I.M.S. fusion*" *takaful* model, is an instrument, whose functioning from the outset appear similar as traditional marine insurance. However, the internal structure of the proposed model has three separate phases or distillation process to create a *Sharia* complaint marine insurance model. The ideology is quite simply satisfaction of the paradigms of premium, risks, excess and compensation in *Sharia* compliant manner in

marine insurance monopoly. The proposed model starts with the aspect of premium payment from the insured to insurer. In practice, the insurer although appears to be one entity, is in fact in reality is an umbrella entity of a number of separate entities e.g. separate claims company, separate underwriting company, separate investment company of the funds and so on and so forth. In the proposed model, the researcher considers two entities in principle, one that of Claims entity (CE) and the other considered that of General entity (GE).

Phase 1 (Premium payment using a) return for service payment or b) lease rental payment):

To commence with, £X would be paid by insured to the insurer, CE. This £X is the premium reflected a payment for risk coverage in traditional marine insurance but due to *Sharia* restriction the same is not possible to be conducted under Islamic law. Therefore, for the £X to reflect a valid cause of action, the researcher uses the Islamic instrument of *Ijarah*, which is of 2 types: i) Labour based *Ijarah* ii) lease based *Ijarah.* The researcher opined that either type can be used but to commence with the easier one is the labour-based *ijarah*. Simply put under labour based *ijarah* instrument, the insured would be paying £X fee in return for the specialist risk management service of CE. The £X is benchmarked against premium, which is normally charged in traditional marine insurance, which is allowed in Islam.

Conversely, the lease based *ijarah* instrument can be used instead of labour-based *ijarah*. As the name suggest, a lease takes place for which the usufruct i.e. defined by HMRC as "*the right to the use and enjoyment of another's property*", can be used without obtaining the ownership and a fee is paid in return. As such, the more the usufruct i.e. enjoyment of property, the more the rent generally, as such they are proportional to one another. The researcher makes a distinction that all properties have two aspects namely benefits and liabilities. Therefore, whilst in most cases it is the usufruct of benefit, which is a positive enjoyment, there is, at least in theory, nothing stopping from having a contract where usufruct to be restricted to only liabilities, which is a negative enjoyment. In the proposed model, the insured enters a lease based *ijarah* contract with CE for the goods that require marine cover, however restricting enjoyment to liabilities only. Of course, risk remains with insured at all times as insured remains the owner but the insured is simply leasing the asset but restricting the extent of enjoyment of this asset for CE i.e. CE have the usufruct for negative enjoyment of the leased asset only. In this circumstances, as rent is proportional to enjoyment of the leased asset, as the enjoyment reverse their boundary so does the rent. As such, with negative enjoyment, the rent becomes payable by the insured to the insurer which is benchmarked against premium that is generally payable in orthodox marine insurance cases, that will be referred as £X.

Phase 2 (Deferred payment sale):

On this second phase of the proposed model, the goods that belong to the insured are being sold to the General Entity (GE) of the insurer, under a deferred payment sale, which is acceptable in Islam called *Bai Mujjal* contract. The goods ownership changes immediately to GE but the parties agrees a fixed payment amount of £C which is deferred to be paid by GE in a certain number of days i.e. Q days. For the moment, the readers needs to keep in mind that Q is a variable of 2 smaller variables of Y and B, where they are both denominators which add up to create the value of Q. Also, it is a freedom of contract agreement between

the parties, that should GE fail to provide £C in Q days that insured agreed to waive off the payment as charity, with no obligations.

Phase 3 (Forward payment sale):

On this third phase of the proposed model, GE is selling goods to the insured in a forward payment sale. The *Sharia* acceptable *Bai Salaam* contract allows that GE to sell the goods which will be in possession of the insurer in a certain future date but payment is provided by the insured immediately. In this case, GE sells Y days matured goods, where Y is the number of days taken for the goods to reach destination point by marine voyage. In return, insured makes a payment of £A, which is benchmarked against excess payment in orthodox marine insurance claim. The reader needs to note 2 aspects: a) £A would have the same value as £C in phase 2 and b) the *Salaam* contract concludes in Y days, where Y is a denominator in phase 2. Each of the phases as such each contract is distinct and separate, as it is crucial to be *halal* but it is a monopoly of variables and timeframes. Finally, in *Salaam* contract, it is permissible to have a surety and so, CE provides £Z security which is benchmarked to compensation.

Ultimatum:

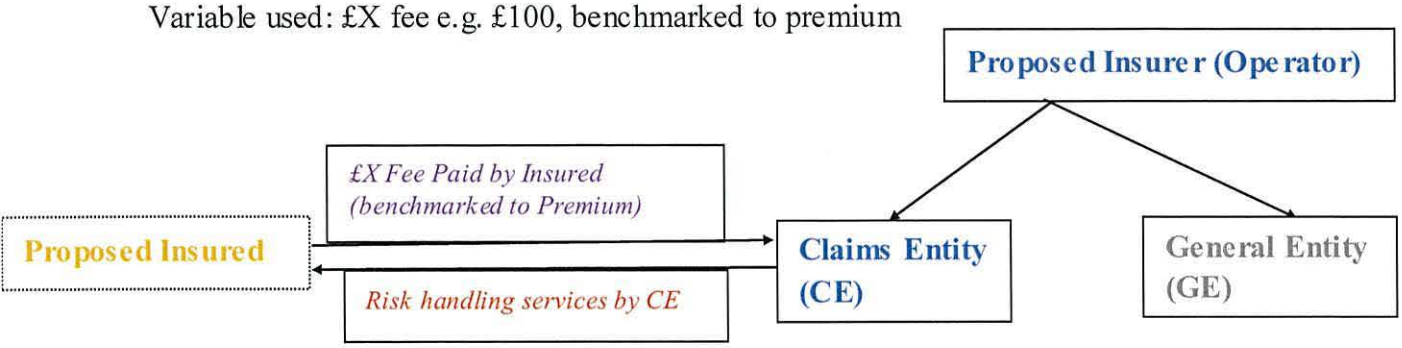
Eventually one of the situations will take place: a) either there will be a loss and a claim would be made or b) no loss so no claims and that is the end of the matter. 1st situation, in the event of loss, in phase 3 a claim is made by the insured by tapping into £Z security provided by CE as compensation, for GE failure to meet obligation within Y days. Consequently, in phase 2, Q days have passed and as per agreement, insured waives off any payment from GE and as such insurer obtains the excess payment in line with orthodox marine insurance. 2nd situation, no loss takes place and GE fulfils his obligation under phase 3, hence no compensation is tapped into by insured. Consequently, in phase 2, GE is able to meet his obligation and pay insured £C, which in essence is the return of the excess amount as is not required as in orthodox marine insurance. In international trade, it is quite common for insured to sell goods to other buyer, who in turn becomes sellers to sell to other buyers. This would not be hindered with the proposed model, as under *Sharia*, the insured is allowed to enter parallel *Salaam* contract i.e. the contract that the insured and the insurer have in phase 3, the insured is allowed to enter a promissory contract with other buyer and so on and so forth. For the assistance of readers a flowchart step-by-step diagram is included with this summary.

This is unique research as the above aspect is considered from western view, of upgrading of an age-old Islamic concept, but keeping remits of both intact. International trading and Muslim population is on the increasing and this project aim not just to set a bridge for getting two very distinct platforms closer but for stepping into a new era. Future views of Islamic insurance may change overall and could give rise to a new generation of modern types of acceptable *halal* insurance.

Proposed *"X3-I.M.S. fusion" takaful* model:

(1) (A) Phase 1 – *IJARAH* (Using Wages based *ijarah*):

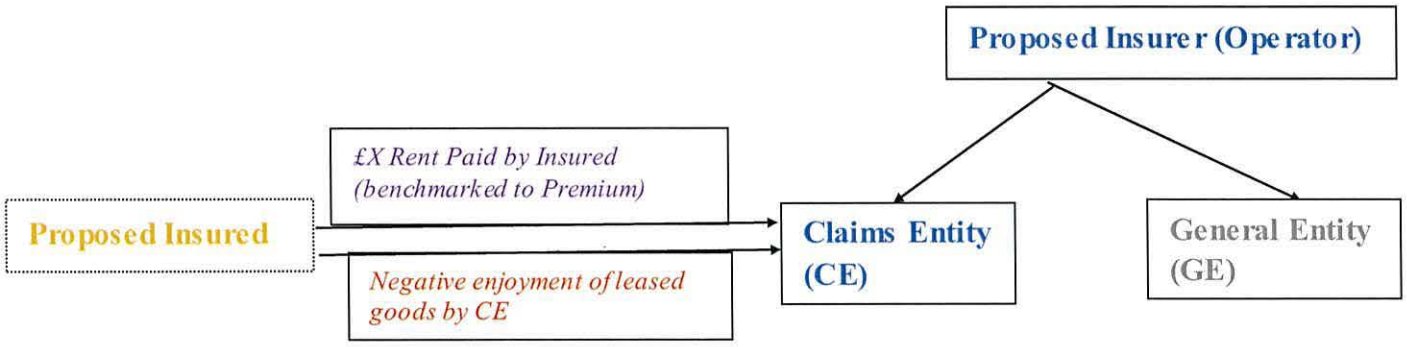
Variable used: £X fee e.g. £100, benchmarked to premium



[OR]

(1) (B) Phase 1 – (Alternative approach) *IJARAH* (Using Lease based *ijarah*):

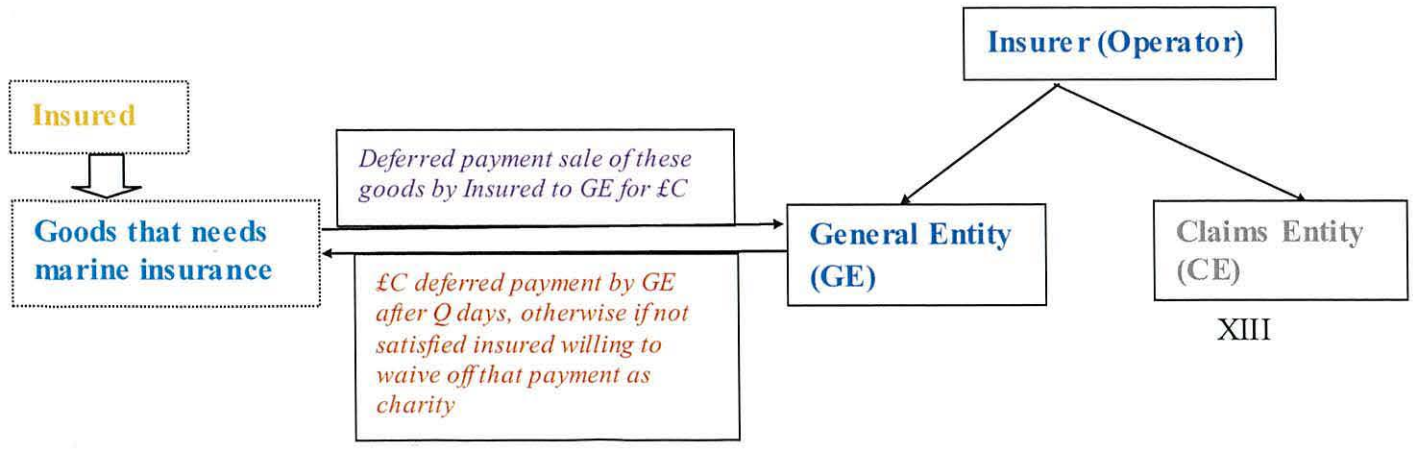
Variable used: £X rent e.g. £100, benchmarked to premium



[AND THEN]

(2) Phase 2 - *BAI MUJJAL* (Deferred Sale):

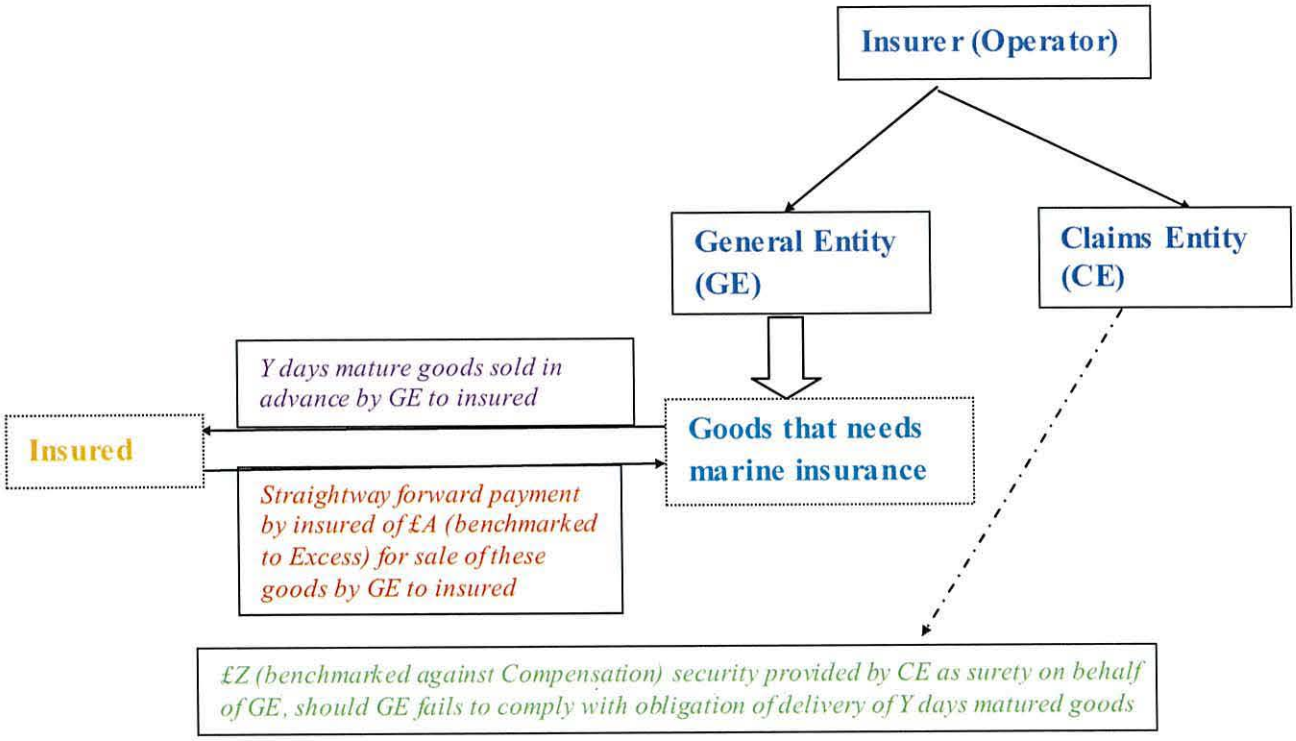
Variable used: £C deferred payment amount e.g. £200. Q days = Y days + B days e.g. 100 days = 80 days + 20 days, where Y days in the number of days of marine voyage for goods to reach destination



[AND THEN]

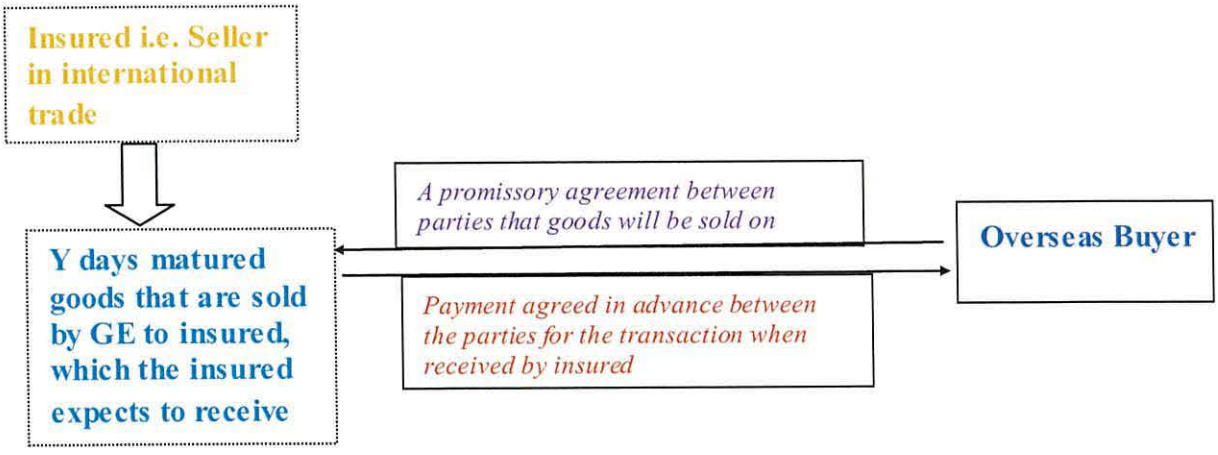
(3) Phase 3 - *BAI SALAAM* (Forward Sale):

Variable used: £A fee e.g. £200, benchmarked to excess, with care that £A and £C (from deferred payment amount has the same value). £Z security e.g. £500, benchmarked to compensation



[IN THE MEANTIME]

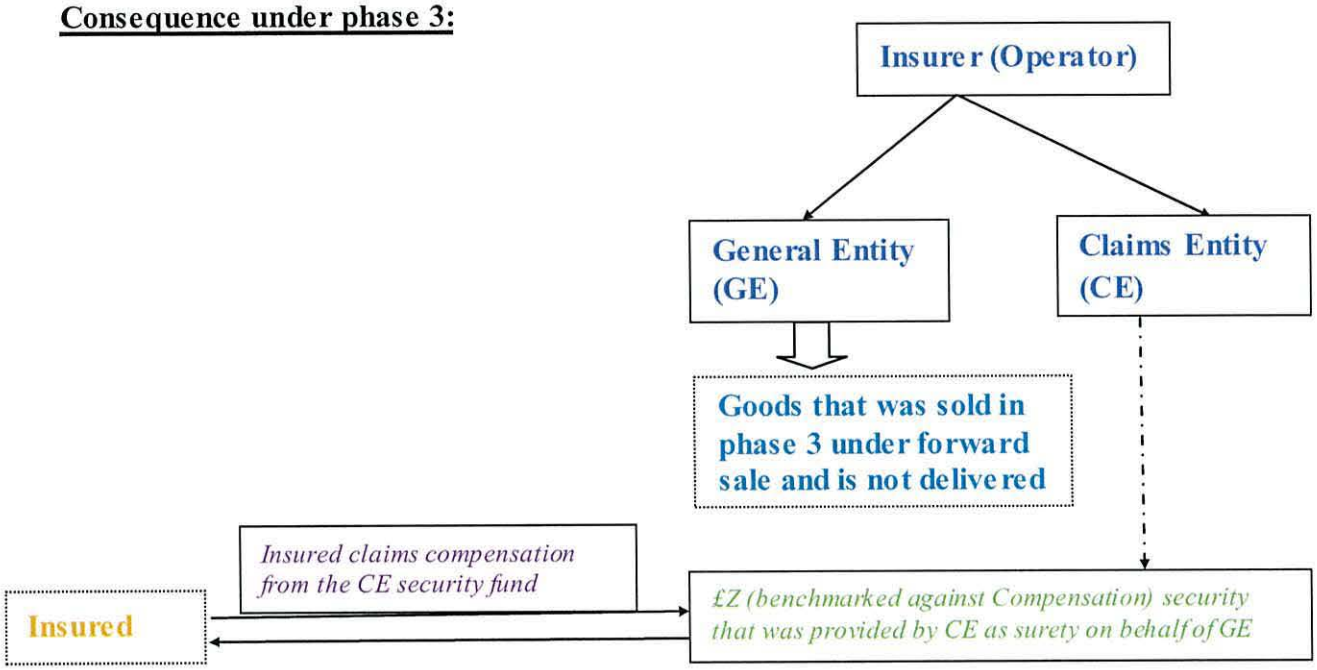
(4) Parallel *SALAAM* contract for retrospective international trading:



[AFTER THE ABOVE]

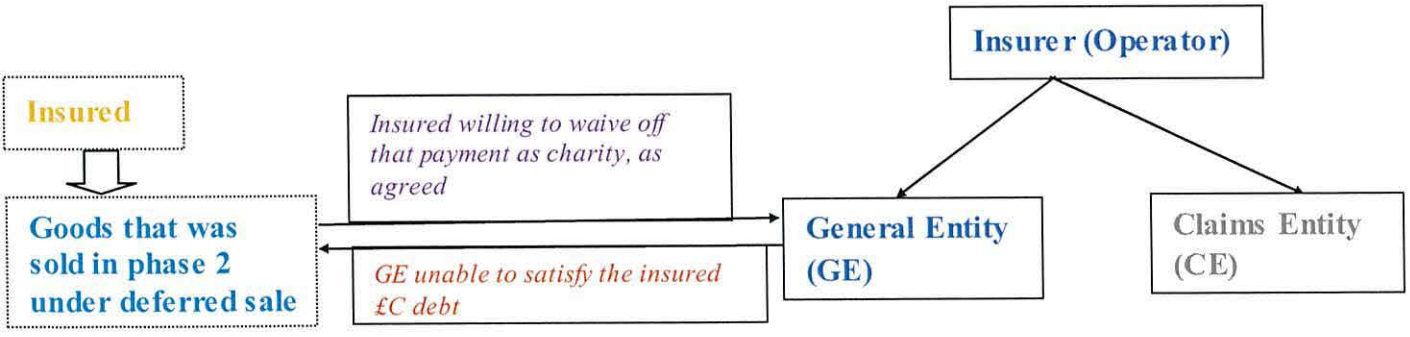
(5) (A) (I) Loss Occurs i.e. failure of GE to provide Y days mature goods to destination point:

Consequence under phase 3:



[AND THEN]

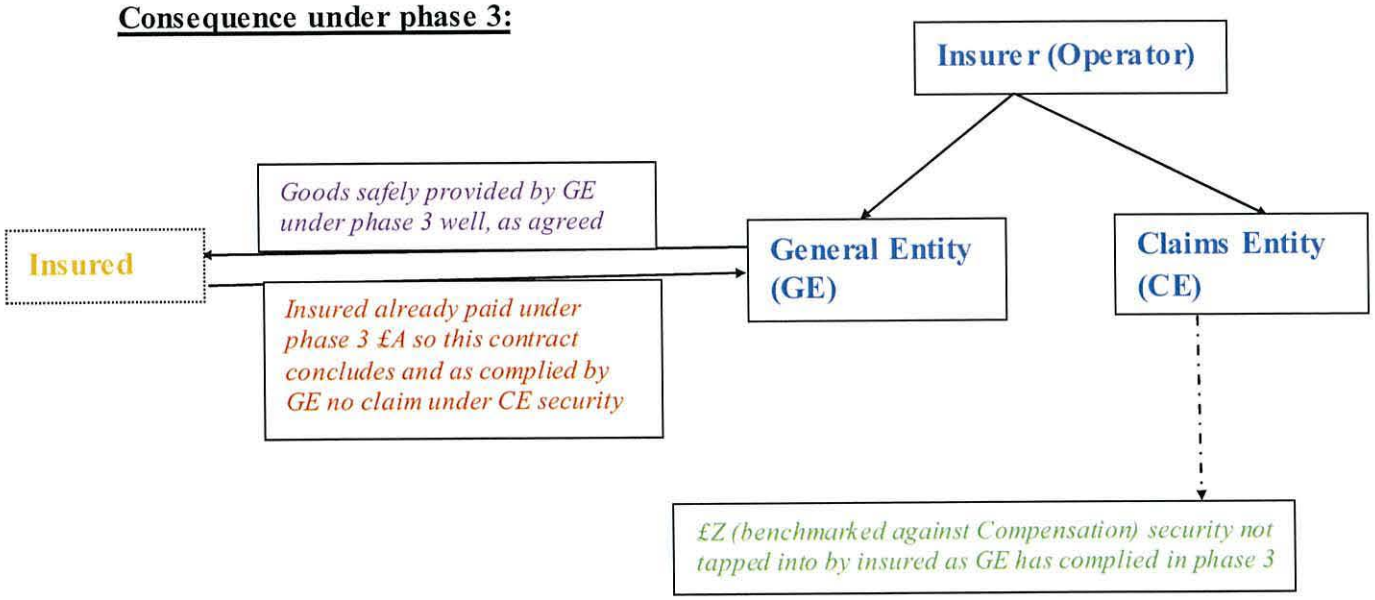
(5) (A) (II) Consequence under phase 2 (as phase 2 is longer since it has Q days i.e. Y days + B days):



[OR]

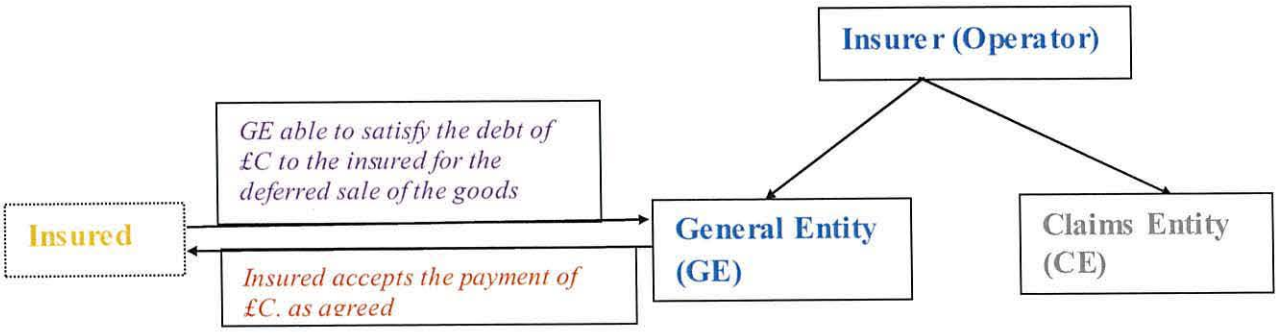
(5) (B) (I) Loss does not Occur i.e. GE able to provide Y days mature goods to destination point:

Consequence under phase 3:



[AND THEN]

(5) (B) (II) Consequence under phase 2 (as phase 2 is longer since it has Q days i.e. Y days + B days):



Part I

Outline and Context

Chapter 1: Introduction of the research

1. Title of the thesis:

"Consideration of Islamic insurance, *takaful* for development, by re-examining and analysing existent *takaful* models vis-à-vis relevant English marine insurance law."

2. Thesis statement:

This thesis proposes a new *halal* insurance model, which could be utilised instead of existent models of *takaful*, particularly from a marine insurance perspective. The thesis targets the four pillars of the insurance indemnification contract relationship; as such, it considers premium, risk, excess and compensation, which are the four sectors that define the business prerogative between the parties.

3. Introduction:

From the earliest of times, when humans conducted straightforward barter transactions, humans always had the uncertain curiosity in their mind of "what if something goes wrong?" To cover this "what if", humans needed some kind of security or assurance that they would be safe or unaffected should the worst that they feared occur. Over time, this security took various shapes and forms, such as villagers coming together to mend a broken hut of an unfortunate fellow villager, to the present position of organisations undertaking to give this kind of assurance. This concept has developed so much that such assurances have become readily available to cover anything from mobile phones to commencing litigation against another, e.g. Before the Event (BTE) insurance and After

the Event (ATE) insurance. This chapter aims to give a brief introduction to the overall research.

This research is confined to analysing the specific topics, namely premium, risk, excess and compensation, present in Islamic insurance models in relation to English marine insurance law. A marine insurance contract, unlike any other contract, is a contract between two parties, where one party (the insured/assured) pays a fixed sum (the premium) to the other party (the insurer) to cover him/her of specified marine losses, should one take place within a certain period of time on a certain voyage. The idea behind this research is to consider the three main restrictions that are present in *Sharia* law that prohibits usage of traditional insurance, namely *riba*, *gharar* and *maisir*, to analyse the existent *takaful* models and ascertain a technique to circumvent these restrictions, in order to make a new upgraded, fully complacent *halal* marine insurance model.

This research is designed to look at the above-mentioned specifics in *takaful* models from a similar viewpoint of marine insurance contracts in England and Wales. This would be done by comparing existing *takaful* models in practising jurisdictions such as Malaysia and Saudi Arabia with the current marine insurance law of England and Wales. The principal objective is to witness whether the alternative structure created under Islamic law called *takaful,* is adequate upon considering of filing the gaps present in the market; also, whether a substitute model should be used in place of the present *takaful* models and, if so, discovering that satisfactory alternative model. The ultimate aim is to propose a model of *takaful* for marine insurance that would satisfy the economic needs, both of the Islamic jurisdictions and English law, and remain well in line with the Islamic belief. It would also be consistent with the prohibition of the three main restrictions of *riba*, *gharar* and *maisir* and would satisfy the basic concepts of premium, risks, excess and compensation.

Islamic society has greatly expanded in the UK and, as a result, the need of the community has arisen for *Sharia* compliant products and services. As a result, various

Islamic financial products have been introduced in line with the well-established Islamic financial system and rules of law for the British community, e.g. Islamic banking, Islamic mortgages, Islamic investments and such others.[1] However, the Islamic insurance industry and its rules of law are still much less developed, along with the Islamic insurance alternative *takaful*, as the existent models are not sufficient to meet the requirements of this expanding society. A new model of Islamic insurance is necessary, which will not only fit the *Sharia* criteria of being *halal,* but will also work alongside the Western underlying ethos, without upsetting the same.

The present tool of *takaful* is clearly not ready to enter the insurance market in England and Wales, particularly the marine insurance market. Whilst it may give an impression of being satisfactory, as it is working well in other countries such as in Asia, the Middle East etc., nevertheless the English insurance market is a much more aggressive market that calls for a more regulated approach rather than a loose model approach, which is present in existent *takaful* models. The biggest problem with the present models of *takaful* is that the operational objectives are not very clear from their structures and this becomes a significant concern when it comes to insurance litigation consideration, e.g. which parties are carrying which title under an insurance contract, and how it must work without confusion. More importantly, it is unclear in *takaful* who is it that bears responsibilities for losses sustained from alleged torts; as a result, there are no appropriate ways of convincing applicable parties to be held accountable. This is primarily the case in *takaful* as, under strict interpretation, it is the participants' responsibility to pay when there are claims made to the *takaful* organisation. This is rather draconian, as the participants are the ones who are taking insurance to control their liability; instead, under *takaful* it would appear that they are taking on additional liabilities. There needs to be a more organised and rigid model, which should relieve this chip from the participant's shoulder and would require the *takaful* organisation to pay out. As may be the case when a valid claim is made, this will ensure that participants' rights are also adequately covered. This is necessary because, when claims are made, and being the fact that marine

[1] Islamic Bank of Britain, 'Home Purchase Plan' (islamic-bank.com) <http://www.islamic-bank.com/home-finance/home-purchase-plan/> accessed 16 November 2014

insurance claims are not small amounts in themselves, there should be some form of security for the victim. Therefore, he/she would not have to be faced with unavailability of funds for compensation or, worse, participants who enter the scheme do not have to take a bigger liability than they bargained for when initially entering the scheme.

4. Rationale of conducting this thesis:

The following thesis would concentrate on creating a working insurance model, which would pave the way for future harmonisation between Western and Islamic jurisdictions. The concentration point of this thesis is to look at and produce a *Sharia* acceptable insurance working structure, which would produce similar results as traditional insurance but from a *halal* perspective. The thesis is angled to consider from a marine insurance law perspective, as marine trade insurance sets the foremost principles of insurance law in England and Wales and also in the Islamic field. The aim is to make a tolerable insurance working model that would both satisfy the strict *Sharia* regulations and, at the same time, be adopted in Western jurisdiction, primarily English law, without changing the basic fundamentals of the longstanding nature of English marine insurance law. This research would mainly be a black letter interpretation of the reasons for the unacceptability of traditional insurance in Islam, along with a consideration of the present models of Islamic insurance, e.g. *takaful* that are existent with the aspiration for advancement in the context of *Sharia* law.

It is, of course, without doubt that one may want to know the reason for considering this particular topic for research purposes, given various major extreme issues of such concepts. The simple response to this query is that, these two concepts at the moment are in two opposite points, and the idea is to pave the way for harmonisation of these two jurisdictions to assist with the aid of advancement, possibly for both of them. Muslims view traditional insurance negatively and the present Islamic insurance models are considered as unambitious by Western society. With the aim of non-Muslims and Muslims to work together for advancement of commerce particularly in international trade where marine insurance is mandatory and crucial, not least for peace of mind as

numerous unexpected perils are faced on the marine voyage, it is a necessity to look into the matter deeply. This portrays rather a compulsory obligation on both sides to find a common purpose and grounds so that they can work together.

In this thesis, the scope of exploration for the discovery of a new *takaful* model would be strictly viewed from four pillars of insurance, namely premium, risks, excess and compensation. It is opined that these four concepts form the basis of any suitable standing insurance model and, hence, it is of relevance to consider these to prepare a concrete foundation. Insurance models are structured on two principal paradigms, namely contractual obligations and tortious liabilities. The contractual obligation is the relationship between the insured and the insurer, whilst the tortious liability is the relationship between the tortfeasor and the insurer; the former is generally the insured, being the rogue in the picture, leaving the insurer to handle the consequential losses of the defined tort that occurs to a third party.

With this in mind, the concept of premium governs with the contractual obligations, as it is the premium payment that sets the ball rolling, in respect of the insurance liaison, in the first place. The concept of risk falls within the parameters of both contractual obligations and tortious liabilities, as the relationship is a contract for the insurer to handle the consequences of the defined risks on behalf of the insured; at the same time, the consequences are tortious in nature, hence touching on the second paradigm. The concept of excess is said to fall within the ambit of a contractual relationship. Excess is the payment that the insured has to pay to the insurer to deal with the claim, without which the insurer would simply not get involved at all; hence, it is a contractual obligation between the parties of this payment. The last part is the concept of compensation, which falls within the boundary of tortious liabilities; this issue becomes relevant only when a defined tort has taken place.

For a long time, Muslims had been in a dilemma over traditional insurance and viewed it as something inappropriate, partly because of the attitude of traditional Western insurance companies in doing their business and partly because of a lack of knowledge in itself.

Mostly, however, it is due to the fact that it has been concluded amongst the Muslim community that such traditional insurance practices break Islamic beliefs and laws. This leads to a subsequent interdiction among the Muslim community on the consideration and usage of traditional insurance, except in dire mandatory circumstances when the requirements of necessity allow a very narrow exception for Muslims to have to purchase the same. This, mainly, is the circumstance when taking insurance, as it is obligatory under jurisdictional law, such as motor insurance, employer's insurance or marine insurance.[2]

The Muslim community has become aware of its drawbacks in its need to keep up with the advancement of Western society. Therefore, the Islamic society introduced an alternative to traditional insurance, which is called *takaful*. *Takaful* means cooperativeness and mutuality, and the functioning is similar to mutual insurance as practised in Western community. *Takaful* is an idea rather than a product in itself, just as the concept of insurance is a notion for safeguarding and security in uncertain circumstances. Over the years, *takaful* ideology has been altered into a number of working models to create products, but all of those models hold firm the concept of cooperativeness at all ~~the~~ times. For better or worse, these *takaful* models are now being practised in a number of countries; although they have various issues, these are the only models available at the moment for the Muslim community and, as such, have to be utilised, with reluctance.

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[2] This is the case with various English insurance requirements in England and Wales e.g. vehicle insurance is compulsory for every driver of the vehicle as mentioned in s. 143 of the Road Traffic Act 1988, "Compulsory insurance or security against third-party risks", even though policies are sold by traditional insurance companies which breaks numerous *Sharia* laws.
The same goes with employers liability insurance which is compulsory for every employer under s. 1 of the Employers Liability (Compulsory Insurance) Act 1969, "Insurance against liability for employees", even though once more these traditional insurance companies are in breach of various *Sharia* restrictions. There is a *Sharia* requirement called *darura* that is translated as the law of necessity in Islam. This has been mentioned a number of times in the Holy Quran and *hadiths* mostly referring to circumstances of consuming of foods that generally would not be considered to be Sharia approved but only allowed in extreme necessity circumstances. For the sake of completion, one of the verses of the Holy Quran in *Surah Al-Baqarah* (Chapter 2), Verse 173, it is mentioned that:
"*He has only forbidden to you dead animals, blood, the flesh of swine, and that which has been dedicated to other than Allah. But whoever is forced [by necessity], neither desiring [it] nor transgressing [its limit], there is no sin upon him. Indeed, Allah is Forgiving and Merciful.*"
Holy Quran, '*Surah Al-Baqarah*' Chapter 2 Verse 173 (quran.com) <http://quran.com/> accessed on 14 November 2013

The various *takaful* models have a number of concerns that will be discussed in more detail in the later chapters in this thesis. Particularly, given the intricate structures of different *takaful* models, it is necessary to peruse the later chapters delicately to understand the problems in detail. However, as a summary, all the existing *takaful* models refer to the concept of cooperativeness and mutuality, yet it is not something that is actually strictly followed in the operations of those *takaful* models. Rather, the models appear to have been created simply to benefit the *takaful* operator, e.g. the organisation similar to the insurer, who is running the *takaful* operation, with the aim of running the trade under the veil of being *Sharia* compliant. This is because *takaful* models have been designed to avoid various *Sharia* restrictions, which in itself is not incorrect, but the difficulty appears when the various elements in the process become inharmonious with each other. For instance, in all existent *takaful* models, the premium payment is considered as *tabarru* payment, e.g. charity payment so as to alleviate various *Sharia* restrictions.[3] Yet, in all the present *takaful* models, the *takaful* operator fails to follow the necessary *Sharia* principles of *tabarru;* instead, the *tabarru* is used as an investment sum to make returns for the benefit of the donor of the *tabarru* using Islamic investment tools. The outcome can be stated to be at best a "*quasi-Islamic*" product; however, under Islamic law, something is not considered *halal* unless full *Sharia* compliance has taken place.

Another problem with the existent *takaful* operation is that the internal mechanics vary from model to model, as such lacking consistency with the initial intentions and promises of the parties to that of the concluding intentions and promises of the parties. In a democratic society, irrespective of whether jurisdictional laws such as English law are applicable or whether *Sharia* law are applicable, it is vital that parties entering into a contract have precise and accurate reflection and intention in order to see the expected outcome. Whilst modification along the process of contractual obligation might be

[3] Three principal restrictions namely *riba*, *gharar* and *maisir* plays a significant role which stops from allowing traditional insurance being acceptable under Islamic law and as acceptable by Muslim community. See chapters 3 and 4 below where these restrictions are discussed in even more details and their relationship to marine insurance particularly, as channelled in this thesis

honoured under the freedom of contract of the parties, provided it is within the ambit of of the law, ambiguous objectives serve a purpose to no party. Unfortunately, such matters appear to have been compromised in the operation of existent *takaful* models.[4]

Alongside the above, one of the main concerns with all of the existent *takaful* models is that the insured or participant, as they are referred in a *takaful* operation, since it is deliberated as a mutual scheme, bear personal liability for the liabilities of the *takaful* operation when the expenses outweigh the revenue. Although different models have in operation a discretionary safety valve for such circumstances, with the *takaful* operator providing a *quad hasan,* i.e. gratuitous loan to cover the deficits, these *quad hasan* payments are not obligatory under *Sharia* principles or under different jurisdictional laws. This leaves the participants with more to cope with than what they initially anticipated, even before entering the *takaful* contract. This is felt to be in itself a call on the risk of uncertainty, which is one of the *Sharia* restrictions, to be applicable in *takaful* operations.[5] As it would become quite prevalent in this thesis, as progressed along the various chapters, it is unfortunate that the *takaful* operator is portrayed as savouring the delights from both ends, by taking on the premiums and, at the same time, avoiding responsibilities. The *takaful* concept is certainly a noble idea but, as opined above, the operational side of it had not been appropriately designed as such, leaving a huge void of dissatisfaction. In addition to the several problems associated with the existent *takaful* models, there is the added issue of models being overly complicated, which restricts the flexibility of working alongside Western traditional insurance. This will be witnessed in later chapters of the thesis. It is perceived that, in modern times, complications can be an acceptable norm, provided flexibility when working alongside existing ideology can be

[4] The various issues with the different types of *takaful* models are discussed in details in later chapters. See below Chapters 6 and 7 for understanding the ideology behind *takaful* and the present *takaful* models with their shortcomings.

[5] The researcher opines that this in itself should be considered as falling under the *Sharia* restrictions of *gharar* and *maisir* as the participants would face uncertainty with their obligations amount at the end of financial year which the parties are simply unaware how much will be at the time of entering the contract. It is simply impossible for the *takaful* operator to state what the total obligation amount the participant will face at the end of financial year as the *takaful* operator is always taking on new participants to fill in the *takaful* pot as big as possible, with the same analogy as the traditional insurance companies that the risk is more spread with more participant numbers.

appointed. It is felt that a complication without flexibility is simply a dead end road as far as commercial advancement is concerned.

For the purpose of this thesis, consideration would be made of the *takaful* models that are in use in different Muslim countries such as Malaysia and Saudi Arabia, with emphasis on the religious law, i.e. *Sharia* principles as set out in the Holy *Quran* and the practices of the Prophet Mohammad (pbuh), which are the primary sources in this respect. It is important for readers to note that, on consideration of Islamic law, it is not the jurisdictions of various countries that exercise Islamic law that take priority. Rather, the roots of those jurisdictional laws are extracted from the primary sources mentioned above, and it is those that take precedence. Consideration is made in terms of English and Welsh insurance law, as English law was a pioneer in international trade. Reference is made at times mainly to English marine insurance law; this is because the whole concept of English insurance law finds its origin starting from marine insurance, and then branched out into various other insurances over time.

More importantly, the English jurisdiction has been considered rather than other jurisdictions such as India, China, Iraq or Iran; this is because English law is based on a common law that allows flexibility for adoption and moulding, unlike other jurisdictions, which are too rigid. This thesis aims to propose a new *halal takaful* model which, if implemented, can adopt within recognised jurisdictions such as English law. Additionally, as the British Empire ruled a number of countries up to the late seventeenth century, the legal systems of many of these countries had been built on English law, including marine insurance, which dates back to the early sixteenth century; these foundations are still concrete to date. It is best to index English law as the centre of the analysis, because it is accepted and followed by numerous jurisdictions throughout the world.

Moreover, the idea behind the screen for considering this thesis and proposing a model is to use it in practice rather than just being on the bookshelf piling up dust. The UK conducts a significant amount of commerce with a number of Islamic countries, given the

multicultural prospect of the UK. Most of the international trade, particularly oil and fuel trade, occurs between Middle Eastern countries and the UK, which calls into play the need for an integrated code of marine insurance. Also, according to a recent report of the Organisation of Islamic Cooperation (OIC), it has been concluded that the UK attained fourth place, and Ireland first place, in their practices of social life including governance, political, human rights and international relations, which are in compliance with *Sharia* principles.[6] This goes on to demonstrate that the *Sharia* aspects already exist within the British community, making it more appealing to consider with English law. Therefore, comparing the underlying concepts with English law in the background would be the best way forward for the advancement both in theory and practice.

Finally, the researcher of this thesis graduated from UK, did his Masters in International Trade law in the UK and studied for his Bar Vocational Course from the UK, emphasising at all times the laws of England and Wales. Also, the researcher had been working in civil litigation and the insurance sector for a prolonged period of time. In his present position as a Senior Partner,[7] he has gained knowledge and experience of insurance litigation, which is a crucial aspect for the creation of any realistic proposal for the development of this arena.[8]

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[6] Paul Hosford, 'Ireland is more faithful to the Qu'aran than Saudi Arabia' (2014) thejournal.ie <http://www.thejournal.ie/ireland-is-more-faithful-to-the-koran-than-saudi-arabia-1507583-Jun2014/>; BBC, 'Islamic compliance report video' (bbc.co.uk) <http://www.bbc.co.uk/programmes/p020c0sq> assessed 14 August 2014
In fact the report found that Malaysia ranked at 33, Saudi Arabia ranked at 93 and Qatar ranked at 111 with *Sharia* conformity within their society. This no doubt may raise some eyebrows among readers on the conformity of Islamic law in Islamic countries in comparison with western counties.

[7] Currently Senior Partner at Kawa, Guimaraes & Associates Solicitors

[8] The researcher feels it is necessary to emphasis on the practical experience as during his experience he has a noted a lot of times issues crop up which are perhaps not paid much heed in textbook. Given the topic of the thesis being insurance, it is pertinent that insurance involves extensive litigation. Whilst writing this thesis, the researcher aims to idealise that any proposed models would need to face the guillotine of litigation where matters which may have been considered insignificant at preliminary stages becomes extremely crucial in determining the outcome of litigation. Hence the researcher objective is to propose a model that would survive judicial scrutiny both from English insurance law view and from *Sharia* point of view.

5. Research Questions:

1. How can Islamic conformity, i.e. *Sharia* compliance, be incorporated into English insurance, particularly in the context of marine insurance in consideration of premium, risk, excess and compensation, without changing the working demographic of English marine insurance?

2. Is the present Islamic insurance alternative, i.e. *takaful*, something that can be considered viable or suitable for the English marine insurance market in its present form? If not, then what are the problems and missing components that hinder it from achieving the same, and how best can it be resolved in consideration of premium, risk, excess and compensation?

3. Aside from question 2 above, of whether *takaful* can enter the English marine insurance market, what are the expectations of *takaful* in adapting to the current English marine insurance working structure without disturbing much of the latter's nature and the available scope for the upgrading of the *takaful* model to make it Western-friendly?

6. Aims and Objectives of this thesis:

For a long time, Muslims have been looking for an alternative instrument to traditional insurance, something that would carry out similar responsibilities and, at the same time, preserve their Islamic faith. *Takaful* has been created and is clearly making its mark on the global insurance market. However, the important question is whether *takaful is* living up to expectations. In fact, a more specific query arises, namely what are the exact expectations of the legal and finance markets in respect of *takaful*? Also, are such expectations truly achievable by *takaful* and are they consistent with settled jurisdictional law, such as English marine insurance law and the Islamic principles at the same time?

The main analogy of this research is to consider the concept of *takaful* and its effectiveness at present, along with the idea for progression, by looking into the core

elements necessary for it to work contractually, namely premium, risks, excess and compensation. Whilst *takaful* is a new creation, it requires advancement mainly in the construction of an appropriate model, but keeping in mind the restrictions of *riba*, *gharar* and *maisir*. Accordingly to Professor Frank Vogel, Islamic finance structuring is conducted from two angles: one is an application from the Islamic point, with the aim of organising within Islamic law remits; the second is for the advancement of Islamic economics, where the idea is the organisation of the Islamic instrument to outmanoeuvre the Western counterpart, with better results and pertaining to moral principles.[9] At present, *takaful* models, as readers would note during the perusal of the thesis, are unlikely to have fulfilled either of these aims.[10]

As a comparative examination, for the advancement and development of *takaful*, English marine insurance law has mainly been considered for the reasons stated earlier. This is, in fact, a perfect opportunity to conduct this research with the ultimate aim of advancing *takaful* with a new innovative model, which will perhaps bring it one significant step closer to the functioning platform of the English marine insurance law. This would be beneficial, not only to Islamic jurisdictions but to non-Muslims as well, in international trading. To categorise, the main aim of the study is to propose a new model for *takaful,* which satisfies the Islamic rules but does not deviate from the nature of traditional insurance. The aim will be achieved by carrying out the following:

1. Analyse the concept of *takaful* and its present situation in relation to the three major hurdles of *riba*, *gharar* and *maisir* and, as such, consider to an extent the three hurdles themselves.

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[9] Hania Masud, '*Takaful*: An innovative approach to insurance and Islamic finance' (2010-2011) 32 U. Pa. J. Int'l L. 1135 – 1136. Professor Frank Vogel was a former Professor at Harvard Law School and a leading expert on Islamic Law.

[10] The researcher opines that neither the first requirement of being adored to Islamic law has been satisfied as the researcher argues in later chapters that various existent *takaful* models in themselves are in breach and clash with different *Sharia* elements. The second requirement of being better than counterpart of traditional insurance is also not satisfied such as in *takaful* the participant/insured bear personal responsibilities for claims (unlike in traditional insurance where insurance company bears the responsibilities), as been mentioned later on in the thesis. Such liability outweighs any benefit that insured may derive in comparison to traditional insurance.

2. Critically analyse the various *takaful* models that are utilised at present and their significant lacking; in particular, to evaluate whether cooperativeness in its present context is actually the way forward by dissecting the various models.

3. Compare *takaful* with traditional marine insurance law in England and Wales by looking into the concepts which gives essence to insurance models, namely premium, risks, excess and compensation.

4. Consider the advancement and development of *takaful* and its expansion in the current Western insurance market, by consideration of relevant Islamic financial instruments that are not presently analysed for *takaful*.

5. Propose a construction of a new upgraded model of *takaful* rather than the ones presently in existence to assist with advancement, keeping in line with prevalent concepts in traditional marine insurance of England and Wales, namely premium, risks, excess and compensation.

6. Whilst proposing the new model for *takaful*, the aim is to lay the foundation for future bridging between *takaful* and English marine insurance law, by the improvement of *takaful,* namely in the important concepts of premium, risks, excess and compensation.

7. Methodology of this thesis:

As mentioned above, the crux of this research would be to extensively consider Islamic views on insurance and on the development of the current *takaful*, by proposing a new model with the use of new relevant *halal* instruments. This would be done with reference to the English marine insurance law from time to time, in the background. The focus would be on further development of *takaful* contract construction by looking into the notions of premium, risks, excess and compensation, which builds the insurance framework, but reserving within the three Islamic main restrictions of *riba*, *gharar* and

maisir. The notion is to examine the perception of Islamic law regarding *takaful* and to remain as close as possible to current ideologies, at the same time allowing enough flexibility for the development and advancement of *takaful* by the introduction of a new model. In the same vein, any proposed model would automatically assist in creating a connection between English and Islamic jurisdictions by bringing them closer to the proposed *takaful* model.

The research would look critically and analytically at the various *takaful* models that are presently in use. This divided the research into a number of chapters for the examination of the different concepts, initially to give some background on the restrictions causing traditional insurance to be unacceptable in Islam, to the *takaful* models prevalent at present, up to the proposal of a *takaful* model in line with the important concepts of traditional insurance, namely premium, risks, excess and compensation. The research would shed light onto both qualitative and quantitative methods for this work, but would emphasise the former as there are more hard data involved rather than just numbers to work with. Therefore, the research would be primarily library-based with a consideration and dissection of the relevant literatures to establish the necessary facts; as such, a black letter law approach would be taken. Each chapter would aim to conclude with a paragraph of the researcher's own opinion, building up the scenario of the proposed *takaful* model; however, throughout the chapters, independent points would be set out as well.

The research would consider by looking at textbooks, articles, journals, magazines and such other periodicals, dealing with *takaful* and English marine insurance law as required. This approach would allow for the consideration of various comments and assertions of academics and scholars from such commentaries. The research would look into the primary sources of information and draw relevant illustrations, which will allow the expression of a bigger picture on the vitality of the proposed recommendations for establishing a strong *takaful* model. Also, it would consider speeches and views expressed and shared on various seminars and discussions on the research topic. Islamic scholarly opinions, which are expressed from time to time, would be taken into

consideration, as well as secondary points. As an advantage, the researcher has the privilege of knowing the practical scenario from the insurer and insured's viewpoint, as a result of various employment experiences within law firms in England. Opinions, views and relevant precedents would be drawn from this aspect and would assist in the development of a proposed *takaful* model.[11] The ultimate aim is to provide recommendations in the comparative analysis of Islamic principles with English law within the aspects of premium, risks, excess and compensation, for the advancement of *takaful*. This ideally would set the basis for both England and Wales and Islamic jurisdictions to work closer together in the marine insurance sector. Consideration would be given to various precedents that exist at present as the need arises in the thesis. The current *takaful* needs an approach from a modern practical point in the changing economic climate rather than the current overly restrictive approach for future and further development.

8. Outline of the research chapters:

This research thesis has been divided, primarily, into four parts containing a total of nine separate chapters. The first part consists of Chapter One and Chapter Two, with the first chapter providing a brief introduction and overview of the current Islamic law position of *takaful*. This chapter will give a general overview of the topic and assist in understanding what this thesis would be looking into, by focusing on the state of insurance under Islamic law in line with traditional insurance. The objective of this chapter is, quite simply, to establish the idea of insurance in human life and how it has been considered under the *Sharia* light of *takaful* of living up to the intended expectations. It introduces the three draconian restrictions of *riba*, *gharar* and *maisir*, which obstruct the validity of traditional insurance, and shows how the present *takaful* model, despite all efforts, is still falling short of the required targets.

[11] The researcher would draw practical knowledge from his employments with various law firms and working at the Insurance departments. The researcher has the advantage of being involved in litigation of numerous insurance cases where he witnessed insurance companies' relentless approach to deny responsibilities for indemnification when casualty occurs to the Insured.

Chapter Two, which falls under the ambit of Part I of the project, discusses the background of the thesis by taking on comparative variables under traditional insurance law and *takaful*. This chapter compares the few common concepts, namely utmost good faith, warranties and contract construction, to demonstrate that the aims of both are the same, e.g. for the safeguard of the participant/insured by providing cover. However, the chapter goes on further to focus on the point of contract construction that is in disparity. It goes on to expose the chaotic condition of contract construction of *takaful* models and pinpoints the elements of premium, risks, excess and compensation that need to be considered for the advancement of *takaful*, describing the need for a new model with the aid of an overview table. The idea is not to indulge deeply into any of the aspects, as the topics are quite complex and would be misinterpreted by unfamiliar readers of Islamic finance; hence, the later chapters go on to discuss in a step-by-step manner. These two chapters, being introductory in nature, aim to provide somewhat early information before delving into the substantive chapters.

The third and fourth chapters form Part II of the thesis, which deal with various restrictions that hinder traditional Western insurance from being acceptable to Islamic society. The third chapter deals with the restriction of *riba,* i.e. usury where someone benefits from and obtains something without doing anything in return. A type of usury is the interest that is either charged by various financial institutions or, conversely, is provided by the same to their customers. Such type of transactions, where one benefits without actually doing anything in return, is not acceptable under Islamic law. This position is reflected in insurance law, as such condemning traditional marine insurance unacceptable, due to the difference in amount between the premium sum and the compensation sum. In this chapter, *riba* is analysed from a religious perspective and its implications on insurance law.

The fourth chapter deals with the restriction of *gharar,* i.e. uncertainty and *maisir,* i.e. game of chances, respectively in business contracts, where it is uncertain of the parties' obligations at the end of the transaction. Specifically, such transactions are unacceptable under Islamic law, which constitutes the second restriction of *gharar*. A type of *gharar*

transaction as an example could be where someone tries to sell to another a whole tree of fruits on a certain date, but neither has any idea of the time of contract, whether the tree will have fruits and, if so, how many fruits will be in that tree on that date of contract, all of which would fall under the remits of *gharar*. This is because the parties are unaware of their obligations under the contract; also, from a moral perspective, there is the possibility it could turn out to be an unfair deal for one of the parties, as it is unascertainable on the subject of sale, i.e. the fruits in the tree. In this chapter, analysis is made about *gharar* and conditions pertaining for the existence of *gharar*. A *gharar* relationship in traditional insurance law is adduced with references made to the religious law and the practices in Western society that are already in place to minimise *gharar*.

The same chapter then discusses the idea of betting in situations, when there is a contract where the outcome is determined by probability, such as in a game of chances rather than determined business risks, such are considered to fall within the domain of *maisir*. A type of *maisir* as an example could be in transactions of gambling, lottery and betting, where the customer paying the fee for entering his stake has no idea what the outcome could be. Whilst various odds are calculated according to the rules of statistics, no one can state or guarantee that each party will ultimately have the outcome in his/her favour. In such circumstances, where the outcome is chance factor rather than certain, these kinds of transactions are not allowed under Islamic law. This chapter goes on to discuss *maisir* from a religious law perspective and its relationship with traditional marine insurance law.

The fifth, sixth and seventh chapters fall under Part III of this thesis, where these chapters primarily deal extensively with explaining *takaful*, it's present position and mention a number of Islamic financial instruments, which become relevant and can be used in understanding the proposed model. The fifth chapter deals with understanding *takaful* in detail by dealing with its background, comparing it with traditional insurance, explaining various different types of opinions, including independent own opinions and discussing the future of *takaful*. This chapter particularises the ideology behind the creation of *takaful* and the structure of *takaful* in general. During the course of this chapter, an

extensive review of literature takes place; opinion analysis of various Islamic intellects on the viability of *takaful* are considered, including various own views during the course of this chapter. As would be noted during the perusal of this chapter, intellects are split on this matter and desperation can be witnessed for the need of a suitable *takaful* model that will serve the insurance objective in a *halal* manner, without transgressing Islamic law. This chapter looks into how best this could be achieved.

The sixth chapter will deal with the various models of *takaful* that are practised at present. To explain the different types of models, background information of different Islamic financial instruments that are utilised for present *takaful* models will be provided with religious laws. As will have been noted from above, discussion will be made on the concept of *mudarabah*, which is an investor & entrepreneur instrument that is utilised to create a *mudarabah*-based *takaful* model. Discussion would be made on the concept of *wakala*, which is a principal & agent instrument that is used to create a *wakala* based *takaful* model. Also, discussion would be made on the concept of *waqf*, which is an endowment instrument that is mixed with *mudarabah* and *wakala* to make ~~to~~ various hybrid *takaful* models. A hybrid *takaful* model of *mudarabah* and *wakala* alone would also be discussed. Importantly, this chapter would focus on explaining, in detail, both in text and pictorial fashion, the various models and elicit the various problems of each of the *takaful* models. Whilst considering this chapter, it will be noted that the concerns and issues are not only major in nature, which outweigh the benefits, but threaten the bare underlying fabric of *takaful* notion and its existence. This chapter goes into the account of the concentrated attempt, to find a suitable *takaful* model that will meet just the right balance with a core contract of premium, risks, excess and compensation, keeping in line with *Sharia* principles.

In the seventh chapter, discussions are made in detail of different types of Islamic financial instruments, namely *Ijarah*, *Bai Salaam* and *Bai Mujjal* along with necessary religious laws that are present in Islamic law, but not considered for *takaful* models. These discussions of the various *Sharia* instruments are relevant because of their bearing in the proposed *takaful* model. The proposed *takaful* model is formed with the

components of these various *halal* instruments, which form the nuts and bolts and, without understanding their respective algorithms, the proposed *takaful* model would be hindered from being explored well. The instrument of *Ijarah* is of two types, namely labour-based *ijarah,* which relates to wage payments made in return for labour/service, and lease-based *ijarah,* which relates to rent payments in return for asset lease. The instrument of *Bai Salaam* relates to a forward payment sale contract when payment is provided immediately and goods are provided at a later date. The instrument of *Bai Mujjal* relates to a deferred payment sale contract when goods are provided immediately and payment is provided later. The discussions made on these various instruments are relevant in the thesis for the modelling of the proposed *takaful* model. The proposed *takaful* model fuses together these various instruments to comply with the core elements of the insurance contract construction skeleton, namely premium, risks, excess and compensation. In this chapter, the final base is put forward before heading to the next chapter that deals wholly with the proposed *takaful* model.

Subsequently, Part IV of this thesis contains Chapter Eight and Nine and deals with the final part of this paper. Chapter Eight introduces the proposed *takaful* model, which deals with the elements of premium, risks, excess and compensation of marine insurance in a *halal* manner. The new proposed *takaful* model is called the "*X3-I.M.S. fusion*" *takaful* model. This chapter pulls down the curtains fully to witness how the proposed *takaful* model is going to work, both textually and illustratively. The proposed *takaful* model is a fused concept of three different instruments presented in the previous chapters, namely *Ijarah*, *Bai Mujjal* and *Bai Salaam.* These are carefully fused together for the fulfilment of elements of premium, risks, excess and compensation for the formation of a *halal* insurance model. However, even though the concepts are fused, it is made clear at all times that three separate independent contracts are in operation. Moreover, the chapter talks in detail of the operational manner of the proposed model and makes it clear that, in this proposed *takaful* model, there is no need to veil concepts from their true nature, as is currently the case in present day *takaful* models.

Furthermore, the chapter examines the proposed *takaful* model that consists of three distinct phases, which are working on one platform to create the "*X3-I.M.S. fusion*" *takaful* model. Under phase 1, the premium payment would be dealt with under an *ijarah* contract between the insured and insurer. There is a distinction made between the *ijarah* type used, where the choice is between labour-based *ijarah or* lease-based *ijarah.* When labour-based *ijarah* is used, then the premium payment is a payment by the insured for the risk management service of the insurer. Where lease-based *ijarah* is used, then the marine voyage goods would be leased to the insurer but restricted to negative enjoyment only, causing rent payment by the insured. Under phase 2, the goods to go on a marine voyage would be sold by the insured under a *Bai Mujjal* contract to the insurer, for which the payment date is fixed later on, after which the insured would agree to waive off payment as charity.

Under phase 3, the specific voyage days, matured goods would be sold by the insurer to the insured under *Bai Salaam* and the contract and payment would be received up front, which forms an excess payment. The risk of nonfulfillment by the insurer is securitised under a compensation payment. If, under phase 3, specific voyage days matured goods are compiled, then the excess payment is returned; as under phase 2 payments, this would have the same figure as the excess payment. If phase 3 is not complied with, then the insured's claims under the security provided for the compensation and any payment due under phase 2 are waived off, as agreed in advance. Risks remains with the insured at all times, as under traditional marine insurance, but when risks turn adverse, the insured has an avenue of claiming for the loss sustained. This chapter also critically examines the proposed *takaful* model to show how the proposed *takaful* model can be used to balance both the *Sharia* rulings and English marine insurance requirements with each of the four concepts of premium, risks, excess and compensation.

Finally, Chapter Nine of this thesis is a concluding chapter, which highlights in general the advantages of the proposed *takaful* model, but also expresses the limitations of the proposed *takaful* model. This chapter concludes by summing up all the work of this thesis, primarily dealing with the present *takaful* ethos and how the proposed model

would aim to resolve the existent problems. Additionally, this chapter would also hint at further recommendations and future work that could not be concluded in this thesis, due to time and word constraints.

Part I

Outline and Context

Chapter 2: Background of the research

1. Introduction:

This chapter aims to look at the background by considering some of the basic principles of traditional insurance as a comparative analysis to that existing in *takaful*. Given that this thesis would be analysing different *Sharia* concepts in proposing a new *halal takaful* model, which would need to work alongside English marine insurance, it would be helpful to give some background information on Islamic law and on English marine insurance.

It is believed that it would assist to demonstrate that a few topics of traditional marine insurance, namely utmost good faith, warranties and contract constructions and *takaful,* are not dissimilar in their principal ideologies. Hence, they are on the same rhythm in regards to the main aspects, but differ from an operational perspective.[12] However, it should be noted that the idea of this thesis is to aid the advancement of that operational aspect of *takaful* within the pillars of premium, risk, excess and compensation that are in line with traditional marine insurance.

1.1. Islamic Law:

[12] It is necessary to note that this thesis aims to show that *takaful* whilst in theory the ideas and wavelength may be the same in certain concepts however *takaful* has significant amount of structural flaws which needs amending and upgrading so as to have any chance of entering and expanding in the western community. These common concepts should not be taken that *takaful* and traditional insurance particularly marine insurance are at the same beat and this thesis would go on to argue why not and what can be modeled to have an increased chances of doing the same.
Muhammad Anwar, 'Comparative Study of Insurance and *Takafol* (Islamic Insurance)' (1994), 33:4 Part II The Pakistan Development Review, in the Textbook: M. Kabir Hassan and Mervyn K. Lewis (eds), *Islamic Finance* (Edward Elgar Publishing), 1315 – 1330, p. – 430

It is felt, for a better understanding of Islamic law, that it would assist greatly to give some background information on the basis of Islamic law, the core of which are the *Sharia* principles. *Sharia* is an Arabic word meaning "*the way to a watering place*" or the path to follow, which is shown by Allah (SWT), the Arabic word for God through His Messenger, Prophet Mohammed (pbuh).[13] For Muslims, their primary aim is to lead their life in compliance with the rules of God, Allah (SWT) as set in their Holy Book, the *Quran* along with consideration of the teachings and lifestyle of their prophet, Prophet Mohammed (pbuh) as mentioned in various *hadiths*. There are four different *hadiths* that are well-known, which are *Sahih Al-Bukhari*, *Sahih Muslim*, *Sunan Anu-Dawud* and *Malik's Muwatta*. Additionally, the majority of Muslims in this world are Sunni and, for them, there are four prominent schools of jurisprudence namely *Hanafi*, *Maliki*, *Hanbali* and *Sha'afi*, who interpret Islamic laws differently.[14]

It is crucial to note that only Allah (SWT) is the Lawgiver and the whole of Muslim society, which is considered as one community irrespective of nationality and ethnicity i.e. *Ummah*, are simply His trustees, who follow His ordinances. The sovereignty belongs to Allah (SWT) alone and any rule in the law made by humans must not conflict with Allah (SWT) laws, as His laws take precedence at all times. This is actually specified very nicely in *Surah Al Kahf* (Chapter 18), Verse 26, which dealt with an incident of a group of youths hiding in a cave to avoid getting involved in worshipping anyone/anything other than Allah (SWT). It is mentioned:

- *"Say, "Allah is most knowing of how long they remained. He has [knowledge of] the unseen [aspects] of the heavens and the earth. How Seeing is He and how*

[13] Brian Kettell, *Islamic finance in a nutshell* (1st edn, John Wiley & Sons 2010) pp.– 84 - 85

[14] For Muslims the principal idea is there is only One God, Allah (SWT) [SWT stands for "Subhanahu wa ta'ala" meaning "Allah is pure of having partners and He is exalted from having a son"; <http://www.irshad.org/glossary.php>] who is the Creator of everything. He had sent His commands to His prophets for spreading the knowledge to the mankind. For Muslims, the commands He had sent through His last prophet, Prophet Mohammed (pbuh) / (SAW) [SAW stands for "Salla Allahu alaihi Wa Sallam". It means "peace be upon him" (pbuh); <http://www.irshad.org/glossary.php> are to be strictly followed. These messages are put together and created the divine book, "The *Quran*". Further Muslims consider the way Mohammed (SAW) passed his life, as ideal example is known as "*Sunnah*". Additionally, the teachings, lifestyle and explanations given by Mohammed (SAW) were recorded by his disciples and created the numerous volumes known as "*hadiths*". Many Muslims consider six collectors of Hadith that became books as "*Sahih*" (meaning accurate), accessed 1 December 2013

Hearing! They have not besides Him any protector, and He shares not His legislation with anyone.""[15]

The last part of the verse makes it very clear that the supremacy belongs to Allah (SWT) alone and He is the sole Legislator. To be precise, for the purposes of this research, consideration would not be given to differences between the various schools of thoughts, as that is not the aim of this thesis, which is more geared towards theological studies. The primary aim of this thesis is to find the orthodox ideologies in Islamic laws and consider them with the background of English marine insurance law, with references to different *hadiths* as the need arises.

The concept of insurance as an economic vessel is comparatively new in Islamic jurisdictions. There have been many disagreements among Islamic scholars on the scope and affordability of insurance in line with Islamic principles, as detailed in later chapters.[16] The main causes of objections of traditional insurance in Islam are agreed, due to the presence of *riba* (usury), *gharar* (uncertain risk) and *maisir* (game of chance) in traditional insurance contracts. Accordingly, Islamic scholars have suggested an alternative to orthodox insurance known as *takaful,* which means guaranteeing each other. Given this is a rather new creation, there are only limited amounts of materials on this subject and the research would be more of a consideration of the problems that exist in *takaful* models, and comparison would be made mainly with English marine insurance law. As mentioned above, this research would aim to look at the concepts of *riba*, *gharar* and *maisir*, in line with modern insurance and look into *takaful* with the aim of further developments. It is important to point out that, whilst considering the Islamic principles, significant references would be made to the various parts of the *Quran* and *hadiths*, as these forms are the basis of the Islamic principles.

1.2. English Law:

[15] Holy *Quran*, 'Surah Al Kahf,' Chapter 18, Verse 26 (quran.com) <http://quran.com/3> accessed 14 November 2014

[16] See chapter 5 below for literature review with disagreements among various scholars regarding validity of insurance in Islam

English marine insurance law has its roots in the 16th century; until that time, English shipping merchants used to come together to create a mutual cooperative fund between themselves to cover marine risks. There had been a lot of ups and downs in English history in regards to marine insurance and the last piece of legislation to tie up the knot was the **Marine Insurance Act (MIA) 1906**. The **MIA 1906** evolved into various different types of other insurances as practised in England and Wales, e.g. life insurance, fire insurance, car insurance and such others.[17] The definition of marine insurance is found in **section 1 MIA 1906**, which states that:

"*A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to marine adventure.*"[18]

It is accepted that a marine insurance contract is a contract of indemnification,[19] where claims and parties' obligations are governed by policy wordings, i.e. agreement terms agreed between the parties. This paradigm found its strengths in the English common law courts by Lord Wright at the House of Lords in *Rickards v Forestal Land, Timber and Railways Co*,[20] where he confirmed that the objective and core principle of marine insurance contract is one of indemnity and to resolve problems as they arose in marine voyages. Additionally, Mr. Justice Brett in the Queens Bench Division at the High Court in *Castellain v Preston*[21] confirmed a marine insurance contract "*is a contract of indemnity, and of indemnity only*". Mr. Brett goes on further to mention that, in the case of a defined loss as per the marine insurance contract, the insured is to be completely indemnified but not more than the actual loss.[22] With these basic principles in mind, the

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[17] John Birds, *Birds' Modern Insurance Law* (7th edn, Sweet & Maxwell 2007) pp. – 1 – 3
[18] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/Edw7/6/41/section/1> accessed 2 December 2013
[19] In essence the rules actually applies for all types of insurance rather than marine specific but since the whole origin of the concepts are from marine insurance, it is best to avoid confusion but sticking to the core point for the moment
[20] Rickards v Forestal Land, Timber and Railways Co [1941] 3 All ER 62 at p 76, HL
[21] Castellain v Preston (1883) 11 QBD 380 at p. - 386
[22] Ibid

whole structure of marine insurance and, in essence, the whole of insurance in England and Wales, is structured.[23]

However, the aim of this thesis is not to delve into the history of English marine insurance law, but to understand the structure of the same for premium, risks, claims and compensation, and compare them with the Islamic law equivalent. As mentioned earlier, comparison shall now be made with a few known variables under both authorities to illuminate an understanding of the common objective standing of both.

2. Common concepts between English marine insurance law and Islamic insurance, *takaful*:

In this section, as stated above, discussion will be made to consider how much likeness exists between English marine insurance law and Islamic law *takaful*. To assist the ease of perusal, analysis would be made on common existing shared concepts, namely utmost good faith, warranties and contract construction. As further consideration is made of the thesis below, it would be noted that the underlying principles, e.g. utmost good faith and warranties, are similar to both, but the divergence is at the structure, i.e. affecting the concept of contract construction. This thesis goes on to examine the complications created due to structure variations and how best to improve, for the advantage of advancement, both English and Islamic law.

2.1. Utmost good faith:

2.1.1. Utmost Good Faith in English law:

One of the core concepts of insurance law is honesty, which is to be exercised at its highest level when entering insurance contracts. First and foremost, the point to mention is that, despite marine insurance being a contractual agreement, there is generally no duty of good faith in contract law. This has been clearly established by the House of Lords in

[23] Susan Hodges, *Law of Marine Insurance* (Cavendish Publishing Limited 2005) pp. - 1 - 4

Walford v Miles and marine insurance is considered rather as an exception.[24] Where marine insurance law is concerned, as set out in **sections 17, 18 and 20 MIA 1906**, the concept of *uberrimae fidei,* i.e. the principle of utmost good faith, is crucial. **Section 17 MIA 1906** makes it very clear that a marine insurance contract is a contract of utmost good faith that is to be respected by both the insurer and insured. **Section 18 MIA 1906** puts a duty of disclosure on the insured before the conclusion of a marine contract, along with **section 20 MIA 1906** stating how to avoid misrepresentation.[25] Lord Mansfield had considered this aspect of utmost good faith in *Carter v Boehm.*[26]

The disclosure duty is strict under English law, allowing the innocent party to avoid the contract where the undisclosed information was material. This duty of exercising utmost good faith is a continuing responsibility even after the creation of the contract.[27] This raises the issue of fraudulent claims where, under the statute, the contract would be considered as void *ab initio,* i.e. retrospective cancellation from the very beginning, but under common law the contract can be avoided, but does not apply retrospectively. As such, claims made before any fraudulent claim is put forth still remain valid, as demonstrated in the case of *AXA General Insurance Ltd v Clara Gottlieb & Joseph Meyer Gottlieb.*[28] In relation to materiality, **section 17 MIA 1906** requires there to be a link for the undisclosed information to be material, but the common law rule does not require as such, as set out in *Agapitos v Agnew.*[29]

The relationship between materiality, utmost good faith and disclosure are very strong in English marine insurance contracts. The insured is under a duty under **section 18(1) MIA 1906** to disclose all material facts be known or ought to have known, otherwise the insurer can avoid the contract. **Section 18(2) MIA 1906** facts are considered material if

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[24] Walford v Miles [1992] 2 AC 128
[25] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/Edw7/6/41> accessed 2 December 2013
[26] Carter v Boehm (1766) 3 Burr 1905
[27] However, the disclosure duty is not applicable once litigation is commenced, as the Civil Procedure Rules 1998 litigation rules are applicable from that point on.
[28] AXA General Insurance Ltd v Clara Gottlieb & Joseph Meyer Gottlieb [2005] EWCA Civ 112, CA
[29] Agapitos v Agnew (The Aegeon) (No 1) [2003] EWCA Civ 247, [2002] 2 Lloyd's Rep 42, CA; Simone Schnitzer, *Understanding International Trade Law* (Law Matters Publishing 2006) p. - 159

they would have an effect on providing the cover and the premium. This duty remains strict even when an agent is employed and the insured, acting in his capacity as a principal, would have the marine insurance contract avoided by the insurer for the failure of the insured's agent. Moreover, **section 20 MIA 1906** provides further strict rules that material representation is to be true. Material representation is an objective test on whether a prudent insurer's decision to provide cover or the premium would have been affected (**section 20(2) MIA 1906**). Representations made under expectation or belief is required to be made in good faith (**section 20(5) MIA 1906**).[30]

In the event of breach of utmost good faith, nondisclosure or misrepresentation, the consequential argument is that the information must have been material. This failure of the insured should play a part for the insurer to enter the marine insurance contract, even though it did not have a significant role as set in *Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd.*[31] The present law position is that, once there is a breach, it is sufficient for the insurer to either affirm or avoid the contract irrespective of the type of misrepresentation, i.e. fraudulent, negligent or innocent. However, to affirm, the insurer would have to fail to act within a reasonable period of time as established in *Liberian Insurance Agency v Mosse.*[32] The above-mentioned is a concise position of practice of utmost good faith in English marine insurance law by the parties; it sets the very high threshold expected for any prototype to achieve if it is to work alongside English marine insurance law.

Nevertheless, this area of law had been currently under scrutiny for a period of time and the Law Commission, the body in charge of proposing changes in law necessary in England and Wales, analysed and submitted the latest Draft bill on Insurance Law [HL] bill 39 in July 2014. In the draft in Part 5: Good faith and Contracting out, under paragraph 13, it has been proposed that the breach of utmost good faith argument be amended as such affecting **s. 17 MIA 1906** to be modified. It has been proposed that

[30] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/Edw7/6/41> accessed 2 December 2013

[31] Pan Atlantic Insurance Co Ltd v Pine Top Insurance Co Ltd [1994] 3 WLR 677, [1994] 2 Lloyd's Rep 427, HL

[32] Liberian Insurance Agency v Mosse [1977] 2 Lloyd's Rep 560, QBD

allegations of a breach of utmost good faith should no longer give a right to set aside the insurance contract and be in line with the Consumer Insurance (Disclosure and Representations) Act 2012.[33] This no doubt reflects an upcoming changing landscape for English insurance, particularly focusing on **s. 17 MIA 1906**; however, this is subject to the English Parliament approving the law, which is another matter of debate in itself and subject to further scrutiny, but outside the scope of this thesis.

2.1.2. Utmost Good Faith in *takaful* under Islamic law:

It is now relevant to consider a similar concept of utmost good faith under Islamic law, particularly under *takaful,* for witnessing the relevance between marine insurance and *takaful*. In *takaful*, the presence of utmost good faith between the parties in a *takaful* contract is very much considered as a compulsory requirement, as this is in line with the Islamic faith, as is detailed below.

"*Takaful* Malaysia", a *takaful*-providing organisation in Malaysia, explains that the *aqad,* i.e. contract between the parties, is that of trust/utmost good faith.[34] Malaysia is one of the pioneering countries to make *takaful* part of the national law, by allowing *takaful* to run alongside traditional insurance, with the implementation of the Malaysian **Takaful Act 1984**. Malaysian constitution, according to **Article 121(1A)** that refers to List II and **Article 3** of the **Constitution of Malaysia**, has allowed a dual system of Common law and Islamic law.[35] In the Malaysian **Takaful Act 1984** there is no mention of the utmost good faith in the statute itself, but to consider the fuller meaning in Islamic concepts, references need to be made to the core Islamic principles. It should be pointed out that the expansion that Malaysia has carried out with *takaful* finds its origin from the primary sources of Islamic law, i.e. the *Quran* and *hadiths*.

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[33] Insurance Bill [HL], 'European Convention on Human Rights' (2014 publications.parliament.uk) <http://www.publications.parliament.uk/pa/bills/lbill/2014-2015/0039/15039.pdf> accessed 7 September 2014

[34] Takaful Malaysia, '*Takaful* understanding in Malaysia' (takaful-malaysia.com.my) <http://www.takaful-malaysia.com.my/corporate/faq/Pages/faq.aspx> accessed 28 January 2014

[35] Constitution of Malaysia, 'Malaysian statute online' (confinder.richmond.edu) http://confinder.richmond.edu/admin/docs/malaysia.pdf accessed 3 December 2013

As a starting point, Islamic principles have always enhanced economic growth so long that this does not involve making money out of money, as such without any effort.[36] In the *Quran*, Surah Al-Baqarah, Surah 2 Verse 275, it is mentioned that:

- *"...Allah permits trading and forbids usury...As for him who returns (to usury) – Such are rightful owners of the Fire. They will remain in it."*[37]

The idea is to encourage Muslims to be involved in business, provided that *riba* can be avoided at all times. Usury is considered to be strongly denied, as it involves making money in the absence of hard work and making money from money alone in the absence of something concrete. Following this point, it is important to note that the Islamic view has always been against any methods that negate involving the whole truth of the matter. It has been mentioned by Prophet Mohammed (pbuh) time and time again to avoid iniquitous tactics in a business. In Sahih Muslim, Kitab Al- Buyu', hadith 3663, it states:

- *"Abdullah b. Dinar narrated that he heard Ibn 'Umar saying: [Mohammed (SAW) mentioned] '...When you enter into a transaction, say: There should be no attempt to deceive.'"*[38]

Further, the subsequent hadith 3664 mentions:

"... narrated on the authority of 'Abdullah b. Dinar [as]... "When he buys he should say: There should be no attempt to deceive."[39]

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[36] That is to say for example in case of traditional loans where interest are charged and money is made out of money without putting any effort from the lender i.e. the lender is not taking any risk and making the extra funds simply because he lend the funds. The same issue actually goes on with insurance as well, as readers would note that compensation is considered to have made money out of money from the insurer without any effort by the insurer and vice versa when the insurer is making money from the premium without any effort when a claim is not made by the insured

[37] Muhammad Marmaduke Pickthall, *The meaning of The Glorious Qur'an: An explanatory translation* (4th edn, Islamic Dawah Centre International 2008) p. - 32

[38] Sahih Muslim, 'The Book of Transactions' (Kitab Al- Buyu') Book 10 Hadith 3663 (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=010&translator=2&start=55&number=3662> accessed 20 October 2013

As these parts explain, Islam has always cited that the buyer must not try to utilise trickery when entering a business agreement. This has never been favoured, neither in the principal Holy book, The *Quran*, nor had such approaches been approved by the practices of the Prophet Mohammed (pbuh). Moreover, in Sahih Al-Bukhari, Sales and Trade, Hadith 352, it states:

- *"Narrated Ibn 'Umar: Allah's Apostle forbade Najsh."*[40]

Professor Dr. Mohd. Ma'sum Billah explains *Najsh* as a form of fraud in a transaction to mislead another.[41] The consequential effects of fraud/deceit in such circumstances are set out in practice by different organisations by their own bylaws, e.g. under the Sudan Rules of the *Sharia* Advisory Board rules, at page 11, a *takaful* contract may be considered to be void *ab initio* if the conduct is not in line with the Islamic principles.[42] In this case, one example could be failure to exercise utmost good faith by either party, which could result in the whole *takaful* contract being avoided from the start retrospectively. As mentioned above, Islamic principles have always prioritised the exercising of honest intentions at all times, under an onerous duty without allowing any opportunities for the existence of deception to enter a *Sharia* compliant transactions. Even if deceit does enter, then the *aqad* would be considered void.

In relation to disclosure of material information and misrepresentation, Islamic principles have also been strict. The Islamic principles have always asked for disclosure of all information in an agreement and to avoid arguments of deceit. The Islamic regulations

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[39] Sahih Muslim, 'The Book of Transactions' (Kitab Al- Buyu') Book 10 Hadith 3664 (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=010&translator=2&start=55&number=3662> accessed 20 October 2013

[40] Sahih Al-Bukhari, 'Sales and Trade' Book 34 Hadith 352 (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=34&translator=1&start=0&number=352#352> accessed 20 October 2013

[41] Professor Dr. Mohd. Ma'sum Billah, 'Regulatory framework of doctrine of "Utmost Good faith" in Takaful (Islamic Insurance)', page – 3; <http://www.panoramassicurativo.ania.it/get_file.php?id=14519>; accessed 5 June 2014

[42] Mohd. Ma'sum Billah, 'Takaful (Islamic Insurance): An economic paradigm' <http://www.takaful.coop/doc_store/takaful/economicParadigm.pdf> accessed 3 December 2013

have made it quite clear that parties to a transaction can go back to their previous position or get out of the deal, before the agreement is made. However, the presence of utmost good faith has been demanded at all times, irrespective of the type of commercial transactions. It is mentioned in Sahih Al-Bukhari, Sales and Trade, Hadith 293, that:

- *"Narrated Hakim bin Hizam: Allah's Apostle said, "The seller and the buyer have the right to keep or return goods as long as they have not parted or till they part; and if both the parties spoke the truth and described the defects and qualities (of the goods), then they would be blessed in their transaction, and if they told lies or hid something, then the blessings of their transaction would be lost."*"[43]

Additionally, in following Hadith 296:

- *"Narrated Hakim bin Hizam: The Prophet aid, "The buyer and the seller have the option to cancel or to confirm the deal, as long as they have not parted or till they part, and if they spoke the truth and told each other the defects of the things, then blessings would be in their deal, and if they hid something and told lies, the blessing of the deal would be lost."*"[44]

Beside the fact that Prophet Mohammed (pbuh) does not consider that such trickery sales are not blessed, other texts consider the lack of disclosure to have consequences. A lack of disclosure and, in essence, a failure of exercising utmost good faith is considered as not within the peripheries of Islam and is treated as *haram,* which means they are prohibited in Islam for Muslims. *Halal* is the opposite of what is allowed in Islam, according to Malik's Muwatta, Business Transactions, Hadith 31.23.54:

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[43] Sahih Al-Bukhari, 'Sales and Trade' Book 34 Hadith 293 (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=34&translator=1&start=28&number=290> accessed 17 November 2013

[44] Sahih Al-Bukhari, 'Sales and Trade' Book 34 Hadith 296 (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=34&translator=1&start=0&number=293#293> accessed 17 November 2013

- *"...Malik [said]..."...Had a man bought defective dirhams from him as being the full weight, that would not be halal..."*[45]

Other Islamic scholars found that failure to disclose could even consider the transaction as illegitimate, as mentioned that:

"Uqba bin Amir (r.a.) said: it is illegal for one to sell a thing if one knows that it has a defect, unless one informs the buyer of that defect."[46]

Moreover, it is ordered by Allah (SWT) that utmost good faith is mandatory and any attempts of nondisclosure are not acceptable, as mentioned in Surah Al-Baqarah Surah 2 Verse 42 that:

- *"Mix not truth with falsehood, nor knowingly conceal the truth."*[47]

Under **Section 28** of the Malaysian **Takaful Act 1984** it makes it explicit that, where fraud, deception, or misrepresentation has been made, the guilty party would be liable for a fine of up to 20,000 Malaysian Ringgit and/or imprisonment of up to 1 year.[48] Although no mention has been made of the effect on the contract, it can be implied that the contract could be held invalid when the consequence has criminal punishment. As an example, *"Noor Takaful"*, a medical cover *takaful* provider in the UAE, Article 10 of the *takaful* contract makes it clear that the Certificate would be *"null and void"* on presence of false declaration and non-disclosure by the Participant.[49] It is a breach of utmost good faith by the participant and breach of a condition of the *takaful* contract that the participant

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[45] Malik's Muwatta, 'Business Transactions' Book 31 Hadith 31.23.54 (searchtruth.com) <www.searchtruth.com/book_display.php?book=31&translator=4&start=0&number=31.23.54#31.23.54> accessed 17 November 2013

[46] Abdulkader S. Thomas, Stella Cox, Bryan Kraty (eds), *Structuring Islamic finance transactions* (Euromoney Books 2005) p. - 23

[47] Muhammad Marmaduke Pickthall, *The meaning of The Glorious Qur'an: An explanatory translation* (4th edn, Islamic Dawah Centre International 2008) p. - 10

[48] Bank Negara Malaysia (Central Bank of Malaysia), 'Malaysian statute online' (bnm.gov.my) <http://www.bnm.gov.my/index.php?ch=14&pg=17&ac=18&full=1> accessed 3 December 2013

[49] Noor Investment Group, 'Malaysian *takaful* operator terms Article 10 (a) & (b)' (noortakaful.com) <http://www.noortakaful.com/medical/Medicare_500_Takaful_Terms_Conditions.pdf> accessed 12 March 2014

refrains from false declaration and non-disclosure. In light of the Islamic prospect, there are severe restrictions against fraudulent representations. As mentioned above, it is quite obvious that *takaful* would consider the Islamic principles in determination of queries.

As a final point, it is worth mentioning that the *Quran* has mentioned expressly against deception in business and commanded that truthfulness be present at all times, as in Surah Hud, Surah 11 Verse 85 that:

- *"...Give full measure and full weight in justice, and wrong not people in respect of their goods. And do not do evil in the earth, causing corruption."*[50]

The sections quoted above are significantly relevant to mention because the whole of the Islamic principles are based on these, and *Sharia* law would take these sections when considering the same when making any decisions. The crucial aspect of such discussion of utmost good faith is intended as an introduction, before delving into the whole thesis, the extremely close working ethics of both traditional marine insurance and *takaful* concepts, particularly in light of the core texts of Islamic law. As would have been noted, the primary concept of exercising utmost good faith is strictly present in both traditional marine insurance and *takaful* in order to demonstrate the close thinking process of both the concepts and the similar primary aim that both of these concepts have. To witness the close relationship of both concepts, a discussion will take place into the aspect of warranties as practised in traditional marine insurance and under Islamic law.

2.2. Warranties:

2.2.1. Warranties in English law:

Another concept that is of common use in traditional marine insurance English law is the concept of warranties, which are basically terms that the parties are required to follow for

[50] Muhammad Marmaduke Pickthall, *The meaning of The Glorious Qur'an: An explanatory translation* (4th edn, Islamic Dawah Centre International 2008) p. - 139

the cover. This is somewhat different from the contract law warranties notion and a brief explanation would assist the reader's understanding further. In the context of contract law, the rules governing the relationship between the parties comprise mainly two types. One is condition, which is the primary term of the contract, while the other is warranty, which is the inferior term of the contract.[51] Lord Justice Fletcher Moulton has defined condition in *Wallis v Pratt*[52] as a critical term in that failure of compliance is at the heart of the contract, resulting in the complete breakdown of the agreement. Warranties have been explained in **section 61 of the Sale of Goods Act (SOGA) 1979** as a secondary term in that failure to fulfil would raise a claim for compensation, but would not allow the disadvantaged party to repudiate the whole contract.[53]

In the case of English marine insurance, as mentioned above, is also considered as a contractual obligation between the parties. Therefore, like contract law, there are also conditions, warranties and clauses present in this relationship; in marine insurance, however, warranties have more significance than in general contract law. The contractual relationship between the insurer and the insured would generally be subjected to the insured fulfilling certain obligations set by the insurer. These obligations could range from sailing with a particular number of individuals on board (as set out in *De Hahn v Hartley*),[54] to not sailing to certain regions (as set out in *The Good Luck* case).[55] These obligations are considered as warranties in English marine insurance, which are strict obligations that the assured have to comply with, or maintain to keep intact the marine insurance cover.

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[51] There is also a third type known as Intermediate/Innominate terms established by the Court of Appeal in Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd [1962] QB 26; [1961] 1 All ER 474, where the court looks at the effect and nature of breach to determine whether the term was considered to have an effect as a condition or not.

[52] Wallis v Pratt [1910] 2 KB 1003 at 1012; affirmed [1911] AC 394; Margaret Griffiths, Textbook: Commercial Law (4th edn, Old Bailey Press 2005) p. - 41

[53] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/1979/54> accessed 4 December 2013

[54] De Hahn v Hartley (1786) 1 T.R. 343

[55] Bank of Nova Scotia v Hellenic Mutual War Risks Association (Bermuda) Ltd, The Good Luck [1991] 2 WLR 1279

Section 33(1) MIA 1906 considers the consequence of breaches of Marine Insurance warranties.[56] The situation is that, any breach of compliance, with the marine warranty occurring discharges the insurer from making payment to the assured, in the event of a loss taking place, i.e. no payment of compensation in the event of claim. As **section 33(3) MIA 1906** illustrates, breach does not need to have any connection with the loss occurring, i.e. there is no need for there to be a link between contractual breach and tortious causation. However, any loss occurring before noncompliance allows the insured to have a legitimate ground to ask for indemnification.[57] From the ordinary person's perspective, this means that the insured would not be entitled to indemnification/compensation in the case of failing to follow the warranties, despite the fact that the breach that occurred has no relationship with the caused event. Further, following the House of Lords' decision in *The Good Luck*, breach automatically discharges the insurer from further obligations to the insured under the insurance contract, rather than giving the insured any option to exercise.[58] It is considered by Lord Goff, quoting from Lord Blackburn in *Thomson v Weems & Others*,[59] that the compliance with warranty is considered as a condition precedent discharging the insurer from the liability to indemnify. As academics had expressed, that breach changes the nature of the contract from what the parties had initially agreed in the first place.[60] However, the aspect, which is of importance, is that concept of warranties exist in English marine insurance law, making the scheme watertight and is an existing character. It is relevant to compare with *takaful* whether such a character exists in that, so as to see how close the working ideologies are.

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[56] Legislation, 'English statute online' (opsi.gov.uk) <http://www.opsi.gov.uk/RevisedStatutes/Acts/ukpga/1906/cukpga_19060041_en_1> accessed 4 December 2013

[57] Susan Hodges, *Law of Marine Insurance* (Cavendish Publishing Limited 2005) pp. - 96 – 99

[58] Bank of Nova Scotia v Hellenic Mutual War Risks Association (Bermuda) Ltd, The Good Luck [1991] 2 WLR 1279; John Birds, supra at pp. 152 – 154

[59] Thomson v Weems & Others (1884) 9 App Cas 671; Ray Hodgin, *Insurance Law: Texts and Materials* (2nd edn, Cavendish Publishing Limited 2002) pp. - 336 – 338

[60] It can be noticed the apparent partiality and severity existent, which has lead English courts using various techniques to interpret the warranties so as to downgrade to suspensory conditions to avoid the its harsh effect. This in effect leads to uncertainty as precedents conflicts in determining whether a particular term obtains the status of warranty.

Before exiting this topic, it is relevant to mention that the Law Commission's Draft bill on Insurance Law [HL] bill 39 on July 2014 considered the concept of warranties as well. In the draft in Part 3: Warranties, under paragraph 9, it is strictly against changing representations into warranties. However, the relevant subsections under paragraph 10 are the crucial points dealing with the effect of breach of warranties. It has been proposed that breach of contract arguments on the basis of warranty breaches are no longer valid. It goes on further to state that the interim period between breach and remedy will not require the insurer to indemnify, save where the breaches are inapplicable to the contract, unlawful or waived off by the insurer. Additionally, it has been proposed that, where the insured is required (or not required, as may be the case) to do something within a requisite period, but fails to do so, yet the risk remains the same as anticipated during the initial contract, then it is considered that the breach is remedied, i.e. where the insured stops the breach that is occurring. Finally, the proposal states for the omission of the second line of **s. 33(3) MIA 1906** and the whole of **s. 34 MIA 1906**, which effectively means that the proposal is asking for a link between breach and causation in warranties, rather than discarding the whole policy flatly.[61] As mentioned above, this is simply a proposal from the Law Commission. This is not the first time, as attempts have been made to amend the **MIA 1906**. So, whilst, it does appear ambitious, it would certainly be a matter of time and, in essence, political circumstances of the UK before the following proposals can turn into law.

2.2.2. Warranties in *takaful* under Islamic law:

As mentioned above, *takaful* is a recent creation and there are very few materials on the aspect of warranties and consequential breaches. A *takaful* contract also has conditions that the participant must satisfy at all times. However, it is important to note that the breach has a somewhat different effect in *takaful,* as is seen in Western communities. This is, of course, reserving the position of breach of utmost good faith concepts, which are mentioned above. Before discussing further, it is important to look at the principle of

[61] Insurance Bill [HL], 'European Convention on Human Rights' (2014 publications.parliament.uk) <http://www.publications.parliament.uk/pa/bills/lbill/2014-2015/0039/15039.pdf> accessed 7 September 2014

a *takaful* contract in order to understand in relation to the Western insurance concept on warranties.

Takaful, as discussed earlier, means guaranteeing each other, which relates to cooperation and mutual help. This is similar to orthodox insurances that are practised in the West, but it is a reciprocated mechanism rather than a traditional insurance, where payment is made at the expenses of the insurer. **Section 2** of the Malaysian **Takaful Act 1984** defines *takaful* in the same vein, in that it is an agreement between a group of individuals, where it is in the common interest that members of this group would be helped when required, as:

- *"...a scheme based on brotherhood, solidarity and mutual assistance which provides for mutual financial aid and assistance to the participants in case of need whereby the participants mutually agree to contribute for that purpose."*[62]

The participants would come together to form a pact where they would contribute to a combined fund as *tabarru,* meaning donation, gift or charity.[63] In the event of loss, the member would be allowed to receive a certain amount in accordance with the pact agreement. In *takaful* generally, liability is not argued, as it is not the expenses of another that one benefits from, since it is a joint paradigm, where a fixed amount would be received on an occurrence of a certain event.[64] The principle behind this is that, under Islamic law, it has been encouraged that individuals should be involved in trade but not at the expense of another's loss and suffering.[65] Nevertheless, in line with this principle, the terms expressed in the *takaful* contract set by the insurers have placed consequences, if not followed, similar to those of warranties in traditional insurance. For example, under *"Noor Takaful"* as mentioned above,[66] Article 16 of the *takaful* contract asks for

[62] Bank Negara Malaysia (Central Bank of Malaysia), 'Malaysian statute online' (bnm.gov.my) <http://www.bnm.gov.my/index.php?ch=14&pg=17&ac=18&full=1> accessed 4 December 2013
[63] Eurekahedge, '*Takaful* explanation on *tabarru'* (eurekahedge.com) <http://www.eurekahedge.com/news/07_feb_IFN_TakafulFunds.asp> accessed 26 September 2013
[64] Angelo M. Venardos, *Islamic Financial Products; Islamic Banking & Finance in South-East Asia: Its Development and Future* (World Scientific Publishing Co. Pte. 2005) pp. – 85 - 86
[65] See above Surah Al-Baqarah, Surah 2 Verse 275
[66] See footnote 36 above

subrogation of the claim to a *takaful* provider to go against the third party.[67] This is a term of the contract between the participant and *takaful* operator that the participant should follow strictly, otherwise it raises the circumstances of breach of *takaful* agreement between the parties, causing the *takaful* operator to go after the participant for the losses paid out.

Additionally, it has been stated in the Holy *Quran* a number of times, as Allah (SWT) has mentioned, that once a promise is made it must be kept. Warranties and conditions are agreement terms that parties have made to one another to be kept. It has always been mentioned that one stays within their limits but, once a promise is made, then one needs to keep those promises, even in the detriment. It is stated in Surah Al-An'am Surah 6 Verse 152 that:

- *"...We task not any soul beyond its scope. And if you give your word, do justice to it, even though it is (against) a relative; and fulfil the covenant of Allah..."*[68]

A similar concept has been emphasised in one of the important Surah, Surah Bani Israel, when Prophet Mohammed (pbuh) went through seven heavens to meet Allah (SWT). Allah (SWT) once again stated that the keeping of promises is paramount and mentioned one must refrain from providing wrong estimates. In Surah Bani Israel Surah 17 Verse 34 it states:

- *"...and keep the covenant. Of the covenant it will be asked."*[69]

And in the subsequent Verse 35:

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[67] Noor Investment Group, 'Malaysian *takaful* operator terms, article 16, p. - 13' (noortakaful.com) <http://www.noortakaful.com/medical/Medicare_500_Takaful_Terms_Conditions.pdf> accessed 12 March 2014

[68] Muhammad Marmaduke Pickthall, *The meaning of The Glorious Qur'an: An explanatory translation* (4th edn, Islamic Dawah Centre International 2008) p. - 90

[69] Muhammad Marmaduke Pickthall, supra at p. - 171

- *"Fill the measure when you measure, and weight with a right balance; that is proper, and better in the end."*[70]

Finally, it is worth mentioning that Allah has ordered Muslims to desist from iniquitous approaches and keep the pledges that they have made. This has been set out very explicitly in Surah An-Nahl Surah 16 Verse 90:

- *"Allah enjoins justice and kindness, and giving to kindred and forbids lewdness and abomination and wickedness..."*[71]

More importantly, in the next Verse 91, it states:

- *"Fulfil the covenant of Allah when you have covenanted, and break not your oaths after the affirmation of them, and after you have made Allah surety over you. Allah knows what you do."*[72]

Accordingly, this would assist in comprehending and appreciating the closeness shared, once more, between traditional marine insurance and *takaful* in terms of a core concept such as warranties. The above considers the position of the concept of warranties under Islamic law, which is the backbone of *takaful*. In addition, it illustrates how, both under traditional and Islamic law, paradigms have the same view and are also shared in relation to the terms of insurance agreement. As a final comparison, it would be of much relevance to consider through the concept of contract construction, i.e. how insurance contract is created under traditional marine insurance law and the same being created under *takaful*. It should be noted during consideration that, even though the thinking aspect of traditional marine insurance and *takaful* synchronises, the formulation functioning aspect is different. It is asserted that this mechanical aspect of *takaful* might be the cause of the present day drawback of *takaful*; this has led to the construction of

[70] Ibid
[71] Muhammad Marmaduke Pickthall, supra at p. - 166
[72] Ibid

this thesis in order to investigate the causes of concerns and the proposing of rectification, as highlighted in the aims and objectives in the previous chapter.[73]

2.3. Contract construction - The formation of an insurance contract:

2.3.1. Insurance contract formation procedure in English law:

A marine insurance contract follows very much the same legal principles as general English contract law, i.e. offer, acceptance, consideration and intention to create legal relations. However, the procedural aspect is quite different than that followed in other contractual dealings. In a concise account, the proposed assured to obtain a marine insurance cover would generally approach a marine broker with details of the cargo goods, vessels, parties and voyages involved in the relevant marine transaction. The broker is considered as an agent of the proposed assured, who would take down instructions from the principle, i.e. the proposed assured, on a piece of paper, which is known as a "slip". The aim of the broker is to approach different marine underwriters to obtain full marine insurance risk cover.

The underwriter would initial/sign and mention the percentage he wants to cover on the slip from respective insurers, which is known as writing a line. The Court of Appeal in *General Re-Insurance Corporation v Forsakringsaktiebolaget Fennia Patria*[74] determined that a contract has taken place with the specific underwriter for the specific premium and percentage the moment when the underwriter writes a line. Once the appropriate amount of risk is covered, the broker would draw a policy and obtain the premium from the insured. However, under **section 22 MIA 1906** the slip, as the contract, must be incorporated with the policy for it to be admissible as evidence;[75] yet, for construing the applicability of a marine insurance contract, the general principles of

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[73] Please see Chapter 1, sections 5 and 6 above

[74] General Re-Insurance Corporation v Forsakringsaktiebolaget Fennia Patria [1983] QB 856; John Birds, *Birds' Modern Insurance Law* (7th edn, Sweet & Maxwell 2007) p. - 89

[75] Legislation, 'English statute online' (opsi.gov.uk) <http://www.opsi.gov.uk/RevisedStatutes/Acts/ukpga/1906/cukpga_19060041_en_1> accessed 10 January 2014

contract law are applied. The insurance contract is considered acceptable so long as the contractual terms are understandable without the need for legibility. The Court of Appeal in *Koskas v Standard Marine Insurance Co Ltd*[76] even allowed the insurer to rely on terms that were hardly legible due to small print. Nevertheless, for the marine insurance to commence, the insured would need to pay the premium and the cover becomes effective.

Once the cover is effective, the insurer has taken the liability for the risk of the defined goods for the defined voyage. In the event a defined catastrophe takes place and loss is incurred, the insured can claim for compensation from the insurer, which of course would be significantly more than the premium amount paid. The insurer would ask the insured for an excess payment before dealing with the claim. Excess can be described as "*the amount payable by you, the insured in the event of damage or loss... expressed in either monetary or percentage terms. An excess is typically used to discourage moral hazard and to remove small claims, which are disproportionately expensive to handle.*"[77] The marine insurer would consider the claim and, if it transpires to be a legitimate claim satisfying all the elements of tortious liability, if it is a third party claim and/or contractual responsibility and if it is a personal claim, then compensation payment is made.

However, the marine insurance contract construction is somehow different than a general contract; but, most importantly, it should be noted that traditional marine insurance contract construction is significantly different than *takaful* contracts. This is where the arrow of this thesis is going to strike, to note whether, aside from the thinking ideology which is similar to both as noted above, the contract formulation feature of *takaful* needs possible remodification. As a result, consideration would be made that to what extent are the elements of premium, risks, excess and compensation would come into play.

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[76] Koskas v Standard Marine Insurance Co Ltd (1926) 25 L.I.L.R. 363

[77] At times the terms 'deductible' or 'retention' is used instead of excess but they have the same meaning. GJW Direct, 'Excess meaning in practice' (gjwdirect.co.uk <http://gjwdirect.co.uk/boatinsurance> accessed 6 June 2014

2.3.2. Formulation of *takaful* contract under Islamic law:

The procedure of the creation of a *takaful* contract is unique compared to marine insurance, even general insurance, in the Western insurance industry. The principles of the formulation of the *takaful* contract are, in fact, built on concepts from Islamic banking. This has resulted in borrowing concepts to devise *takaful* to work as an insurance tool. Therefore, unlike marine insurance, where the structure and flow of events are pretty much straightforward, the contract construction and flow of events in *takaful* largely depend on an instrument used to devise a different model of *takaful*. The aim of this section is to look briefly at the main different types of *takaful* contract construction used. Currently, three different instruments involving models of *takaful* contract construction are used, namely by the use of the instrument of *mudarabah*, *wakala* and *waqf*. Other variations are made by creating a hybrid and all these various models are fully discussed later on in the thesis.[78]

One of the most common procedures of construction of a *takaful* contract is to use a *mudarabah* relationship, which is frequently used in Malaysia. A *mudarabah* contract is a profit and loss sharing-based relationship, where one party acts as an investor and provides funds to another party who acts as an entrepreneur. The entrepreneur is to invest the funds in *halal* projects with the profits from the project to be shared between the parties in proportions agreed before commencement. If there is a loss, generally the investor carries the liability for this risk.[79] In *takaful*, this *mudarabah* instrument is implemented by applying the terminology that the participants act as the investors and the *takaful* provider as the entrepreneur. The monies provided as contribution by the participants are as a donation and the entrepreneur invests these in one pool of fund; the profits generated are shared between the entrepreneur and investors as agreed in advance. In the event of a loss, the *takaful* provider bears the loss instead so as not to make the participants liable for the operation's loss.[80]

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[78] See below chapters 5 and 6

[79] Brian Kettell, *Islamic finance in a nutshell* (1st edn, John Wiley & Sons 2010) pp. - 36 - 37

[80] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) p. - 17

An alternative arrangement for construction of a *takaful* contract is by a *wakala* instrument normally used in the Middle East. A *wakala* contract is a principal and agent relationship, where the principal provides sums to an agent, *wakil,* to invest on his/her behalf as advised and appropriately to raise revenues. The agent is entitled to a fee that can be taken from the invested sum, or from a portion of the profit.[81] In *takaful* using a *wakala* instrument, the participant acts as principal investor by providing the funds and the *takaful* operator acts as the *wakil.* The funds provided by the participants are considered as a donation and the *takaful* operator keeps any revenues generated. However, on strict interpretation as there is a principle and agency relationship, the *takaful* operator charges the participants with a fixed fee on profits generated and consider to have the funds returned to the participants.[82]

Additionally, a hybrid of *mudarabah* and *wakala* has also been in use among the Muslim community, where the aim has been to avoid problems that are present on an individual level. The above use of a *mudarabah* and *wakala* instrument and their hybrids is quite common in *takaful.* Lately, a new model has been introduced by the use of a *waqf* instrument for *takaful. Waqf* is a trust where an endowed property is kept and used for charitable or religious purposes.[83] In a *waqf*-based *takaful* model, it is an amalgamation of *waqf, mudarabah* and *wakala* where an initial donation is made by *takaful* shareholders to commence the *waqf.* Subsequently, as donations are received from participants, they are divided under a *wakala* agreement along with the *takaful* operator taking a portion, while the remainder is invested under a *mudarabah* agreement. The profit generated is apportioned under a *mudarabah* contract that is used to pay off operational and management expenses of the *takaful,* with any surplus for the participants' consideration.[84]

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[81] Brian Kettell, *Islamic finance in a nutshell* (1st edn, John Wiley & Sons 2010) p. - 150
[82] *Reorient, 'Wakala* succinct analysis' (reorient.co.uk) <https://www.reorient.co.uk/web_package.php?packageId=15> accessed 5 May 2013
[83] *Merriam-Webster, 'Waqf* succinct analysis' (merriam-webster.com) <http://www.merriam-webster.com/dictionary/waqf> accessed 6 June 2014
[84] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 423 - 426

As examined above, the *takaful* contract construction is significantly different than the straightforward traditional marine insurance structure. This raises concerns, where the various concepts of insurance contract operation, namely premium, risks, excess and compensation, fit in these various *takaful* models. After all, the whole aim of *takaful* is to be an alternative to insurance with the aim of safeguarding the insured for defined catastrophes. Whilst it is obvious that the core underlying objectives of insurance and *takaful* are similar, as witnessed above, with utmost good faith and warranties, yet the operational aspect of *takaful* misses out on the vital organs of contract construction, namely premium, risks, excess and compensation.

The above snapshot of a *takaful* contract construction is discussed in a general sense and in extensive discussions of each of the various models of takaful, as the application of the different types of instruments is discussed later in the thesis. As would be noted later on in this thesis, the existing *takaful* model structures are, in fact, quite complex, as with the very concise overview that is explained above. However, the scholars and academics, particularly Islamic intellectuals themselves, have been diversified in their views on the validity of various present day *takaful* models and have been in conflict within their own community, regrettably.[85] This has provided the basis for the research to analyse in-depth the concept of contract construction of various types of *takaful* models, in line with the core concepts of premium, risks, excess and compensation, and in discovering an alternative *takaful* model, which will not only suffice Islamic law, but also established jurisdictional law, such as English marine insurance law. This thesis will not be looking into the life *takaful* models, which are connected to life insurance concepts, rather it will be focused on the aspect of general *takaful* models in this respect.

[85] See below chapters 5 and 6

3. Overview Table:

Area of Insurance Law examined on the proposed *halal* marine insurance model				
Research questions to access the workability of the *halal* marine insurance model	**General**		**Claims**	
	Premium	**Risks**	**Excess**	**Compensation**
1. What is the link between traditional insurance law and the proposed *halal* marine insurance model?	In both cases, premium is charged although, in a *halal* insurance model, it would be a fee benchmarked against premium.	In both cases, the risks would be covered for individual cases; a safety pot would also be kept. By insurer/ *takaful* operator for covering the insured amounts.	In both cases, excess has to be paid for a valid claim although, in a *halal* insurance model, it would be a fee benchmarked against excess.	In both cases, compensation would be paid for insured perils within the ambit of level of cover agreed in advance between the parties.
2. To what extent has this area been influenced by western insurance, i.e. UK marine insurance law?	Presence of payment by insured has always been existent within *takaful* models as well.	The whole idea is to have defined risks covered by insurer, rather than putting liabilities on	This would be a new introduction to proposed *halal* insurance model as present *takaful* models	This would be a new addition to the field as present *takaful* models makes it a cooperative responsibilities with

		insured in case of deficits as is currently the case with existent *takaful* models.	do not ask for payment of excess.	the liability baton passed to the Participants/ Insured.
3. Is there a possibility that the current *takaful* provisions are being influenced by a more necessity and catch up with the traditional Western culture?	Presence of initial contribution as premium payment has always been present from the earliest of times in both cases.	Once more, risks covering in both cases have been the motto, but with the proposed *halal* model it will be along the same line as traditional insurance.	The current *takaful* models are alien to this concept on excess as it is likely that the models became flawed, which will be repaired in the proposed *halal* model.	The present *takaful* models are not well structured in compensation payments and muddled in their cooperative approach, which is corrected and restructured in the proposed *halal* model.

Part II

The restrictions prohibiting traditional insurance acceptability in Islam

Chapter 3: *Riba* (Usury)

1. Introduction:

This chapter examines the concept of insurance from an Islamic viewpoint. Before explaining the exact position of Islam in insurance, it is appropriate to look at the historical perspective of Islam within insurance and a few core Islamic concepts, which will assist in understanding the position fully.

2. Brief historic position:

The initial concept of insurance derived from the practice of *aqila,* where tribes people used to come together to pay off *diyya,* i.e. blood money, as compensation to the victim's family on behalf of the murderer, so as to avoid vengeance conflicts. This coming together to compensate for the victim was used by business-related losses by merchants in Makkah, Saudi Arabia, before the coming of Prophet Mohammed (pbuh). As cited by the author, Afzal-ur-Rahman, on one occasion trading caravans were lost in the desert and various members paid into the contributory fund, including Prophet Mohammed (pbuh) who, at the time, was trading with his first wife Hazart Khadijah's capital.[86]

Following that, it appeared that the first time the Muslim community had considered the existence of insurance and, to be precise, marine insurance, was when the Islamic scholar Ibn Abdin,[87] who lived between 1784 until 1836 in Damascus and who was very influential at the time, considered in his text, "*Scrutinized answers for dispersed*

[86] Afzal-ur-Rahman, 'Banking and Insurance (Economic Doctrines of Islam)', Vol. IV (London, 1979), 32 mentioned by Syed Khalid Rashid, "Islamization of Insurance – A Religio-Legal Experient in Malaysia", in the Textbook: M. Kabir Hassan and Mervyn K. Lewis (eds), *Islamic Finance* (Edward Elgar Pulishing 2007) p. - 406

[87] Full name Mohammed Amin Bin Omer Bun Abdel Aziz Aldemashqy Abdeen

questions". In his chapter "*The trust of the unbeliever*" in part of "*Al jihad*", he explains the procedure of the usual practice of traders to hire boats and pay hire charges along with a deposit on top as security, which were used to cover any damages that might have occurred during the voyage, minus the agent's fee for giving this security. This payment was called "*sowkra*" and the transactions were with non-Muslims. Ibn Abdin goes on further to suggest that the traders would not get back any of the funds as "*commitment to offer something non-committable*". Those ideologies, of making promises of the unseen and unmanageable such was considered as an unmeritorious contract, were such that Muslims could not enter with each other.[88]

Additionally, Ibn Abdin considered attempts to distinguish between insurance of agents and pledges of hire charges, but concluded that insurance would not be legitimate, as it would not have the same status as the pledges.[89] Later on, the Ottoman Maritime Code of 1863 was constructed, but there were uncertainty about the concept and was considered *haram*.[90] As such, it was regarded that insurance itself was forbidden for Muslims and this lead to a slowing of advancement in commerce. However, towards the second part of the nineteenth century, when Western banking institutions started to expand with *halal* banking, the legitimacy of insurance in Islam started to become a debatable issue. In the 1970s, Muslims considered an alternative form of insurance called *takaful* and, in 1979, the first Islamic insurance company called the "*Islamic Insurance Co. Ltd*" was created in Sudan. This company was making up to 10% returns for its shareholders, which lead to other countries investing in the *takaful* industry.[91]

3. Arguments against traditional insurance:

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[88] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) p. - 13

[89] Aly Khorshid, supra at p. - 14

[90] S.H.Amin, 'Islamic Law in the Contemporary World', (Glasgow, 1985), 71 – 84 mentioned by Syed Khalid Rashid, supra at p. - 406

[91] Mher Mushtaq Hussain and Ahmad Tisman Pasha (Corresponding Author), 'Conceptual and Operational differences between general Takaful and conventional insurance' (2011) Vol. 1 No. 8 [23-28] Australian Journal of Business and Management Research, pp. - 23-24

There are a number of arguments that are being raised against traditional insurance. As will be witnessed, what in fact should be the arguments against the working principle of traditional insurance, has been considered by the Islamic society as reasons for loathing insurance overall. This is an issue that will be dealt with later in the thesis.[92] However, coming back to the arguments made by Muslims for considering traditional insurance as *haram,* there are a number of concepts. The first in line, and one of the major points of concern, is the concept of (1) *riba* along with the concepts of (2) *gharar* and (3) *maisir/qimar*. Author Oliver Agha mentions the concept of *tawakkul,* i.e. reliance of God,[93] but it is felt that the above three restrictions pretty much cover the grounds on contravention of *tawakkul*. It is important to note that these concepts apply equally to all types of contracts or transactions in determining whether the contracts are *halal*. Apart from these restrictions, any Muslim who chooses traditional insurance as opposed to *takaful* does so with the view that traditional insurance is only there to fill their own pockets and infringes the Islamic set standards for their own gains.[94]

4. *Riba*, the concept:

In normal conversation, when anyone hears the word *riba,* a possible image that comes to mind would be a Muslim complaining about the interest he has to pay on his loan or concerned about the interest he is receiving in his bank account; in such cases, he is probably referring to *riba*. However, the scope of *riba* is quite broad and, more importantly, during perusal of this thesis it shall become more obvious that it is a lot broader, even from an insurance perspective, than what has been considered by *fuqaha,* i.e. Islamic scholars to date. It is well accepted among *fuqaha* that *riba* is the main reason why the Islamic society has a problem accepting traditional insurance. *Riba* is a noun and the simple verb for it is *raba*, which means increased or grew.[95] It has been defined by

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[92] See chapter 4 below where the researcher discusses about the ideology behind the existent Islamic insurance alternative

[93] Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, p. – 71

[94] Haemala Thanasegaran, 'Growth of Islamic Insurance (Takaful) in Malaysia: A model for the region?' (2008) 143 Sing. J. Legal Stud., p. - 145

[95] Ruba Alfattouh, Abdulkader Thomas and Najwa Abdel Hadi (trs), 'Riba in Lisan Al Arab' Translated and abridged from Imam Abi Fadl Jamaluddin Muhammad bin Mukarram, "Lisan Al Arab (Beirut; Dar

Al-Jaziri (1986) that *riba* means "trading two goods of the same kind in different quantities, where the increase is not a proper compensation".[96] Therefore, it has been co-related to the simple fact and the aspect that is related to this thesis, that where money is exchanged for money (e.g. as in loans) it would be viewed as *riba*. It is generally accepted among the scholarly community that *riba* refers to the concept of "usury", which described the custom of lenders lending funds to recipients but charging a high interest rate along with the return of the principal sum. Among Muslims, it is considered that money is an avenue of exchanging different types of items, which themselves are not considered valuable, but as equipment for use in the transaction. The objective of money is to assist with the valuation of items of exchange and nothing more. As shall be witnessed below, the *Quran* and *hadith* have made this aspect very clear and it is worth exploring some of the divine literature so as to make the concept clear.

5. Religious laws:

5.1. Analysis under Islamic law:

Riba is considered a severe sin among the whole of the Muslim community and the Holy *Quran* and the *hadiths* talk strongly against it. The main express restrictions from dealing with usury were ordained by God before the battle of Uhad on 19 March 625, where in *Surah Ali Imran* (Chapter 3), Verses 130 to 132 it is mentioned:

- *"O you who have believed, do not consume usury, doubled and multiplied, but fear Allah that you may be successful.*
- *And fear the Fire, which has been prepared for the disbelievers.*

Saadr, n.d.)", p. - 304 and further abridged from the original translation, which appeared in The American Journal of Islamic Finance

[96] Mohamud A. El-Gamal, *Islamic Finance: Law, Economics and Practice* (Cambridge University Press 2009) p. - 49

- *And obey Allah and the Messenger that you may obtain mercy."*[97]

There had been a number of other warnings in the Holy *Quran* from God against *riba* and, instead of exploiting others in this respect, the same has been compared with *zakat* (compulsory charity) or *sadaqah* (voluntary charity), as mentioned in *Surah Ar-Rum* (Chapter 30), Verse 39:

- *"And whatever you give for interest to increase within the wealth of people will not increase with Allah. But what you give in zakah, desiring the countenance of Allah - those are the multipliers."*[98]

Additionally, in *Surah An-Nisa* (Chapter 4), Verses 161 to 162, it is mentioned:

- *"And [for] their taking of usury while they had been forbidden from it, and their consuming of the people's wealth unjustly. And we have prepared for the disbelievers among them a painful punishment.*
- *But those firm in knowledge among them and the believers believe in what has been revealed to you, [O Muhammad], and what was revealed before you. And the establishers of prayer [especially] and the givers of zakah and the believers in Allah and the Last Day - those We will give a great reward."*[99]

Most important of all, there will be severe consequences, as has been warned by God, against the taking of *riba* in *Surah Al Baqarah*, Chapter 2, Verses 275 to 281, where it is strictly mentioned:

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[97] Holy *Quran*, 'Surah Ali Imran' Chapter 3, Verses 130 to 132 (quran.com) <http://quran.com/3> accessed 11 November 2013

[98] Holy *Quran*, 'Surah Ar-Rum' Chapter 30, Verse 39 (quran.com) <http://quran.com/3> accessed 11 November 2013

[99] Holy *Quran*, 'Surah An Nisa' Chapter 4, Verses 161 to 162 (quran.com) <http://quran.com/3> accessed 11 November 2013

- *"Those who consume interest cannot stand [on the Day of Resurrection] except as one stands who is being beaten by Satan into insanity. That is because they say, "Trade is [just] like interest." But Allah has permitted trade and has forbidden interest. So whoever has received an admonition from his Lord and desists may have what is past, and his affair rests with Allah. But whoever returns to [dealing in interest or usury] - those are the companions of the Fire; they will abide eternally therein.*
- *Allah destroys interest and gives increase for charities. And Allah does not like every sinning disbeliever.*
- *Indeed, those who believe and do righteous deeds and establish prayer and give zakah will have their reward with their Lord, and there will be no fear concerning them, nor will they grieve.*
- *O you who have believed, fear Allah and give up what remains [due to you] of interest, if you should be believers.*
- *And if you do not, then be informed of a war [against you] from Allah and His Messenger. But if you repent, you may have your principal - [thus] you do no wrong, nor are you wronged.*
- *And if someone is in hardship, then [let there be] postponement until [a time of] ease. But if you give [from your right as] charity, then it is better for you, if you only knew.*
- *And fear a Day when you will be returned to Allah. Then every soul will be compensated for what it earned, and they will not be treated unjustly."*[100]

As one can witness, the words from God are very clear about Muslims taking usury, such as *riba*. Not only are we informed clearly that *riba* is not allowed, but also the taking of the same would be penalised severely. God has mentioned clearly that a Muslim is

[100] Holy *Quran*, 'Surah Baqarah' Chapter 2, Verses 275 to 281 (quran.com) <http://quran.com/3> accessed 12 November 2013

allowed to ask for the return of the main sum that was initially lent, but it is considered that Muslims who ask for interest have declared war against God and His messenger, Mohammed (pbuh). There are a number of rationales behind the prohibitions of charging of interest such as exploitation of the weak, making money out of money without doing anything; but, more importantly, as mentioned above, in comparison to transactions where God has allowed trading to take place to make money, making free money doing nothing is strictly prohibited.

The prohibition of *riba* is not only strongly mentioned in the Holy Quran, but also in the *hadiths* of Prophet Mohammed (pbuh). It is considered as one of the seven restrictions set by Prophet Mohammed (pbuh) which are: (a) Not considering one God; (b) Making magic; (c) Unlawful killing; (d) *Riba;* (e) Unlawful appropriation of orphans wealth and inheritance; (f) Not going to war when called for faith; (g) Not considering bad scandals against unchaste women.[101] It is worth mentioning a few of these to assist in understanding the gravity of the prohibition of *riba* in Islam and also, more importantly, in understanding the solutions proposed, as shall be witnessed later. Jabir mentioned that:

- *"The Prophet (pbuh) cursed the receiver and the payer of interest, the one who records it and the witnesses to the transaction and said: 'They are all alike [in guile]'."*[102]

Additionally, is has been mentioned in the chapter on Riba, Kitab al Musaqat, Muslim, 1981, the Prophet Mohammed (pbuh) mentioned:

- *"Gold for gold, silver for silver, wheat for wheat, barley for barley, dates for dates and salt for salt – like for like, equal for equal, and hand to hand; if*

[101] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) p. – 211
[102] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) p. – 46

commodities differ, then you may sell as you wish, provided that the exchange is hand to hand."[103]

As the above expresses, like for like in exchange is what has been advised by Prophet Mohammed (pbuh) and, if the mediums are different, then transactions are allowed as God has allowed trading. A couple of the most important *hadiths* that underline the *riba* aspects are as follows:

- On one occasion, one of Prophet Mohammed (pbuh) apostles, Bilal, visited the Prophet with good quality dates and Prophet asked about the source. Bilal informed that he exchanged two volumes of poor quality dates for one volume of high quality dates. The Prophet mentioned, "*This is precisely the forbidden Riba! Do not do this. Instead, sell the first type of dates, and use the proceeds to buy the others.*"[104]

- One another occasion, a man who was assigned to collect the zakat brought for Prophet Mohammed (pbuh) some good quality dates from Khyber. Upon enquiry whether all the dates of Khyber are similar, the man informed that he exchanged an amount of this kind of dates for two or three amounts of another kind. The Prophet informed, "*Do not do so. Sell (the lower quality dates) for dirhams and then use the dirhams to buy better quality dates. (When dates are exchanged against dates) they should be equal in weight.*"[105]

Therefore, as this can be clearly established, where a barter takes place it must be like for like. However, if profits are to be made, it must be through clear transactions where monies are used as a medium and the parties are aware of the position clearly. All this goes well in line with God's command as mentioned above "*...But Allah has permitted trade and has forbidden interest...*" Otherwise, it would be considered *riba*.

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[103] Ibid
[104] Ibid
[105] Ibid

There are different types of *riba,* namely *riba al-nisah,* which deals with exchanging money for more money transactions due to delay in time and performance, e.g. in loans, and *riba al-fadl* which deals with barter transactions, where it has been instructed to use money as the medium so as to avoid any unjust increase.[106] It is necessary to make the above points very clear in this chapter as it expresses one of the principal reasons for the restriction of Muslims in entering Western contracts; also, as will be witnessed in later chapters, proposals have been discovered in this thesis that can be utilised to make the working mechanism of Western insurance *halal* as the proposals go around the prohibitions of *riba*. It is felt that, at this point, it might appear that the Islamic perspective of *riba* to non-Muslims might represent an unnecessary burden. So, it would assist both, in the interest of perusal and to emphasise the importance of prohibition of *riba,* that a short analysis of the rest of the world be considered so as to complete the picture.

5.2. Analysis under other religious and jurisdictional views:

Over time there have been arguments between various groups as to whether it is correct to charge for usury. Even before the birth of Jesus Christ, the Greek philosopher Aristotle concluded that, unlike property, money itself cannot be destroyed, rented, change value or reproduced and, therefore, cannot be used to provide back excess of what is lend, as such practice would be usury which was not allowed. Roman law allowed interest provided risk was taken except for voyages with rates initially set at 12%, but later changed to a sliding scale.[107]

However, Christianity appears to have had strong objections against usury and interest. In numerous Christianity-related scriptures, this aspect has been frowned upon. In the Old Testament in the Book of Exodus, section 22 paragraph 25, it is mentioned that, where

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[106] Zamir Iqbal and Abbas Mirakhor, *An Introduction to Islamic Finance: Theory and Practice* (2nd edn, John Wiley & Sons Asia Pte. 2011) pp. – 58 – 59

[107] Economic History Association, 'Analysis on usury' (eh.net) <http://eh.net/encyclopedia/article/jones.usury> accessed on 28 May 2014

funds are provided to the poor, the lender is not a usurer and he is not to charge usury.[108] Similarly, in the Old Testament in the Book of Deuteronomy, section 23 paragraphs 20 and 21, it is mentioned that usury is not allowed among "*brothers*" and the borrower must pay back when agreed.[109] Additionally, reference against usury was stated in the Old Testament in the Book of Ezekiel, section 18 paragraphs 7 and 8, and again in the Old Testament in the Book of Leviticus, section 25 paragraphs 35 and 36.

It appears that, over time, people's views on usury started to change, particularly from the early 15th century onward. Well-known scholars and individuals of the time, such as Jean Gerson, Conrad Summenhardt, Gabriel Biel and John Eck, stated that, where the aim of the lender is to oppress the borrower, the usury applies, otherwise taking of ususry is acceptable. John Eck argued 5% was an appropriate amount for genuine businesses and so structuring the association as a charitable relationship is fine for usury to work on. This intension test was strongly disputed by others such as Philipp Melanchthon and Martin Luther, the latter even arguing usurers were equal to thieves and murders.[110]

At the same time, scholars such as John Calvin on 1545 argued that one should look at the circumstances of an individual to determine issues of interest and considered looking into the meaning of usury, which could possibly originate from two translated Hebrew words, "*neshek*" and "*tarbit*" meaning "to bite" and "to take legitimate increase". Thus, he concluded that the former type of loan is prohibited, but lending to businesses that can make a profit is acceptable so long as they do not charge the poor and impoverished. Matters developed further with scholars such as Charles Du Moulin, Domingo De Soto and Luis de Molina, who disagreed with Aristotle's views; they even attacked sections of the Gospel of Luke in the Bible, as the Bible does not mention it is wrong to charge interest.

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[108] Bible on the Web, 'Holy Testaments' <http://www.bibleontheweb.com/bible/KJV/Exodus-22> accessed on 28 May 2014

[109] Bible on the Web, 'Holy Testaments' <http://www.bibleontheweb.com/bible/KJV/Deuteronomy-23> accessed on 28 May 2014

[110] Economic History Association, 'Analysis on usury' (eh.net) <http://eh.net/encyclopedia/article/jones.usury> accessed on 28 May 2014

All these movement caused in the second part of 16th century to allow interest charging loans to be acceptable and lawful. It was stated that the interest charging loans to be provided with good intentions and the state would not interfere unless it was considered to be antisocial. On the other extreme, the usuers were referred in the literatures as "socially inept fools"[111] rather than evil. By the 17th century, it was becoming the norm for interest to be acceptable and countries were concerned about the rate of interest. The UK parliament approved a rate of 8% in 1624 from the 10% rate set in 1571, going as far as announcing that such usury did not interfere with God's law. To date, the statutory judgment interest rates at courts are set at an 8% rate of interest as per s. 69 of the County Courts Act 1984. By the 18th century, usury was viewed as morally acceptable and the public considered that it is acceptable to make money out of money either by collateral or normal banking. However, there were disputes among Catholics about the validity of charging usury up until early 19th century, when Roman Congregations ruled to allow usury, but this lead to the socialists considering usury as the "*new slavery*".[112]

As mentioned earlier, although it may appear that this thesis portrays religious studies rather than concentrating on the topic in hand, it is very important that the *Sharia* points are made clear, as they explain the reluctance of a Muslim to enter traditional insurance and, essentially, describe models that can be designed to circumvent these restrictions. Also, there is a reason behind the need to look into the scriptures on *riba* from a Christianity point of view. It is not only because, from a religious viewpoint, Jesus Christ is considered by Muslims as one of the prophets of God, so his views are respected and regarded by Muslims; but, more importantly, if this paper is to propose amendments for the future of marine insurance in order to make it compliant with *Sharia* law, it would simply be unfair to satisfy only Muslim needs, leaving aside the remaining individuals of faith, given that Christianity is the biggest religious sect in UK, comprising about 72% of

[111] Economic History Association, 'Analysis on usury' (eh.net) <http://eh.net/encyclopedia/article/jones.usury> accessed on 28 May 2014
[112] Economic History Association, 'Analysis on usury' (eh.net) <http://eh.net/encyclopedia/article/jones.usury> accessed on 28 May 2014

the UK population.[113] As can be witnessed from the above viewpoints, usury has been a concept of arguments between generations of human beings, not only from a religious viewpoint but from a scholarly concept as well.

6. Relevance of *riba* concept to insurance:

The *riba* concept mentioned above is relevant to the aspect of traditional marine insurance being considered by the Islamic society. The concept that is of concern is that the Insured makes payment of a premium, which is a minimal amount compared to the compensation he gets to receive, when he make a claim. To be precise, this relates to the concept of *riba al-naisah*, which is basically the restriction set by the *Quran* and *hadith* on making money out of money. More specifically, this is exactly the opposite of what happens when one takes a loan and usury is charged. The reverse would be true as well and would once again fall under the restrictions of *riba* as, in that case, the insurer would be making money without committing anything, as is the way with traditional marine insurance. An example might assist in understanding the position clearly.

As an illustration, let it be assumed that the insured agreed to pay £x premium to the insurer for the marine voyage, depending on the arrangement, either one-off or for every month for y months until the goods reach the destination port. The insurer has set out the risks that the insured is covered for. In the unlikely event the goods are lost during the voyage, provided it is one of the insured perils, the insurer would have to pay the insured a significant amount of compensation, say £z. This £z would at all times be more than the £x that the insured had been paying to the insurer. There is a clear *riba* in this respect, as the insured did not actually do anything to receive the money from the insurer. It can be argued that the insured lost his goods in the voyage, hence he is being compensated. Whilst that is correct, it still that does not answer the question why the insurer is paying for the loss of the insured. The former is not in a transaction for the goods with the latter, so why should the former be held liable for this? In this aspect, the insured is simply

[113] Free Enterprises, 'United Kingdom Census 2001 – Religion' (2001 free-enterprises.co.uk) <http://www.free-enterprises.co.uk/Religion-Statistics/Office-of-National-Statistics/Census-2001/> accessed on 29 May 2014

making more money, i.e. £z out of £x, without doing anything in return, which is considered *riba* and is unacceptable under *Sharia.*

On considering a reversal scenario, the goods do reach the destination point without losses. In that case, the insured cannot ask for the return of compensation, i.e. £z amount, neither can he ask for the return of his premium, i.e. £x, as the insurer would argue that he undertook the risk and that was the contract between the parties. So, in this case, again the insurer is making money, i.e. £x out of doing nothing. It can be argued that the insurer took the risk so justifies the premium, but the risk taking in such cases is simply *gharar,* which is another *Sharia* prohibition, as shall be seen below; parties cannot enter into a contract where there is too much high uncertainty involved, thus no one knows the outcome. The insurer undertook to cover insured risks wholly on him for some events he did not even know what, when or if those events would happen. It is similar to going to a fortune-teller and asking to read the tarot cards, where the fortune-teller simply picks cards at random and make predictions with no basis whatsoever. The events mentioned by the fortune-teller might or might not happen but there is no guarantee. Therefore, the insurer has now made £x money, which is *riba,* even though nothing has been provided in consideration for the same.

It is felt that at this point it is necessary to co-relate issues on trading with *riba.* As mentioned above, in *Surah Al Baqarah*, Chapter 2, Verses 275 "*...That is because they say, 'Trade is [just] like interest.' But Allah has permitted trade and has forbidden interest.*"[114] In Islam, there needs to be certainty in contracts that parties enter. There needs to be a clear pathway on who has what responsibility and what will happen if they make a business loss or profit. Everyone who is involved gets rewarded if the joint enterprise makes a profit and the same is applicable should the enterprise make a loss. Unlike insurance, where there is no reward for the insured if there is no claim,[115] *Sharia*

[114] Holy *Quran*, 'Surah Baqarah' Chapter 2, Verses 275 to 281 (quran.com) <http://quran.com/3> accessed on 6 June 2014

[115] The researcher is aware that insurer attempts to reward the insured by offering "no claims bonus" but this is just another marketing strategy rather than rewards being reaped from the transaction.

approved financial instruments work on a risk/profit sharing basis.[116] It is based on the Islamic maxim of "*al ghunm bil ghurm*" which essentially means that there is "no return without risk."[117] Risk in business is acceptable in Islam and is dealt with in more detail in the *gharar* section later. However, risks in relation to uncertainty of the contract, whether one party is in for a loss on an unknown event, is simply unacceptable under the *Sharia* law.

7. Conclusion:

In conclusion, as mentioned above, prohibitions of *riba*, *gharar* and *maisir* restrict traditional insurance from being acceptable in Islam. In this chapter, discussion has been made on *riba,* keeping in line with its impact on traditional marine insurance. *Riba* certainly possesses a threat to the development of Islamic insurance models, as any unjust enrichment falls under this vital trap making it *haram*.[118] This leads to the suggestion of whether a marine insurance model can be proposed, which would justify enrichment under Islamic law and whether such enrichment can be allowed or controlled within the ambit of Islamic law. If such features can be contained then, perhaps, there is a hope of a way forward for a *halal* marine insurance model, as the restriction of *riba* can be sidestepped, which would validate enrichment without breach of the sacred provisions. Upon further perusal of the thesis, it would become evident that the various *takaful* models portraying *Sharia* compliant insurance are, in fact, filled with significant problems in themselves. This, in essence, raises significant doubts over whether the cost of sacrificing traditional insurance is too steep, simply for the apparent satisfaction of illustrating that *riba* is being avoided.[119] However, it is opined that that there could be an innovative way forward for avoiding *riba*, even when using the working mechanics of

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[116] Zamir Iqbal and Abbas Mirakhor, *An Introduction to Islamic Finance: Theory and Practice* (2nd edn, John Wiley & Sons Asia Pte. 2011) p. – 65

[117] Bank Negara Malaysia (Central Bank of Malaysia), 'Risk and return in Islam' (bnm.gov.my) <http://www.bnm.gov.my/files/publication/fsps/en/2013/cp02_003_box.pdf> accessed 17 November 2014

[118] In fact, strictly following concept of *riba* causes an issue for other faiths as well as mentioned above. However, this thesis would be concentrating on the Islamic viewpoint on marine insurance and current chapter is about *riba*. Considering other faiths, save making references, would take it outside the scope of this thesis.

[119] See chapter 5 below where the researcher discusses about various Islamic insurance alternative known as *takaful* and evidences the various gaps existent with those present *takaful* models

traditional marine insurance and without trespassing the ambits of the divine guidelines, which become unravelled as one progresses along the various chapters of the thesis.

Considering the scenario explained above, the issue of *riba* appears to attack primarily the concept of premium and compensation. This is due to the imbalance of the amount of payment, such as in the event when a claim is made, when compensation is more than the premium amount paid. Conversely, in the event when a claim does not take place, the premium amount is more than the compensation, since no compensation is paid at all. Therefore, it is believed that a platform could be invented, where the interdependency bond shared between premium amount and compensation payment can be strategically separated, yet keeping both of the concepts within the same legal environment. Therefore, this would lead to a condition where the concepts would coexist in the same ambience, but independently, then the imbalance argument of enrichment would have no place to argue. Therefore, the concepts become distinct enough for avoiding *riba* to crop into the equation, but still close enough to coexist in the same atmosphere. This could lead then to a situation, at least in respect of *riba*, where the requisites, both jurisdictionally and from a *Sharia* point of view, are satisfied and there could be a way forward for further commercial advancement. In fact, such is the working analogy for the elimination of *riba* concerns that are behind the proposed *takaful* model, as would be witnessed later on in this-thesis.[120] The idea is, quite simply, that the presence of *riba* will not allow traditional marine insurance to be *Sharia* compliant, and so any insurance model should eradicate the presence of *riba* in its model. The proposed *takaful* model is to find an alternative way so that the premium amount stays in its own circle and the compensation payment stays in its own circle, unrelated to one another, yet within the same platform, so that the marine insurance instrument could work in a *halal* prerogative.

[120] See chapter 7 below where researcher talks about his proposed *takaful* model which can eliminate the *riba* issue but still can be implemented into traditional marine insurance working structure

Part II

The restrictions prohibiting traditional insurance acceptability in Islam

Chapter 4: *Gharar* (Uncertainty) and *Maisir* (Game of chances)

1. Introduction:

In this chapter, consideration will be made of the other two restrictions that hinder traditional insurance from being allowed under Islamic law. Analysis will be made of the concepts of *gharar* and *maisir*. The concept of *gharar* deals with the aspect of uncertainty of the insurance contract, while *maisir* deals with the characteristic of insurance, which is similar to gambling due to the presence of the improbability of whether a claim would be made or not.

2. *Gharar*, the concept:

The second restriction after *riba* that threatens traditional insurance from being within the ambit of Sharia provisions is the concept of *gharar*. Whilst *riba* is a major restriction, *gharar* is no small hurdle either; to make things more complicated, the number of texts on *gharar* are even less than that on *riba*. *Gharar* is an Arabic word that literally means "*fraud*"[121] but, in terms of business, it means "*risk, uncertainty and hazard*".[122] Moreover, *gharar* finds its roots from the word "*ghr*", which means "*to deceive or fog the mind*".[123]

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[121] Mohammad Hashim Kamali, *Islamic Commercial Law: An Analysis of Futures and Options* (Islamic Texts Society 2010) Chapter 8, Uncertainty and Risk-Taking (*Gharar*) in Islamic Law. Notes and Handout of Professor Shahid Ebrahim, Bangor University Business School, Winter 2012

[122] IMA, 'International Standards for Islamic Finance' (2008 kantakji.com) <http://www.kantakji.com/fiqh/Files/Fatawa/A303.pdf> accessed 7 March 2013

[123] Abdulkader Steven Thomas, 'Gharar: Deception in Financial and Business Relationships, What is Permissible now!?' (1995) The Muslim Converts Association of Singapore, p. 16, Chapter 2 - Notes and Handout of Professor Shahid Ebrahim, Bangor University Business School, Winter 2012

The aim of *gharar* prohibition is to avoid unfairness in a contract due to cloudiness in the contract on obligations. Various authors have mentioned *gharar,* but the most commonly preferred view is that *gharar* relates to the improbability of a contract due to the presence of ambiguities regarding the object of the contract, i.e. subject matter or price, as they are non-existent at the present time. As such, the consequences of the same are simply unknown to either of the parties. Alongside, subjecting the object of a contract by linking it to a variable (which may or may not happen), as such the factor being outside the ambit of parties, makes a contract contain *ghrara.* As mentioned above, *gharar* also refers to fraud and deceit; however, for the context of this thesis, it would be confined with the aspect of uncertainty as in commercial transactions. Examples of *gharar* could include selling someone birds in the sky or fishes in the river, where the quantity is unclear to either party, i.e. buyer or seller.

An established definition has been provided by the late Professor Mustafa Al-Zarqa, who explained *gharar* as "the sale of probable items whose existence or characteristics are not certain, the risky nature of which makes the transaction akin to gambling".[124] In simple terms, whenever there is any kind of lack of information leading to uncertainty and risks in the contract, elements of *gharar* are considered to be present. As can be noticed from the definition itself, *gharar* has been linked to gambling, i.e. *maisir* and this is considered in detail below along with religious laws. Upon considering the above, it may appear that double standards have been applied here.

On one hand, Islam restricts money being made without risk, leading to *riba* restriction; yet, on the other hand, Islam restricts risks being taken at all in the contract. It is important to note that not all risks are considered under the umbrella of *gharar.* Business risks are considered to be acceptable under *Sharia* and the risks that the investor takes in a business is not considered *gharar.* This is because risks in sales[125] are considered to be risks that are part of life and such risk-taking is necessary to make the return *halal,* otherwise the return could be considered as *riba,* e.g. interest being paid in the bank

[124] Mohamud A. El-Gamal, *Islamic Finance: Law, Economics and Practice* (Cambridge University Press 2009) p. - 58

[125] May it sale of goods or services, as is relevant to the thesis here

account of account holders, where they do not take any risks. To be more precise, in the case of this thesis, it is the insured that is getting paid the compensation without personally taking on any risks in the contract between him/her and the insurer.

The principal point of *gharar* in this respect is the item in question, its quantity, its quality, obligations of each party on their respective duties and the actual condition of the items; all of these variables must be specific in order for the sale contract to avoid *gharar*. In this analogy, *jahl,* i.e. ignorance, must be avoided in contract to make it *gharar* free. In fact, it has been considered by the *fuqaha* that, in the modern world, all individuals live with some *gharar,* therefore it will always be present and it is almost impossible to eliminate *gharar* in its entirety. Therefore, *gharar* has been distinguished into major and minor *gharar*. The former rescinds the whole contract, while the latter could be borne as an acceptable "necessary evil".[126]

3. Conditions for the presence of *gharar*:

It has been nicely set by Professor Al-Darir that four conditions need to be present for *gharar* to destroy a contract, which are as follows:

(1) That the *gharar* present is extreme and not minor.[127] An example of minor *gharar* could be that, the colour of the goods provided is not the right type of shed of that particular colour.[128]

(2) That an affected contract is connected to financial aspects, for example a sales contract.[129]

[126] Mohamud A. El-Gamal, supra at p. – 58
[127] Mohamud A. El-Gamal, supra at pp. – 58 - 59
[128] Of course, it goes without saying that if the right colour shed of the goods are a condition of the contract and that has not been specifically clarified between the parties beforehand and it becomes an issue in relation to payment (as stated in the next point), then it becomes a major *gharar*.
[129] Ibid

(3) That *gharar* is affecting the heart of the contract, e.g. subject matter or price.[130] For example, the price of a necessary domestic animal, like a cow, would be higher if the cow is pregnant with a calf. However, it is not possible to make a contract on the sale of the unborn calf as neither of the parties knows how the calf will be born, therefore the sale of calf would be *gharar*.

(4) If the excessive *gharar* contract is necessary to meet a need, then it can be allowed. This last point is more of a very narrow exception of the principal decree rather than a rule. For example, the Prophet Mohammed (pbuh) has allowed as an exception that *Salaam* contract is *halal* and can be utilised where the sale items are delivered later in the contract, even if the price is paid in advance.

Detailed discussion shall be made about *Salaam* contract in more detail later on, as it forms part of the proposed solution for the current problem in hand. However, *fuqaha* has already made rulings that traditional insurance contracts do not fall under this narrow exception of point (4), of public need, and is considered *gharar* due to the satisfaction of the other three points mentioned above.[131]

Considering Professor Al-Darir points above, it is very obvious that he has tried to express the presence of *gharar* in the modern world and has attempted to limit its scope and allow flexibility. However, it must be kept in mind that God has ordained restrictions of *gharar* in contracts for the good of mankind and, whilst a similar view is shared, that minor *gharar* might be acceptable, perhaps Professor Al-Darir's over-optimistic approach might be scrutinised as an approach that is somewhat far-fetched from God's set parameters. Professor Thomas makes an interesting analogy in this respect, stating that *gharar* in the Islamic community is not about selling the "unknown or non-existent", but it relates to the concept of selling "the unpredictable" or "uncontrollable" and "without

[130] Ibid
[131] Ibid

knowledge".[132] The argument is one of whether the seller can actually satisfy his obligations under the contract that he is entering into; for, in reality, he does not know if he can or cannot, or he does not know of his obligations because they are outside his remits, or he simply does not have any idea what he is getting into. Upon reflection of this, it becomes obvious why the Islamic community frowns upon traditional insurance, but a detailed example is given later to clarify the position even more.

Additionally, another well-known scholar, Ibn Taimiyah, has reasoned that, "*Gharar* found in the contract exists because one party acquired profit, while the other party did not".[133] This is similar to the principle of "pareto optimality", an economics theory set by the Italian economists Vilfredo Pareto, which basically states that one may only benefit from the price of the loss of at least another.[134] The Islamic society has, rightly or wrongly in respect of their own views, been viewing traditional insurance under the specs of the above definition closely (although, perhaps not in hindsight of Vilfredo Pareto's optimality principle) which, unfortunately, has hindered *Sharia* advancement in this field. It is felt that, whilst the above definition of *gharar* is correct, traditional insurance might not be correct when considered in the same analogy. Insurance in itself is not a tool to make gains, but to compensate for whatever wrong has occurred to another. Whilst it would be correct that the functioning system of the traditional marine insurance might not be *Sharia* compliant, the concept itself is not *haram*. In short, if the aspects that are considered as parasites reflecting insurance as *haram* can be removed from the traditional insurance concept and re-modelled without these parasites, then there should be no reason why the traditional English marine insurance cannot be considered as *halal*. While this is the view being put forward in one sentence, ~~and~~ this thesis would aim to argue along those lines, along with proposals for the marine insurance future.

4. Comparison of *gharar* to Western society:

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[132] Abdulkader Steven Thomas, 'Gharar: Deception in Financial and Business Relationships, What is Permissible now!?' (1995) The Muslim Converts Association of Singapore, p. 16, Chapter 2 - Notes and Handout of Professor Shahid Ebrahim, Bangor University Business School, Winter 2012

[133] Institute of Islamic Banking and Insurance, 'Takaful Islamic Insurance' (islamic-banking.com) <http://www.islamic-banking.com/prohibition_of_gharar_masir_riba.aspx> accessed on 10 June 2014

[134] Library of Economics and Liberty, 'Pareto optimality consideration' (econlib.org) <http://www.econlib.org/library/Enc/bios/Pareto.html> accessed on 10 June 2014

With all the texts mentioned regarding the severity of this principle of *gharar*, it may be felt that this is an alien concept that this thesis is trying to compel onto the Western culture, which simply does not fit in and hinders the project in hand. However, the contrary is argued instead; should one look into the structure of the Western community, one would see the presence of the *gharar* principle very much existing but in a different cloak. It would be worth looking into the concept from the financial perspective of a Western community.

For instance, whenever, any person wants to take out a financial product such as a bank account or, more related to this context, insurance from a broker or from the insurer direct, the financial advisor is under a duty to conduct his due diligence. Therefore, we would ask, what is this due diligence? A due diligence, in short, is a procedure that ensures, by verification and checking, that the customer or prospective insured is who they say they are. That begs the next immediate question, why is there a need to do the same? The simple answer is to make sure the financial provider is not getting involved in such a transaction he/she is not sure about, as such to avoid the uncertainty and risk leading to the consequences of the unseen or unknown.

In similar lines, perhaps consideration should be made to the concept of litigation, whether it be civil or even criminal. The reason being, part of the present-day Islamic insurance, *takaful,* has one of its defects in line with a Western litigation perspective. In litigation, the parties are under a duty for early disclosure of supporting evidence in relation to their respective cases. The supporting evidence does not mean the evidence that supports that particular party's case only, rather supporting evidence includes evidence that might even hinder or undermine their respective case. In civil cases, **Rule 31.6 of Civil Procedure Rules** subsections defines clearly that the following disclosures must include, "*(i) adversely affect his own case; (ii) adversely affect another party's*

case; or (iii) support another party's case".[135] Also, the duty of disclosure is on-going, which means that, through the course of litigation, when either party finds supporting evidence, they are to disclose the same in line with the above principles of the Civil Procedure Rules.

This further begs the obvious question once more, why the need for disclosure and how is this relevant to *gharar*? The answer is actually very simple, in that the procedure has been set in the heart of English legislation so that the parties and the judiciary are well aware in advance of what the concept is here and the evidence in support of that. Supporting evidence will either support or hamper either side, but either way it would give certainty to the disputed issues. If not, then there is a significant risk that there would be unexpected surprises in the trial, which will hinder the sides from reaching a fair result with such certainty. The disclosure rules are there so that the parties are aware of the situation they are getting into, so that the nothing unforeseeable would happen when the matter reaches trial.

Even if the trial judge decides the matter one way or another, the result would always be reflected on the disclosures already provided and not on aspects that are unknown or uncontrollable or without knowledge. One can immediately co-relate to the point that this thesis has been trying to emphasise to avoid *gharar,* in order to to remove the veil of uncertainty, so that the associated parties know exactly what they are here for. With litigation, the same has been utilised for centuries now. Other examples can include insider trading regulations set by the Financial Services Authority and fair contractual regulations in statutes such as **Unfair Contract Terms Act 1977** or **Sale of Goods Act 1979**; other examples include the equity maxims that have been utilised, such as "*caveat emptor*", meaning let the buyer beware, which advises the buyer must conduct their due diligence before concluding the transaction. In light of these arguments, it could be illuminated that the existence of *gharar* has been present in the Western community for much longer than one believed and is not a foreign paradigm, rather an enforcement of

[135] Justice, 'English Civil Procedure Rules online' Rule 31.6, Standard disclosure – What documents are to be disclosed (justice.gove.uk) <http://www.justice.gov.uk/courts/procedure-rules/civil/rules/part31#IDAAT0IC> accessed on 10 June 2014

the underlying foundations. The following are just a few examples of the essence of *gharar* presence in the Western community, which further reinforce the concept.

5. Relevance of *gharar* concept to marine insurance:

It might be of grave assistance to demonstrate the effects of *gharar* in the functioning rules of insurance to make the matters explicitly clear. A traditional marine insurance contract is made with the aim of getting the insured compensated by the insurer should one of the insured perils take place. More simply, if some sort of defined catastrophe occurs, e.g. hurricane, tornado, pirates, etc., and one of these causes a loss, then the insurer would pay the insured for the loss sustained. In principle, the concept is legitimate even from a *Sharia* perspective, in that one party compensates the other party for loss sustained. But what makes things *haram* is mainly due to the fact that none of the parties know whether a hurricane or tornado would take place, or if pirates would attack. Say, for the sake of argument, it is taken that those disasters are unknown to humans and are sidestepped, or that they form minor *gharar* and are considered acceptable. However, even then there is a bigger *gharar* existent as none of the parties know if or when, or how much loss would be sustained, which can lead to the uncertainty in the contract.

As an example, the insured has obtained marine insurance cover on his goods from the port of departure to the point of destination which, of course, requires a marine voyage over water. In line with the earlier example, the insured has paid £x premium to the insurer. Now, if one of the insured calamities takes place, as mentioned above, and for the sake of argument it is taken that the calamity is a minor *gharar*, yet there is no way to find out if damage will take place. Just because a catastrophe takes place, it does not mean there would always be damage. For some calamity would be minor enough not to cause any suitable damage of concern. Even if it is taken that damage would be caused every time there is a catastrophe, there is no way to determine the extent of the loss due to that catastrophe. A hurricane can destroy the vessel, but it might be possible to rescue all the goods safely from the bottom of the sea, or a fire may have taken place, but

perhaps the fire was contained in time and the damage was negligible. This uncertainty in relation to causation raises a major *gharar* problem in itself to the insurance analogy.

This is because causation is directly proportional to the insurer's payout, which, in line with the above example, is £z. If the loss is little, the payout might be little; if the loss is substantial, then the payout would be more. Without a doubt, the payout would never exceed more than 100% of the cover that is set against the value of the goods. However, there is no way to determine the insurer's responsibility of the payout, i.e. how much of the £z the insurer needs to pay out. In other words, it is not possible to determine before the said catastrophe what would be the percentage of the indemnity cover that the insurer would be held accountable for. Additionally, as with the marine insurance practice in the UK, when the insured is claiming compensation, he would ordinarily have to make an excess payment of £a. This £a excess would have to be paid when the claim is made and to be pursued. Once more, the insured is now at the mercy of a determination factor, which is something unspecific or uncertain, and so the parties' obligations are unclear, as such making the traditional marine insurance functioning procedure *haram* due to the presence of *gharar*.

6. Religious laws:

As stated earlier, texts on *gharar* are very limited compared to *riba*. Sale contracts of *Mulamasah* and *Munabadhah* are contracts that have an uncertainty element in them. Imam Malik (1985, pp. 423-424) has defined these two types of contracts with an example that highlights the *gharar* element. He has explained as follows:

"*Mulamasah is when a man touches or feels a garment, but does not unfold it nor ascertain (its character). Munabadhah is when a man throws to another a garment in exchange for a garment that the other throws to him without both of them examining them.*"[136]

[136] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 143 - 144

In line with the above, the argument highlights that, in both cases of the different types of *gharar* related sale, contract items are being transacted without ascertaining the features of the object of sale, which forms the heart of the contract. Parties are entering blindly into a business relationship uncertain of the future outcome in relation to the products and obligations. As mentioned earlier, texts on *gharar* are much more restricted comparatively and are much more literal, thus consideration is needed for clarification as expressed above. A number of authors, including Aly Khorshid, have combined the concept of gambling under the heading of *gharar*. Aly Khorshid goes on to deal with the aspects of probability arguments in his chapters on *gharar* and portrays this to be under the same heading.[137] However, it is asserted that the comment in relation to probability and chance is to do with the doctrine of *maisir*, which is a different concept in itself, as will be discussed below. Although the two concepts may go side-by-side, they are distinct and require individual emphasis.

7. *Maisir*, the concept:

In line with the above analogy, it is now necessary and relevant to mention that the concept of *gharar* is interrelated with the concept of *maisir*. *Qimar* is also sometimes used as a synonym to *maisir,* although they are not the same, but both of them are used to explain the concept of *maisir*. *Maisir* means obtaining wealth by chance without caring whether the same would amount to depriving someone else. For example, in gambling one of the gamblers may make money without considering whether he wins the next hand and, if so, he would take someone else's wealth; or, if he loses, someone else will take his wealth, all of which is determined by chance. *Qimar* means a chances game, where one gains wealth at the loss of another, as such relating to speculation; for example, in gambling, which is a game of chance, on accruing or losing money in the next hand.

Although the two concepts are slightly different, they are not far apart in relation to the subject matter that is being analysed in this thesis. To avoid any confusion during

[137] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004), pp. - 38 - 43

consideration of this paper in relation to the connection between *gharar* and *maisir*, *gharar* relates to the aspect of uncertainty, where the consequences are unknown. Subsequently, following the path of *gharar* leads to the sin of *maisir*, where the individual becomes involved in a transaction similar to a game of chance, as he/she does not know the outcome of the next set of events.

Muhammad Ayub puts it nicely in his book about the origin of *maisir,* which came from the word "*yusr*", which means having something conveniently without paying appropriately, either in hard work or monetary, or without responsibility of the same, by means of chance. *Qimar* means receiving some kind of benefit including monetary, by way of chance, at the expense of another. Although Muhammad Ayub does talk about the very basic religious aspect of *maisir* and *qimar* in his paper, he emphasised that a lottery transaction has the presence of the *maisir* related concepts that cause the lottery-related business to be unlawful under God's laws. He goes on further to discuss the banking principle and insurance concept and points out that the presence of *maisir* causes the disproportional standing of parties in the financial transaction.[138] Muhammad Yusuf Saleem, who explained *maisir* as easily obtaining something without any effort, sets a similar definition.

8. Religious Laws:

God has mentioned explicitly in the Holy Quran in *Surah Al – Ma'idah* (Chapter 5), Verses 90 and 91, that:

- "*O you who have believed, indeed, intoxicants, gambling, [sacrificing on] stone alters [to other than Allah], and divining arrows are but defilement from the work of Satan, so avoid it that you may be successful.*

[138] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 61 - 63

- *Satan only wants to cause between you animosity and hatred through intoxicants and gambling and to avert you from the remembrance of Allah and from prayer. So will you not desist?*"[139]

Additionally in the Holy Quran in *Surah Al – Baqarah* (Chapter 2), Verse 219, it is mentioned that:

- "*They ask you about wine and gambling. Say, "In them is great sin and [yet, some] benefit for people. But their sin is greater than their benefit." And they ask you what they should spend. Say, "The excess [beyond needs]." Thus Allah makes clear to you the verses [of revelation] that you might give thought.*"[140]

As the above paragraph mentions, God has strictly denied *maisir* and, as such, *gharar*. According to God's laws, any situation, where the ultimate outcome is to be determined by circumstances unknown to either of the parties, then it would be categorised under the restrictions of *maisir*. On the paragraphs from the divine book mentioned above, it is not just hinted but, rather, clearly pointed out that activities, such as gambling or divining arrows,[141] where the individual does not know what he/she is entering into and what the outcome of his/her action would result in, have been prohibited.

It may be argued by some that, irrespective of the bad effects of entering transactions with *maisir*, there are good points, in that it raises competition and, at the end, there is a beneficiary and the wealth goes into circulation without remaining idle. Whilst it is true that there are some benefits, as God has already pointed out in *Surah Al – Baqarah* (Chapter 2), Verse 219 above, the detriment outweighs the benefits. That happens

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[139] Holy *Quran*, '*Surah Al – Ma'idah'* Chapter 5 Verses 90 and 91 (quran.com) <http://quran.com/5> accessed on 21 March 2014

[140] Holy Quran, '*Surah Al – Baqarah'* Chapter 2 Verse 219 (quran.com) <http://quran.com/2> accessed on 21 March 2014

[141] Diving arrows was one of the activities, which the Arabs practised, in the dark ages before Prophet Mohammad was given guidance by Allah on the Holy Quran. The Arabs of those times used to take arrows and shot, for deciding various issues, with uncertainty of the outcome e.g. deciding what to do next or who will take what. Allah has forbidden such activities as these are, just like gambling, activities where individuals have no knowledge of what they are getting into or what will be the outcome. Now a days lottery would be considered under the restriction of *maisir* and is *haram*

because, in transactions involving components of *maisir,* there are raised issues of disbelief and unfairness in the minds of the parties, in line with the provisions set by God. In Britain, it has been reported that gamblers lose £100 every 20 seconds, with gambling being named as the "crack cocaine" of the high street.[142] Keeping aside God's law for a moment, if *maisir* components had benefits prevailing over harm, even society would not equate it to drug addiction. It may, perhaps, be a common point of agreement that, in any transactions, it is crucial that the parties have trust and faith towards the other party and such comes from knowing the obligations and circumstances to its fullest. Having *maisir* or *gharar* would hinder the progression of business due to the presence of the distrust among the parties as a result of lack of surety.

9. Relevance of *maisir* concept to marine insurance:

As in line with the structure adopted in these chapters, it would be prudent that an example should be set to show the relevance of *maisir* in traditional marine insurance. Maintaining the same variables as mentioned throughout, if an insured pays £x as a premium, then the chances of the insured facing an insured peril and losing all his goods and claiming for compensation is 50/50, which is half and half in line with the basic principles of probability. Now, if he does not face an insured peril and his goods reach their destination, he will not receive back his £x premium as the insurer would argue that they are entitled to this part as it is their risk covering.

If, on the other hand, there is an insured peril and the insured loses the goods, he claims for compensation of £z from the insurer. In both cases, he is taking chances, where someone is benefiting from the wealth of someone else irrespective of the outcome. The problem that arises is that neither knows who will be the next beneficiary. If there is a catastrophe, the insured is gaining £z, which is well over the £x which he is taking away without any regard for the insurer, which is *maisir;* another way of looking at it is that he is taking it away at the loss of the insurer, which is *qimar*. In either analogy, insured falls

[142] Hayley Dixon, 'Britons gamble £46 billion on betting machines' (2013) The Telegraph <http://uk.finance.yahoo.com/news/britons-gamble-46-billion-betting-003724680.html> accessed 17 February 2014

under the doctrine of *maisir*. Alternatively, if there is no catastrophe, the parties switch places and now the insurer's actions lead to *maisir* and *qimar*. In that case, the insurer is taking the premium only by chance, without caring whether it is at a loss for the insured.

10. Conclusion:

In conclusion, as discussed above, a number of authors have raised concerns about the presence of the principle *Sharia* restrictions of *riba, gharar*, *maisir* and their impacts on traditional contracts. The above analogies were necessary in order to allow an in-depth understanding of the concept as, without emphasising the concepts and the restrictions relevant to traditional marine insurance, it would simply be impossible to propose, or even justify, an intended proposed *halal* marine insurance model. The purpose of this research is to propose a model for the English marine insurance that will be *Sharia* compliant, but interfering as little as possible with the existent English marine insurance working algorithm. The intention is to implement the proposed model in practice and the idea is to avoid the proposed instrument from malingering excessively with the working practice otherwise it may led to loss of confidence. This points to the analysis of whether the impediments of *riba*, *gharar* and *maisir* can actually be controlled, either by removing or even circumventing in some way.

If that is successful, then it could lead to an effective proposed model, where a *halal* instrument can operate in the track lines of English marine insurance without breaking any restrictions one way or the other. Following on from the summarisation of the previous chapter of separating the concepts of premium and compensation, the ideal proposed model can be seen as follows: the payment of the premium by the insured was a consideration made by the insured to the insurer, due to a circumstance where the premium was paid for an immediate consideration to be provided by the insurer. This could justify the premium payment simply because it would make a contract on its own, where a payment is made (i.e. premium) by someone (i.e. insured) to someone (i.e. insurer) and the latter provides something in return. For the latter, it could either be a consideration of services or goods, in response to the payment (i.e. premium), which

could give rise to a *halal* contract, where at least in part it would deal with the premium payment within the *Sharia* ambit. This is because it is a trading scenario, where payment is made as part of a business risk, which is allowed and even strongly encouraged in Islam.[143]

Subsequently, it is suggested that the primary concern is the risk prevalent in the insurance concept, leading to a compensation payment relating to a valid claim being made. Therefore, should an alternative be proposed, so that compensation payment be routed in a way, that will not infringe the restrictions of *riba*, *gharar* and *maisir*, then this could led to the rising of an innovative *halal* insurance model. It is opined that, should the risk be controlled and the compensation payment be offset as security payment, when the risk becomes adverse leading to a loss, then it could led to a position whereby the three principal *Sharia* restrictions could be avoided. This is because, the compensation payment is being channelled as security payment, separate from other aspects of insurance and, as by its nature, a surety remains dormant until a specified event triggers its ignition, which is acceptable in Islamic law. Along the same lines, in traditional insurance the concept of payment of excess arises on claims and it is opined that, should the payment of excess be implemented in such a manner that it is effective only when a claim is made, perhaps by the injection of an additional distinct contract, then the operational structure would be the same as traditional insurance, but in a *halal* manner. The proposed *takaful* model aims to achieve these objectives but ensures that the various *Sharia* restrictions are kept intact from applying and interfering. The next chapter goes into more details on the precarious conditions the present day *takaful* models that are in, the various lacking which are causing such whirlpools and how the proposed *takaful* model fits in with fulfilling these gaps to shape, perhaps, a different advancing future for Islamic insurance.

[143] See above Chapter 2, Footnote 24

Part III

The basics of Islamic Insurance

Chapter 5: *Takaful* principles existent at present

1. Introduction

This chapter will look at the present principles and practices that exist for the operation of *takaful* in order to understand the mechanics of *takaful*. The thesis has already talked about the restrictions hindering traditional insurance from being considered *halal* and it is necessary at this stage to discuss the concept of *takaful* itself.

Takaful, as briefly discussed in Chapter 1, is an Arabic word which means cooperation between individuals, coming together in the event of a hazard to assist the victim in very short, mutual assurance. *Takaful* finds its routes from the earliest of times when individuals used to come together as a group to support each other. The equivalent word in Arabic for *takaful* is "*ta'mein*" and the paradigm was called *aqila*, which means amicable moral support and assistance. That was represented in the old times, by selected Arabs that used to work together until the damage caused by the disasters were mitigated.[144] Some prehistoric concepts that shed light onto the past practices leading to the concept of *takaful* in the Islamic society are as follows:

- *Kafala* which means guaranteeing, such as standing as surety for someone else, i.e. in the case of default by the existing owner, the surety provider would step in. This is similar to taking on liability on behalf of someone else in the event of claim by a third party and no more.[145]

[144] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 420 - 421
[145] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) pp. - 23 - 24

- Another concept is *Diyya,* which means blood money. This is another moral instrument that is to pay compensation for the death or harm caused to the victim by the crime-committing perpetrator.[146]

- One more concept is *Jiala*, which means incentive payment by someone to another unknown person for providing a task which is successfully carried out. The aim is to give motivation to carry out the task and, despite controversial views, this has been allowed due to need at the time.[147]

- Finally, the concept of *Muwalat* where someone gives their estate to another on the condition that the receiver would satisfy any *diyya* that may arise against the transferor.[148]

Some scholars have suggested comparing traditional insurance with the concepts mentioned above, such as Muhammad Ayub; however, other scholars, such as Aly Khorshid feel, that these likenesses are just coincidental.[149] Other scholars confer that such practices of mutuality and compensating for damages were practised in Mecca and Medina as tribal customs more than 1400 years ago in Saudi Arabia. In Asia, the practice started around the early second century of the Islamic era, when the Arabs expanded their international trade with Asian countries, including India and Malay Archipelago. Long voyages carried significant risk of losses and, as such, they came together to cover each other by mutuality.[150]

Nevertheless, all these are different moral concepts, which lack in some way or another from being able to function similar to traditional insurance. For example, *kafala* can only provide a third party liability, whilst *diyya* can only be in a position if the perpetrator's family pays for a criminal act and no more. Similarly, *jiala* can only be used to give a

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[146] Ibid
[147] Ibid
[148] Ibid
[149] Ibid
[150] Haemala Thanasegaran, 'Growth of Islamic Insurance (Takaful) in Malaysia: A model for the region?' (2008) 143 Sing. J. Legal Stud., p.144

reward if the task is completed and does not provide sufficient room for movement. Additionally, *muwalat* have been considered by the Hanbali school of thought to be invalid and only deals with someone else's liability in narrow scopes and no more.[151] With such restrictions, the moral concepts are simply outside the zone of traditional insurance and could not come within the ambit of traditional insurance.

2. Ideology of *takaful*

As mentioned previously, the whole aspiration of considering *takaful* in place of traditional insurance is because of the presence of *riba, gharar* and *maisir,* as has been explained in the previous chapters. Oliver Agha states that traditional insurance contravenes the concept of *tawakkul,* i.e. reliance on God, as the insured is relying on the insurer rather than God for assurance.[152] It is opined that the concept of *tawakkul* is breached in any event when the three restrictions of *riba, gharar* and *maisir* are infringed. However, Oliver Agha goes on to justify that *tawakkul* alone is the only cause of why insurance is incorrect, as authority exists which confirms that risk reduction is not contrary to God's will, and given that *takaful* deals with cooperative risk allocation, which is permissible under *Sharia* law.[153] In this respect, author Aleem Khan Falaki explains nicely that the ideology is that the insured is putting trust in the insurer instead of God, but both parties are entering a consensual contract for protection and welfare from unforeseen mishaps.[154]

It is relevant to note that, for Muslims, there is a strong belief that, whatever God has willed, it is not possible to prevent; however, the effects of any harsh destiny may be reduced. A brilliant example has been provided by Sheikh Mustafa Azzarqa, Professor of Islamic Law, who compared insurance to iron bars put on top of a building to divert

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[151] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) pp. – 23 - 24

[152] Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, pp. – 70 - 71

[153] Oliver Agha, supra at pp.– 72 - 73

[154] Aleem Khan Falaki, 'Life insurance and the Muslims' 2nd edition, Media Plus Publications, 2007, Chapter 9 Article 3 <http://li.aleemkhanfalaki.com/chapters/adil-salahis-views-on-insurance/> accessed 6 February 2014

thunderbolts. The architect's idea was not to avoid the thunderbolt from taking place, but to safeguard the building he structured by diverting the thunderbolt deep into the ground.[155] Additionally, even Imam Abdullah Al-Sheikh in his *kutba* on 25th July 2014 at Bangor Mosque correlated *tawakkul,* i.e. reliance on God, to insurance, with the difference being that, whilst the recompense for insurance comes later on after the event, for *tawakkul* the reward is before the event takes place. Thus, literally it is safe to state that *tawakkul* itself does not possess a threat to the validity of insurance in Islam.

Takaful as hinted above works under the ideology of sharing the responsibility with the aim of common benefit and harmonisation for everyone in that *takaful* union. The word *takaful* itself has been derived from the verb *kafala.*[156] The Islamic laws which form the present basis of *takaful* conform on policyholders working together with liabilities shared so as to limit uncertainty and none are unfairly disadvantaged. There are various relevant Islamic texts emphasising this idea, including a *Quranic* verse from *Surah Al-Maidah* (5):3 that: "*Help one another in righteousness and piety, but help ye not one another in sin and rancour.*" Also, it has been stated in a number of *hadiths* including "*Allah will always help His servant for as long as he helps others*"[157] and "*By my life, which is in Allah's power, nobody will enter Paradise if he does not protect his neighbour who is in distress*".[158]

The basic idea, as has been expressed previously, is that each participant pays his/her contribution into a joint pot to cover needs, as may arise. As there are uncertainties involved under Islamic law, the *gharar* concept restricts this contribution to a commercial payment as each party's obligations are vague. Therefore, the Islamic jurists have introduced the idea of framing the contributions as donations, i.e. *tabarru*, so that each of

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[155] Aleem Khan Falaki, supra at Chapter 3 Article 5 <http://li.aleemkhanfalaki.com/chapters/adil-salahis-views-on-insurance/> accessed 6 February 2014

[156] Mohd Ma'sum Billah, , 'Islamic banking and the growth of *takaful*' (2007) in the Textbook: M. Kabir Hassan and Mervyn K. Lewis (eds), *Handbook of Islamic Banking* (1st edn, Egward Elgar Publishing Limited 2007), p. – 405

[157] Narrated by Imam Ahmad Ibn Hanbal and Imam Abu Daud; Syed Othman Alhabshi and Shaikh Hamzah Razak, '*Takaful* insurance: concept, history and development challenges' in the Textbook: Mohamed Ariff and Munawar Iqbal (eds), *The foundations of Islamic Banking: Theory, Practice and Education* (Edward Elgar Publishing 2011) pp. – 190 - 191

[158] Narrated by Imam Ahmad Ibn Hanbal; Ibid

the participant agrees to waive off their contribution for the greater good, in the event of someone in a *takaful* union suffering a loss due to defined calamity. This, in essence, works to show that point of mutual help between each other, where each one considers the other to be their brethren. The aim of having a mechanism that would assist an individual within the ambits of *Sharia* rulings is not a concept that is being considered evil especially, where the case is one of genuine losses suffered due to calamities outside the control of the loss suffered. Scholars such as Muhammad Ayub and Oliver Agha approve such aims of *takaful* and concentrate on the point of finding appropriate solutions to circumvent *Sharia* restrictions.[159]

Hania Masud identifies five different considerations of a *takaful* organisation. The first one is the presence of the mutual guarantee, as such the existence of solidarity among the participants. The second is that the ownership of the fund belongs to the participants and the *takaful* operator is there for management purposes. The third is the uncertainty eradication by the utilisation of *takaful*. The fourth is the *takaful* operator's determining which rewarding model to utilise for fund management. The fifth is the *takaful* operator deciding the organisation structure on investment conditions.[160]

The ideological basis of *takaful* certainly appears to have gained in public credence. Over the past few years, it has been reported that *takaful* industry has been growing at a rate of twenty per cent every year, with a recorded double digit growth in 2009 at the time of the recession.[161] For an industry that is just over 30 years old, with the first company beginning in Sudan on 1979, this is notable. As per Oliver Wyman's report of 2007, the global *takaful* premium was at least US $20 billion with 20% income generated from

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[159] Hasanuz Zaman, (1991) p. - 418, in the Textbook: Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007)
Also: Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, pp. – 81 to 82
[160] Hania Masud, '*Takaful*: An innovative approach to insurance and Islamic finance' (2010-2011) 32 U. Pa. J. Int'l L. 1133
[161] Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, pp. – 70 to 71

non-Muslim customers.[162] It has been noted that the global *takaful* industry have grown from US $1.4 billion in 2004 to US $5.3 billion in 2008 and this has been participated in both Muslim and non-Muslim countries, with GCC countries fund generation being more than half of the market. Malaysia holds the largest volume of *takaful* contributions, standing at US $889 million in 2008, with some financial institutes having a non-Muslim customer base of between 50% and 70%.

There have also been a number of significant correlated ventures between organisations for the advancement of *takaful*. For example, in November 2008, Zurich Financial Services agreed a joint venture with Abu Dhabi National Takaful; in June 2009, AXA insurance agreed a partnership with Salama in the UAE; FWU Group became a stakeholder in Al Ahli Takaful Company and agreed a distribution partnership with the National Commercial bank, in Saudi Arabia. In November 2009, Allianz Takaful agreed with Standard Chartered Bank for a promotion of its insurance products. In December 2009, Generali, one of the largest Italian insurance companies, agreed with Qatar Islamic Bank to enter the GCC *takaful* market.[163]

However, it is necessary to state that it has become rather an open secret in the *takaful* industry that the *tabarru* models under *mudarabah* and *wakala*, set for conducting *takaful* business, have raised grave concerns among the community over the ability of working in compliance within the remits of *Sharia* rules. It has been debated among the scholars that the models of *mudarabah* and *wakala,* and even their hybrids in some way or another, leads to the breaching of *Sharia* rulings as such leads to the questioning of the workability of the whole *takaful* structure. It is opined that, to an extent, this perplexity may have contributed to the lack of availability of a rigid working structure of *takaful* and, leaving the various jurisdictions, to come up with models that they felt appropriate. This caused a lack of analytical consideration of each of the models proposed against a standard scale. This is discussed later in more detail ~~later~~ below, when consideration is

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[162] Syed Othman Alhabshi and Shaikh Hamzah Razak, '*Takaful* insurance: concept, history and development challenges' in the Textbook: Mohamed Ariff and Munawar Iqbal (eds), *The foundations of Islamic Banking: Theory, Practice and Education* (Edward Elgar Publishing 2011) pp. – 204 - 205

[163] Zamir Iqbal and Abbas Mirakhor, *An Introduction to Islamic Finance: Theory and Practice* (2nd edn, John Wiley & Sons Asia Pte. 2011) pp. - 216 - 219

made of each of the models in details along with their respective drawbacks. Nonetheless, due to the problems by the *mudarabah* and *wakala* models over recent years, the Islamic jurists have considered extending mutual help with the introduction of a *Waqf* instrument rather than simply restricting it to cooperativeness.

Waqf has been illustrated as an endowment or donation by authors, which relates to the setting of assets for charitable causes or for the needs of defined groups of individuals, such as the members of a donor's family. *Waqf* has been reported to be of three types under *Sharia* rules: religious *waqf*, philanthropic *waqf* and family *waqf*. The principle of *waqf* is that the *waqf* is considered as a separate legal entity that takes over the title of the property from the creators of the *waqf*.[164] That property belongs to *waqf* at all times, which can never be sold but named beneficiaries are entitled to use the usufruct of that property.[165] Mohammed Ayub mentions that the donor of the *waqf* are entitled to enjoy the benefits of that *waqf* and goes on to mention that the participants, also being the beneficiaries of the contribution, are providing the funds in a *waqf* relationship with the aim of cooperativeness and loss mitigation.[166]

It has been put forward that certainly there are a number of serious doubts about using *waqf* as an instrument for *takaful*. This is in addition to the issue on the *waqf* model that is being utilised, which shall be scrutinised in the relevant section in a later chapter, when the various models are considered. However, as a minimum point, it is worth noting that *waqf* is not even a financial instrument, unlike other model instruments such as *mudarabah* and *wakala,* and so it is not designed to work effectively in the same manner. Moreover, *waqf* by its nature is a voluntary instrument and subjected to a number of strict regulations that need to be adhered to, which are discussed later on, and is not simply efficient to be used on a large-scale basis of obligating participants. It is important to note that, unlike traditional insurance where an insurance model has been established, it is

[164] Unlike companies in UK where a Limited company is considered as a legal entity on itself separate from the directors and shareholders, who may have brought the company into existence.
[165] The author feels that this is analogous of the use of usufruct as in *ijara* leasing contracts where the title of the property at all times remains to that of the lessor and the lessee only entitles to use the usufruct of that leased property, which must return at the end to the lessor. *Ijara* contracts are discussed later below.
[166] Hasanuz Zaman, (1991) p. - 418, in the Textbook: Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. - 421 – 422

implemented and pretty much used everywhere, which is that the insured pays a premium to the insurer for the covering of defined risks for a defined period. In contrast, in *takaful* there is nothing set as such other than an idea, but one has to be careful not to simply disregard *takaful*, as the whole concept behind the introduction of *takaful* is for *Sharia* compliance, which in itself is aimed at conforming to the ideas and principles set by Almighty God. This has led to the production of various different models for *takaful* so as to attempt observation of the divine rules. However, a common point shared among scholars is that there is a need for the development of a *takaful* model, a model that would be universally recognised and would attract consumers' confidence for the advancement of communities.[167]

3. Comparison features between *takaful* and orthodox marine insurance:

It is not disputed that the aims of *takaful* is to serve the purpose of risk limitation, as in traditional insurance. In the introductory chapters, as mentioned above, some well-known concepts were used as illustrations such as utmost good faith, warranties and contract construction to aid as a succinct comparison with traditional marine insurance in England and Wales. As all of these are present in *takaful,* this brings it on the same line as that of traditional marine insurance, as the operational objectives of both of them are identical. In both cases, the calculations are done in line with the risk faced, loss ratio, claims history and liability evaluation, amongst others.[168] However, without repeating much of what had been mentioned in previous chapters, *takaful* also faces uncertainties as regards traditional marine insurance. *Takaful* managers retain this to a minimum by keeping the contributions from participants as a way of helping each other out and waiving the participants' rights as funds being provided as charity. Moreover, the *takaful* operator is always put on standby to assist into the rescue of participants by providing *quad hasan,* i.e. gratuitous interest free loans, when the *takaful* operation falls into crisis and

[167] Abdul Rahim Abdul Wahab, 'Takaful Business Models - Wakalah based on WAQF: Shariah and Actuarial concerns and Proposed Solutions' <http://www.baj.com.sa/takaful/Presentations/PanelFour/Takaful%20Models%20Based%20on%20Waqf%20by%20A.%20Rahim%20Abdul%20Wahab.doc> accessed 4 January 2014

[168] Haemala Thanasegaran, 'Making an entrance – Can Australia contribute to *takaful* (Islamic insurance) law reform?' (2013) 24 Insurance Law Journal, p. – 107

participants are faced with liabilities for the deficit. This is undoubtedly quite different from orthodox marine insurance, as the insurers simply obtain the monies from the insured as premiums, with the assurance of risk cover, and do not involve the insured in any of the joint pot concepts. The cooperativeness of the organisation is much more prevalent in *takaful* than in traditional marine insurance.

Nevertheless, it is worth discussing that there are a number of features that make *takaful* different from the traditional marine insurance at present, some of which include business aims, structure, investment strategy and returns.[169] Firstly, unlike traditional marine insurance, where on the onset it is a buying and selling contract of protection, in a *takaful* operation there are at least four parties involved, which are: the participant, the *takaful* operator, the insured and the beneficiary. The participant is the one who joins the *takaful* scheme by paying the *tabarru*; the *takaful* operator is similar to the insurer in traditional insurance, managing the *takaful* scheme; the insured is the name given to the *takaful* cover under the *takaful* scheme; the beneficiary is the one who receives the compensation following the making of a claim.[170] However, like general marine insurance, where money is paid by the insured into the insurer's account as a premium, in *takaful* the contribution paid by participants are invested; and, in certain cases, such as in family *takaful,* these funds are divided and allocated into two separate accounts: one account, which follows the profit & loss sharing, whilst the other account is considered as donations for charity.[171]

Secondly, author Haemala Thanasegaran emphasises in her article that one of the differences between traditional insurance and *takaful* is that the participants in *takaful* aim for religious purposes rather than profit only and that is the driving factor for *takaful*

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[169] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 427 - 428

[170] Considering under the specs of straightforward traditional insurance, the participant, the insured and the beneficiary might appear to be the same individual but under the specs of unorthodox insurance e.g. life insurance, the participant can be the person paying the premium, the insured could be the person's spouse and the beneficiary could be the person's children. Even under marine insurance prospective, the participant can be the seller, the insured could be the buyer and the beneficiary could be the buyer's buyer.

[171] Mohd Ma'sum Billah, 'Islamic banking and the growth of *takaful*' (2007) in the Textbook: M. Kabir Hassan and Mervyn K. Lewis (eds), *Handbook of Islamic Banking* (1st edn, Egward Elgar Publishing Limited 2007), pp.– 405 - 406

in comparison to traditional insurance.[172] This view appears to have been shared by Mohammed Ayub as well, who argues that premium amounts in traditional insurance are aimed at maximizing profits alone.[173] Whilst in principle, perhaps, we can agree with the comments of Haemala Thanasegaran, it is disagreed that it was not necessarily portraying the fact that profits alone should be viewed when in the limelight and seen as evil. As mentioned earlier, the Holy Quran has allowed as in *Surah Al Baqarah*, Chapter 2, Verses 275 "*...That is because they say, 'Trade is [just] like interest.' But Allah has permitted trade and has forbidden interest.*"[174] Therefore, it is felt that making profit alone certainly should not be considered as a bad influence for the promotion of an instrument as long as it is *Sharia* compliant.

Thirdly, one important point to note is that *takaful* is not there to protect the participants in the event of a loss. This is not possible, as the *takaful* operator would then be entering the realms of *gharar* and *maisir*, which means promising to cover an unforeseen event, which would take it outside the remits of being considered *halal*. The working terminology of *takaful* instead is cooperative cohesion, which warrants financial certainty for a member of the group by sharing the responsibilities between the participating members, with each participating member bearing the risk for one another by providing premiums as donations into the *takaful* fund.[175] This obviously is different to how traditional marine insurance is set up, where a premium is paid by the insured for the unforeseen risks, irrespective of whether that takes place or not. The responsibility of the protection of the insured falls squarely on the insurer in such circumstances as the concepts that threaten *takaful* are not a problem in traditional marine insurance.

Fourthly, however, it should be noted that the charity aspect of *takaful* has undoubtedly raised concerns among scholars on the viability of the *takaful*. Authors such as Oliver Agha view *tabarru* as confusing in *takaful* models, as the idea behind the setting of

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[172] Haemala Thanasegaran, 'Making an entrance – Can Australia contribute to *takaful* (Islamic insurance) law reform?' (2013) 24 Insurance Law Journal, pp.– 104, 109
[173] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) p. - 427
[174] Holy *Quran*, 'Surah *Baqarah'* Chapter 2 Verses 275 to 281 (quran.com) <http://quran.com/3> accessed 19 January 2014
[175] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) p. - 420

tabarru is that there is no obligation on the payer to return the fund as it is a donation and there is no requirement on the insurer to return the fund as it is given as a charity. However, this creates a problem, as there remains no obligation on the insurer to pay the fund in the event of a loss, as it was given as a charity only.[176] In simple terms, this creates a concern that, when a participant suffers loss, in theory at least, the *takaful* operator is not obliged to pay as it was a charity payment given away by the participant with no intention of seeing again. It was a one-way payment provided as *tabarru* by the donor (i.e. participant), which does not set a condition on the donee (i.e. *takaful* operator) that payment should be returned on certain conditions. Of course, in traditional marine insurance one does not face these issues as conventional insurance works, as mentioned above, on the straightforward basis of receiving premiums, but breaching the *Sharia* restrictions. Orthodox insurances are not concerned about the receipt of charity payments, since all funds from Underwriting are payments that are taken as income for the insurance business.

Fifthly, the responsibility of the orthodox marine insured is simply restricted to the payment of premium and, even in mutual cover, the insured are limited to such payment with surpluses forming reserve funds. As mentioned above, in *takaful* the insured do not make premium payments but provides a donation known as *tabarru,* which is used as investment and the returns are allocated depending on the type of *Sharia* approved arrangement, e.g. *mudarabah* or *wakala* agreed between the participant and *takaful* operator.[177]

Sixthly, an investment of funds in an orthodox marine insurance business would be made into any kind of venture, whichever will maximise the profit of return, including interest-based opportunities irrespective of whether the project is *halal* or *haram.* In *takaful,* investments are made only into profitable ventures of *halal* opportunities, which are

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[176] Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, p. – 72

[177] Abdullah Haron and Dawood Taylor, 'Risk management in *Takaful*' in the Textbook: Editor: Simon Archer, Rifaat Ahmed Abdel Karim and Volker Nienhaus, *Takaful Islamic insurance: Concepts and Regulatory issues* (John Wiley & Sons Asia Pte. 2009), pp. – 172 – 174

supervised by the *Sharia* supervisory board within the *takaful* organisation and returns are managed, as per prior *takaful* agreement, between the parties.[178]

Seventhly, when claims are made with traditional marine insurance, the insurer is responsible for satisfying the claims and, if mutual insurance is there, the insurer's pool of funds is used to pay those off. In *takaful,* it is the *takaful* operator's responsibility to pay these liabilities but, if there is a deficit, the *takaful* operator has to provide an interest-free loan to aid the organisation come out of negative balance, according to all of the present *takaful* models.[179]

Eighthly, both in orthodox marine insurance and *takaful,* the insurer has access to share capital, save with mutual insurance where the insurer cannot have access to share capital. However, with debt, orthodox marine insurance and mutual insurance are responsible for the satisfaction of debts and liabilities. In *takaful,* the participants bear the responsibility for debts, although the *takaful* operator may have to pay a gratuitous interest-free loan out of their own funds (separate from the *takaful* operation as it made a loss), to keep the *takaful* operation on-going.

Finally, it is considered that a *takaful* operation is much more transparent as the relationship is one of mutual cooperation and avoids participants from being swindled. However, in orthodox marine insurance, even if compensated under a valid claim, the compensation received by the insured would reflect only a small fractional percentage of the profit made by the insurer on investment returns.[180]

4. General structure of a *takaful* company

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[178] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 427 – 428; **And** Abdullah Haron and Dawood Taylor, supra at pp. – 172 - 174

[179] Abdullah Haron and Dawood Taylor, supra at pages – 172 - 174

[180] Aleem Khan Falaki, 'Life insurance and the Muslims' (2nd edn, Media Plus Publications 2007) Chapter 3 Article 5; <http://li.aleemkhanfalaki.com/chapters/main-difference-between-takaful-and-insurance/> accessed 8 February 2014

The basic structure of a *takaful* company, keeping aside the different types of models available for operation, at the onset is relatively straightforward and somewhat similar to traditional insurance.[181] The relationship between a *takaful* company and the participants giving the contribution is that of a trust-giver and trustee. The participants give the funds to the *takaful* company in trust, which is put in the *takaful* fund and the latter manages the funds by investing and attempting to make a profit in *halal* ventures.

The *takaful* operator's responsibility is the handling and management of the funds provided. Liabilities such as claims are compensated from this fund, whilst any surplus or deficit in the Underwriting are on the participants to share or cover up. However, the *takaful* operator is always present to give efficacy to the operation by providing *quad hasan,* i.e. gratuitous interest-free loan, to cover deficits. Depending on the type of model used, e.g. *mudarabah* or *wakala,* this would determine how the return from the investment of the *takaful* fund would be shared between the participants and the *takaful* operator, and how the latter would be remunerated. Similarly, depending on the type of model, e.g. *mudarabah* or *wakala,* this would determine how the Underwriting surplus would be distributed between the participants and the *takaful* operator.[182]

A pictorial diagram, diagram 5.1, shows the annex in order to assist in understanding the basic working structure of *takaful*, irrespective of the type of model currently existing. The different types of models of *takaful* are dealt with in the next chapter.

The diagram demonstrates the basic working structure of a *takaful* organisation with the participants. In relation to the organisational structure, there is normally a head general manager, under whose supervision there are four departments in the *takaful* organisation.

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[181] This is excluding consideration of *takaful* life policies whose working principles are different than how the remainder of the *takaful* policies works. This is because with other types of *takaful* policies there is always a chance that the covered perils may or may not occur, whilst with life policies, the event will happen for sure i.e. death, the only question being one of time as when the incident will take place. Therefore, the management of *takaful* life policies are set out in different working principle of keeping aside part of contributions even to cover the claims, which as mentioned, will take place for certain. Obviously, keeping into consideration, that the participant maintains the *takaful* life policy at the time of his/her death and didn't close the account i.e. bring the relationship to an end before the ordained event i.e. death. This thesis will not consider dealing with life related *takaful*.

[182] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. 422 – 423

Each of the departments is distinct and operates independently. Firstly, there is the family *takaful* department which, as the name suggests, deals with family-related insurance products. The second is the general *takaful* department, which has three separate divisions of Underwriting, claims and *retakaful*. When there are any claims, the claim divisions categorise between motor and non-motor claims.[183]

The third department is Finance and administration, while the fourth department is Marketing. In fact, the finance department plays a major role in the management of the contributions provided by the participants. The finance department is split in two divisions, one of investment and the other of accounts. When the participants pay their contribution, this is handled by the accounts division by placing it as shareholders funds and set aside for further consideration. As funds come in from the participants under the general *takaful* policies, the funds are treated as *tabarru,* i.e. donation, and put into the Participant's special account (PSA). From thereon, the investment division takes on the funds for investment and to generate profit. In the event of a profit from the investment, the surplus is shared in the model agreed between the parties, but in the event of a loss, participants are liable for the losses. In the event, the participant has to claim due loss suffered, and he/she will still receive compensation, as when the initial *tabaru* was provided he/she had already entered the cooperative scheme. The loss sustained by investment of the fund by the *takaful* operator is a business risk that the participant and *takaful* operator took together, in the course of business and any profit or loss from this venture is totally distinct from the loss claim that the participant makes in the event of a defined catastrophe. Whilst the former relationship relates to business risks, the latter relationship relates to a cooperative scheme. The following structure appears to be prevalent in Malaysia, Bahrain and Saudi Arabia.[184]

5. Relevant reviews and opinions of Islamic scholars about insurance and *takaful*:

[183] Mohd Ma'sum Billah, 'Islamic banking and the growth of *takaful*' (2007) in the Textbook: M. Kabir Hassan and Mervyn K. Lewis (eds), *Handbook of Islamic Banking* (1st edn, Egward Elgar Publishing Limited 2007), pp.– 406 - 408

[184] Ibid

This section has attempted to deal with the standing of Islamic *fuqaha*, authors on admissibility of insurance in Islam and the present position of acceptability. It is no secret that the Islamic *fuqaha* has been in a dilemma about the permissibility of traditional insurance under Islamic rules for a long time. This is mainly because there is nothing directly mentioned about either allowing or rejecting insurance in the *Quran* or in the *hadiths* or *Sunna*. Hence, there is a lack of any authoritative literature on this subject matter, resulting in subjective scholarly views, who themselves lack the requisite knowledge about insurance and terms of relationship.[185] Therefore, it becomes relevant to fall back onto secondary sources such as the opinions of *fuqaha,* called *fatwas*, acceptable consensus among Muslims called *imam* and analogies of various relevant authors. It should be noted that scholarly opinions such as *fatwas* do not automatically have legal effect until incorporated into law; however, they do form the basis for the development of respective jurisdictional law.[186] In this section, it has been aimed to look at well-known secondary sources which would assist in understanding the current border grounds of insurance in Islam, which would appear to be similar to a literature review in this perspective.

To start with, the prominent Egyptian scholar Sheikh Mohammed Abu Zahra, who lived between 1898 and 1974,[187] considered the issue of insurance in detail and deliberated that cooperative insurance is acceptable, but discarded the uncooperative insurance. His determination could be summarised in three main points:

i. Mohammed Abu Zahra stated that a flexible and understandable approach to be adopted by Islamic jurists for insurance, except where such contract is in violation with Islamic basic laws.[188]

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[185] Khalaf 1974: Vol. 11; Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) p. - 60

[186] Madzlan Mohamad Hussain, 'Legal issues in *Takaful*' in the Textbook: Simon Archer, Rifaat Ahmed Abdel Karim and Volker Nienhaus (eds), *Takaful Islamic insurance: Concepts and Regulatory issues* (John Wiley & Sons Asia Pte. 2009), pp. – 74 – 75

[187] Ralph H. Salmi, Cesar Adib Majul and George K Tanham, *Islam and Conflict Resolution: Theories and Practices* (University Press of America 1998) ISBN 9780761810964, p. - 90

[188] Aly Khorshid, supra at pp. – 58 - 59

ii. Mohammed Abu Zahra witnessed that some Islamic jurisdictions have allowed insurance contracts due to their benefits, which is a positive factor. He mentioned that trying insurance products for true and genuine purposes is acceptable. He went further to consider whether commercial insurance is a public or private beneficence and noted that a minor percentage of individuals use the same.[189]

iii. Abdel Rahman Issa stated that an important aspect of insurance nowadays is that it is a necessity and part of daily life. Mohammed Abu Zahra enquired whether commercial insurance is the sole alternative, but considered that existence of necessity shows that cooperative insurance is present, otherwise the latter needs to be created.[190]

As a result, as mentioned above, Mohammed Abu Zahra approved of cooperative insurance and not the non-cooperative ones. However, he justified this by stating the presence of "*taints of gambling, temptation and usury,*" which would void the contract. He viewed that, in such circumstances, it appears to be a misuse of resources against warrant and so could not be considered as a necessity.[191] Aly Khorshid appears to disagree with Mohammed Abu Zahra as he distinguishes the commercial aspect of insurance from the everyday impact of insurance in daily life. He goes further to argue for restructuring of the Islamic lifestyle by allowing adjustment with accepting insurance provided in a *halal* manner.[192]

Likewise, the *Fiqh* academy of the Organization of Islamic Conference[193] in their ninth declaration at the second session in Jeddah, Saudi Arabia on 22nd-28th December 1985,

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[189] Ibid
[190] Ibid
[191] Ibid; This raises question in the mind of researcher that if stated characteristics could be removed then there should not be any reason to consider traditional insurance acceptable.
[192] Aly Khorshid, supra at pp. – 59 - 60
[193] Organization of Islamic Conference is the second largest inter-governmental organization after UN, whose aim is to safeguarding and protecting Muslims interest in the world. There are at present 57 state members. <http://www.oic-oci.org/oicv2/page/?p_id=52&p_ref=26&lan=en> accessed 4 February 2014

ruled that commercial insurance is *haram.*[194] On consideration of their ruling, the committee had made some concrete conclusion on the issue of insurance, which had been set in three points, which author Mahmoud A. El-Gamal has also cited in his literature as follows. The first point decided by the committee, as quoted by Mahmoud A. El-Gamal, is that a traditional insurance contract, where a set premium is paid, is not acceptable because of the presence of excessive *gharar*. This makes the contract ineffective between the parties as, under Islamic laws, the contract would be unlawful.[195] However, the original paper of Organization of Islamic Conference states that the commercial insurance contract contained "*major elements of deceit, which void the contract*".[196] This slight discrepancy of the texts can be compromised, if the author had attempted to correlate or paraphrase the rulings; but, for safety purposes, it is best to remain with the original paper that the *Fiqh* academy felt contained major presence of deceit in traditional insurance, resulting in them considering it as *haram.*[197]

The second point is that the committee went further to confirm that they consider cooperative insurance to be a substitute to traditional insurance, as they view the former as being set in the beliefs of cooperation and voluntary contributions and went ahead to

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[194] Primary texts in Arabic: <http://www.fiqhacademy.org.sa/qrarat/2-9.htm> accessed 6 February 2014 English translation from secondary text: 'Resolutions and Recommendations of the Second session of the Council of the Islamic Fiqh Academy: Jeddah (Kingdom of Saudi Arabia) 10-16 Rabiul Thani 1406 h/22-28 December 1985' Resolution No 9 (9/2): Concerning insurance and reinsurance, in the Text: "Resolutions and Recommendations of the Council of the Islamic Fiqh Academy 1985 – 2000" (1st edn, Islamic research and training institute: Islamic Development Bank 2000) pp. – 13 – 14 <http://www.irtipms.org/PubText/73.pdf> accessed 4 February 2014

[195] Mahmoud A. El-Gamal, *Islamic Finance: Law, Economics and Practice* (Cambridge University Press 2009) p. – 147

[196] 'Resolutions and Recommendations of the Second session of the Council of the Islamic Fiqh Academy: Jeddah (Kingdom of Saudi Arabia) 10-16 Rabiul Thani 1406 h/22-28 December 1985' Resolution No 9 (9/2): Concerning insurance and reinsurance, supra at p. - 13

[197] It is of quite clear that the texts have a discrepancy with explanation, which although not within the ambit of this thesis to consider book reviews but it is relevant to mention and deal with the appropriate texts and consider the correct meanings for the advancement of the final proposed model of the researcher. As the researcher has pointed out, it is possible that the author, Mahmoud A. El-Gamal wanted to summarise the rulings hence the version as mentioned use. Or the other alternative could be that the author meant "*gharar*" to have the equivalence of "*deceit*". This is because *gharar* means uncertainty and *deceit* in Islamic law refers to the concept of *Ghabn*, an example of which is *bay' al-najash* which means a fraudulent action sale where price increased by fake buyer tactics so that real buyers bid more. Although a far fetched description, it may be considered that a *bay' al-najash* can be considered to be *gharar*.

set similar ideologies for reinsurance as well.[198] Additionally, the third point the committee proposed was that Islamic countries should work harder for promotion of the cooperative insurance and reinsurance so as to avoid reliance on the traditional insurance, which they proposed is practised contrary to God's commandments.[199]

However, the late Professor Mustafa Al-Zarqa dissented on that conference in line with his published paper from 1961, in which he opined that he considers traditional insurance of all types acceptable subject to insurers changing their investment part of the business to avoid *riba* aspects. Dr. Ali Jumah, Grand Mufti of Egypt, later considered these various opinions and, in September 2004, he argued differently in that conventional insurance is permissible with some small changes and passed a *fatwa* in this respect.[200] Dr. Ali Jumah mainly compared insurance with other financial concepts such as banking, for which there is nothing explicitly mentioned in Islamic canonical texts. However, he pointed out the Holy *Quran* verse 4:1 that stated, "*O people of faith, fulfill your contracts*", which he argued referred to all types of contracts including insurance contracts. Also, he referred to the last speech of Prophet Mohammed (pbuh) in Mina where he mentioned, "*It is not permitted for anyone to take the property of his brother except with his consent*" and argues that, if mutual parties decide to deal on agreed terms as in insurance contracts, there is no objection. Dr. Ali Jumah felt that *mudarabah* and customary rules are acceptable and saw no reason why authorisation should be withheld for commercial insurance when cooperative insurance is allowed. He expressed that life insurance is considered to have excessive *gharar*, which does not affect parties' contractual obligations or commercial insurance, where parties know in advance the amount paid and would receive, so there should not be any arguments of excess *gharar*.[201]

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[198] 'Resolutions and Recommendations of the Second session of the Council of the Islamic Fiqh Academy: Jeddah (Kingdom of Saudi Arabia) 10-16 Rabiul Thani 1406 h/22-28 December 1985' Resolution No 9 (9/2): Concerning insurance and reinsurance, supra at p. - 13

[199] Ibid

[200] Mahmoud A. El-Gamal, supra at p. – 147

[201] Mahmoud A. El-Gamal, supra at pp. – 149 - 151

The committee of the Council of Islamic *Fiqh* academy again sat recently to discuss commercial insurance. In their Resolution 187 at the 20th session in Oran, Algeria on 13th-18th September 2012, they reaffirmed the committee's previous decision of Resolution 9/2 (above), that commercial insurers' practice of charging a fixed premium is a contract of exchanging, which contains extensive *gharar* and is not considered *halal*. However, the committee acknowledged that *takaful* is facing severe statutory and regulatory issues and recommended a remodelling of cooperative insurance to be considered further for draft resolution in the next meeting.[202]

Nonetheless, prior to this, on the fifth ruling of the first session of the *Fiqh* academy of the Muslim World League[203] that took place on 10th-17th Sha'ban 1398H,[204] it determined that commercial insurance is unacceptable and the only acceptable form is cooperative insurance. Their decision, which is broken into six main points, is summarised as follows. (1) Commercial insurance has severe uncertainties and parties do not know at the time of the contract what will be paid and what will be received by each party respectively; (2) Commercial insurance activities have the likes of gambling where, in respect of the payment of premium, the insured may not get any monies in return or get substantial amount of monies, more than the premium amount, in compensation; (3) The payment is considered *riba* as the exchange of payment is unequal and paid later; (4) The commercial insurance is compared to betting and does not fall under the permitted betting category;[205] (5) Monies of the insured are taken in return for nothing and this is contrary

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[202] 'Resolution No.187 (2/ 20) on: Cooperative Insurance: Sharah Rules and Regulations' Islamic Economic Studies, Vol. 21, No. 1, June 2013, pages – 104 – 106 <http://www.irti.org/irj/go/km/docs/documents/IDBDevelopments/Internet/English/IRTI/CM/downloads/IES_Articles/Vol_21_No_1/Resolution_of_OIC_Fiqh_Academy.pdf> accessed 6 February 2014
It does not appear that the next committee meeting and the decisions has been published yet according to the Council of Islamic *Fiqh* academy official website <http://www.fiqhacademy.org.sa/> accessed 6 February 2014

[203] The Muslim World League is an organization which is based in Makkah Al Mukarramah, Kingdom of Saudi Arabia whose primary aim appears to assist in the practising of Islam in the correct manner within the ambits of Islamic law <http://en.themwl.org/taxonomy/term/19> accessed 5 February 2014

[204] Islamic calendar dates are different from the traditional Georgian dates that are used everywhere. 10th – 17th Sha'ban 1398H translates to between 16th – 22nd July 1978 <http://www.islamicfinder.org/Hcal/index.php?lang=english> accessed 5 February 2014

[205] It is mentioned in the resolution that Prophet Mohammed (pbuh) has allowed betting in three permitted activities in the saying that: "There is no competition except in camel race, horse race and arrow contest" and it is considered that commercial insurance does not fall under any of these categories;

to one of the provisions in the *Quran*;[206] (6) The insurer is entering a contract to oblige payment as a guarantor on an uncontrolled uncertain event and takes monies from the insured for this, but does no work in return.[207]

The committee considered various arguments put forward for approving insurance in Islam but disregarded the arguments are for benefit, necessity, applicability unless prohibited, customs, blood money, payment as security provider, deposit payment and cooperative cloth merchant deals. The committee made clear that a *mudarabah* contract cannot be in the realms of an insurance contract as, unlike *mudarabah*, in insurance monies paid i.e. premium, ownership changes along with the fact that upon the insured's death, inheritance is on any compensation not the premium and unlike sharing in *mudarabah*, the same does not take place from the premium that was initiall provided by the now deceased. As mentioned, they approved cooperative insurance, on four premises namely that it works on a donation principle by sharing responsibilities cooperatively with no aim of profits from other monies. The second in cooperative insurance, *riba* is absent as there is an unequal or delayed payment issue. The third is that uncertainty is not an issue in cooperative insurance, as it is not considered to be a financial transaction. The fourth being that cooperative insurance combined funds can be used to do what is required.[208]

Akin's decision was reached by the committee of *Ulama Al-Majma al-Fiqh al Islami*, where they decided that insurance is disallowed since someone is making profits from the misfortune of another and so, the only acceptable concept is on mutual or cooperative

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<http://en.themwl.org/content/fifth-resolution-insurance-its-various-kinds-and-forms> accessed 5 February 2014

[206] The resolution makes reference to Holy Quran in *Surah An – Nisa* (Chapter 4), Verse 29, that:

> "*O you who believe! Eat not up your property among yourselves in vanities; but let there be amongst you traffic and trade by mutual goodwill.*"

As the researcher would like to point out and the readers would note that according to *Quran* exchange of properties can take place where trading is involved.; <http://en.themwl.org/content/fifth-resolution-insurance-its-various-kinds-and-forms> accessed 5 February 2014

[207] Muslim World League, 'The Fifth Resolution on Insurance with Its Various Kinds and Forms' (en.themwl.og) <http://en.themwl.org/content/fifth-resolution-insurance-its-various-kinds-and-forms> accessed 5 February 2014

[208] Ibid

basis.[209] Author, Mahmoud A. El-Gamal, stated that cooperative insurance should not be the same as mutual insurance but as one, where claims payments find their way from the *tabarru* so to avoid the trap of *gharar*, by not entering a two way contract. Funds in *takaful* companies are invested in *halal* activities, thus avoiding the problems of *riba*, which is one of the scholarly opinions of proposed *takaful* operations as an alternative to insurance.[210]

On the mentioned committee meeting of the *Fiqh* academy of the Muslim World League, the late Dr. Mustafa Al-Zarqa was the only one who dissented. He argued that he did not consider there to be any basis that commercial insurance is any different from cooperative insurance, as proposed by the committee. In any insurance, the idea is of safeguarding and insureds contribute to the insurer funds, which grow bigger and require additional employees, as more and more insureds join in the scheme. He continued that the premium charged by the insurer should be on the appropriate analysis of the risk, which is the same in both existent and proposed insurance. In addition, Dr. Mustafa Al-Zarqa noted that, at this committee meeting, when the resolution was passed that considered insurance as *haram*, half of the committee members were not present. He emphasised that declaring a motion as grave as insurance needs to be confirmed by at least a majority of all members of the committee. Also, he went on to state that academic views of unrelated scholars need to be obtained and considered before declaring a prohibition on a necessity such as insurance. However, Dr. Mustafa Al-Zarqa was strict in his view that, where insurers are involved in a monopoly to unjustly charge higher premiums or unfair terms, *Sharia* enforcement should take place to avoid exploitation.[211]

Author Mahmoud A. El-Gamal has also considered some of these aspects in his literature and quoted some of the important views of Dr. Mustafa Al-Zarqa during his lifetime. Dr. Mustafa Al-Zarqa stated that he found no evidence in Islamic texts which confirmed that

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[209] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) pp. – 60 - 61

[210] Mahmoud A. El-Gamal, *Islamic Finance: Law, Economics and Practice* (Cambridge University Press 2009) p. - 148

[211] Muslim World League, 'Muslim World League dissenting view' (en.themwl.og) <http://en.themwl.org/content/dissent-dr-mustafa-al-zarqa> accessed 5 February 2014

insurance is prohibited, but instead noted that the overriding ideology in Islam is "*...to point jointly toward its permissibility and approbation, as a means of eliminating risk and loss*".[212] Dr. Mustafa Al-Zarqa further commented that those who argued to the contrary have unnecessarily raised hesitation in the community and portrayed a dim view of insurance. He continued "*...Some of those who raise such doubts are driven by obstinate desire to defend earlier opinions that they had issued in haste, and find it psychologically difficult to admit their faults, and others for various other reasons but without belief in what they say.*"[213]

A similar decision has also been received by Dr. Rafiq Yunus Al-Misri, who determined that insurance in general is acceptable and he mentioned *Sharia* scholars' approach at times to dealing with controversial matters. He mentioned that, by approving cooperative insurance, in principle they have accepted that insurance is allowed without concurring on details. He further stated that "*...I prefer permissibility of insurance, without hiyal (legal stratagems, or ruses); for these are jurists who forbid one thing, and then return to permit by various legal stratagems and means of circumvention, without worry or shame...*"[214]

Correspondingly, Adil Salahi, who was a regular article commentator in the Saudi Arabia newspaper "Arab News", initially was against insurance by following the ruling of the *Fiqh* academy of the Muslim World League. However, he later changed his mind and approved insurance as being acceptable to Muslims following correspondence with Ishaq Khan, then director of the CCI insurance company in Saudi Arabia. The correspondence of Ishaq Khan published in Arab News on 17th September 1988 highlighted some crucial historical acceptance of insurance in Islam. Ishaq Khan explained that insurance provides for humanitarian causes and encouraged scholars to study with any prejudice. He pointed out that one of the earliest *Sharia* approved insurance companies was set up in 1932 called "*Eastern Federal Union Insurance Company*" in Calcutta, India by the eminent Muslim scholar, the late Abdul Rahman Siddiqui, who had the support of important

[212] Al-Zarqa (1994, p. 8); Mahmoud A. El-Gamal, supra at pp. – 147 - 148
[213] Al-Zarqa (1994, p. 9); Ibid
[214] Al-Misri (2001, p. 6); Ibid

leaders of the time including the Nizam of Hyderabad, the Nawab of Bhopal and the Aga Khan III. Then, in 1934, under life chairmanship of Dr. Mohammad Iqbal, a prominent Islamic poet set up a *Sharia* approved insurance company in Lahore, Pakistan called "*Muslim India Insurance Company*". Temptation did not drive his motivation and, for that purpose, he limited it to 1 share only of four rupees even though, at times, he signed and authorised policies, which goes on to show the relevance and acceptance of insurance in earlier times.[215]

Equally, the Islami *Fiqh* academy (*Al Majma Al Fiqh Al Islami*) on their fourth meeting on 9th-12th August 1991 at Hyderabad, India approved life insurance as being acceptable, following the footsteps of *Darul Uloom Deoband,*[216] which confirmed a *fatwa* approving insurance in Islam and that of *Majlis-e-Tahqeeqat Shariah* in Lucknow, India who had also approved insurance by publishing a *fatwa* in 1965. However, the *Darul Uloom Deoband* in 2010 passed a *fatwa* confirming that the majority of insurance is non-Islamic because of the presence of "*interest and gambling or only gambling*".[217]

Conversely, the Islami *Fiqh* academy considered the insurance position in greater detail in their fifth meeting in 1992 at Azamgarh, India and confirmed that, although present insurance practices are invalid as per *Sharia* due to *riba*, *gharar*, *maisir* etc., they were still considered to be applicable in Islam under the doctrine of *"Azzaroorat taba'al Khatoorat, Rafa Zarar, Dafa al Harj, and Tahaffuze Jaan wo Maal (The necessity at the time of danger, combating the damage, eradicating the peril, and protection of life and property)".*[218]

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[215] Aleem Khan Falaki, supra at Chapter 3 Article 5 <http://li.aleemkhanfalaki.com/chapters/adil-salahis-views-on-insurance/> accessed 7 February 2014

[216] Darul Uloom Deoband is an Islamic University and school of thought in India <http://www.darululoom-deoband.com/> accessed 6 February 2014

[217] Darul Uloom Deoband, 'Fatwa' (darulifta-deoband.org) <http://www.darulifta-deoband.org/showuserview.do?function=answerView&all=en&id=24243&limit=10&idxpg=0&qry=%3Cc%3ETAD%3C%2Fc%3E%3Cs%3EUAI%3C%2Fs%3E%3Cl%3Een%3C%2Fl%3E> accessed 6 February 2014

[218] Aleem Khan Falaki, supra at Chapter 3 Article 1; <http://li.aleemkhanfalaki.com/chapters/islami-fiqh-academy-al-majma-al-fiqh-al-islami/> accessed 5 February 2014

In relation to the extra funds, which are reached when compensation is received, that is generally considered as *riba*, a *fatwa* was approved by Mufti of Darul Ifta on 19th February 2001 approving such additional funds as acceptable for Muslims in a non-Muslim jurisdiction, provided there is no fraud involved. It was stated that *"...By Shariah it is not Riba. This comes under the 'Aqd Fasid' (a contract between a Muslim and a non-Muslim. It also means a disliked contract, which can not be avoided)..."*[219] Also, the *Nadwat ul Ulema*[220] committee in their December session in 1965 conferred about insurance and its legitimacy. They concluded that insurance, like any transactions, is bilateral and if both parties are Muslims then Islamic law strictly followed. However, where the transaction is between Muslim and non-Muslim and such cases of insurance contract, the committee confirmed that insurance is not without *riba* and gambling, but that given insurance runs deep in daily life, insurance can be allowed for emergency purposes only, which includes risk of intolerable loss of life, property and dependants.[221]

Additionally, intellectuals such as Dr. Mohammad Al Awwa concur that insurance is a necessary element and is acceptable under *Sharia* law. He makes reference to a few *hadiths* to justify his point, with the first one stating the preventative ideology that is mentioned in a *hadith* of Prophet Mohammed (pbuh) that "*If a Muslim sees his brother being exposed to a grave risk of a great loss but does not take steps to protect him and spare him such risks and losses, he actually gives him away and lets him down*". He goes on further to stress the importance of insurance to mitigate adversity by mentioning another *hadith* of Prophet Mohammed (pbuh) that "*Whoever relieves a Muslim of one hardship of this life will be relieved by God of one of the hardships of the Day of Judgment, and whoever makes things easy for a person in a difficulty will have his things*

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[219] See Alamgeeri, Vol. 3, page 131; Aleem Khan Falaki, supra at Chapter 3 Article 3 <http://li.aleemkhanfalaki.com/chapters/jamia-nizamia-hyderabad/> accessed 7 February 2014

[220] Nadwat ul Ulema is a religious and educational Association and Institute for Islamic Learning in India; <http://www.nadwatululama.org/index.php> accessed 8 February 2014

[221] Dr. Mohammad Muslehuddin, 'Insurance and Islamic law' *Newspaper Dawat* (New Delhi, 4 March 1966) 164 – 165; **Also:** Aleem Khan Falaki, supra at Chapter 3 Article 4 <http://li.aleemkhanfalaki.com/chapters/nadwat-ul-ulema-lucknow/> accessed 7 February 2014

made easy by God both in the life and in the life to come." This, the scholar argues, is suffice to see how imperative it is that insurance is used and allowed in Islam.[222]

Joining him in a similar agreement is another intellectual, Dr. M. Haitham Al Khayyal, mentioned on the Arab News on 17th June 2002, who supported strongly that, for mitigation of risks in daily life, it is constructive to work cooperatively. He refers to a *hadith,* where Abu Musa Asha'ari quoted Prophet Mohammed (pbuh) mentioning that "*When the Ash'aries are on an expedition and they happen to run out of food supplies, or if food becomes scarce for their families in Madinah, they put together everything they have in one lot and divide it all equally among themselves. They belong to me and I belong to them*". This showed that it is acceptable in Islam when those types of schemes are created in order to help those mutually in need. Dr. M. Haitham Al Khayyal, in the same newspaper, goes on further to discredit arguments that ignorance is present in insurance as he expressed that the law of large numbers,[223] which forms actuarial mathematics, shows it is incorrect. He stated that insurance has no relationship with betting and gambling and usury is non-existent in insurance. He sums up by stating that insurers work in return for premiums, by investing to maximise the funds and that expansion of insurance can have a higher public benefit.[224]

However, author Sayid Abul A'la Mawdudi remains steadfast when he says that insurance is *haram* and points out three main proscriptions against traditional insurance by *Sharia*, which is that investment by insurance companies is *haram*. Also, that excessive payment as compensation is considered containing elements of *gharar* and inheritance distribution, in the event of death, is not in line with *Sharia* law, rather on a nominated individual as in the policy. He opined that *haram* could not become *halal*

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[222] Aleem Khan Falaki, supra at Chapter 3 Article 6 <http://li.aleemkhanfalaki.com/chapters/awwas-views-on-insurance/> accessed 5 February 2014

[223] The Law of Large Numbers (LLN) is an arithmetic theorem which manages on matters that takes place a significant number of times and is used by actuaries in insurance companies in calculating the risk factors, which in essence deceases as the number of happenings increases. Aleem Khan Falaki, supra at Chapter 5 Article 3 <http://li.aleemkhanfalaki.com/chapters/what-is-risk-and-law-of-large-numbers/> accessed 9 February 2014

[224] Aleem Khan Falaki, supra at Chapter 3 Article 7 <http://li.aleemkhanfalaki.com/chapters/haitham-khayyal-views-on-insurance/> accessed 7 February 2014

simply because insurance is crucial nowadays. However, Sayid Abul A'la Mawdudi goes on to mention that, to make an insurance operation *Sharia* compliant, investment can be made on a partnership basis on *halal* activities and sharing returns on a proportionate basis. He goes further that in life insurance, inheritance would be distributed as per *Sharia* laws and be share only the actual funds contributed, but if surpluses are there then it be considered that parties enter into partnership agreement to invest and make returns, which is to be shared proportionally.[225] On a similar note is another key academic, Dr. Mohammad Hashim Kamali, Professor of Law at International Islamic University of Malaysia, who stated that *gharar* remains present in *takaful*, like in traditional insurance, but the extent of this is reduced in the former. This is because the *takaful* is set on cooperativeness and mutuality, which lacks the competing interests between insurer and insured, as present in traditional insurance.[226]

Other thinkers such as Syed Ahmed Urooj Qadri Rahimahullah have strong views that insurance is just a combination of *riba*, *gharar* and gambling, where, like bankers, the insurers entice the prospective insured with the "*bait*" of compensation. However, worse than bankers, the paid premiums are lost if the insured default in their payment of further premiums and the culture of investment and compensation packages falls under *riba*.[227] Alongside him, Sheikh Al Azher, Al Sheikh Jadal Haq Ali Jadal Haq in Egypt on July 1995 issued a *fatwa* about illegitimacy in life insurance but emphasised that, in *Sharia,* the insuring of one's property is allowed in cases of "*fear of unjust enrichment, losses or destruction*". He made his determination based on the presence of unacceptable *gharar* and absence of a contact of mutual cooperation.[228]

In addition, two intellectuals of Saudi Arabia, Sheikh Mohammad Saleh Al Munajid and Sheikh Faisal Mawlawi, passed *fatwa* against the admissibility of insurance in Islam. They based this as there was no mention of insurance at the time of Prophet Mohammed

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[225] Sayid Abul A'la Mawdudi, *First Principles of Islamic Economics* (The Islamic Foundation 2011)
[226] Mohammad Hashim Kamali, *Islamic Commercial Law: An Analysis of Futures and Options* (Islamic Texts Society 2010) pp. – 93 - 94
[227] Aleem Khan Falaki, supra at Chapter 4 Article 1 <http://li.aleemkhanfalaki.com/chapters/syed-ahmed-urooj-qadri/> accessed 7 February 2014
[228] Aleem Khan Falaki, supra at Chapter 4 Article 2 <http://li.aleemkhanfalaki.com/chapters/sheikh-al-azher-egypt/> accessed 7 February 2014

(pbuh) and his companions had noted nothing in this respect. Also, they determined that insurance consists of restrictions of *riba*, gambling, ambiguity gharar and that insurance practice is a parlour game to trick individuals of their monies, which they based on the information as per a German expert who stated that payout is less than 2.9% of the premiums paid into. However, they did approve of cooperative and mutual Western insurance, but expressed reluctance for traditional insurance, but only in time of need and even then to take the minimum cover required only.[229]

Interesting, author Aleem Khan Falaki refers in his literature, two *fatwas,* where the intellectuals concurred that all insurance contacts are *haram* due to the presence of gambling and *gharar*. Rather strangely, they determined that the compensation received by the victim of a defined casualty from the insurer is *halal* because the victim has a right to pursue and obtain his entitled compensation for the tort, irrespective of whoever is required to make the payment, as the latter is not the victim's responsibility. The thinkers made a distinction between the contractual relationship between the insurer and insured, from the tortuous relationship between the insurer and victim. Aleem Khan Falaki raised concerns about the justification of these *fatwas* as it is turning a blind eye on the necessity of taking insurance cover, but proactive in approving the compensation element. He doubted that, without taking an insurance cover in the first place, there is no compensation to claim and the *fatwas* contradict as if taking insurance is *haram*, as it fails to justify how the outcome of a *haram* instrument can be *halal*. Aleem Khan Falaki does not appear to approve the thinkers' stance and stated that, for the fairness of the society, insurance is to be acceptable in Islam.[230]

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[229] Aleem Khan Falaki, supra at Chapter 4 Article 3 <http://li.aleemkhanfalaki.com/chapters/saleh-al-munajid-faisal-mawlawi-saudi-arabia/>; Accessed on 7/2/14 at 12:32

[230] The author refers to an interesting example of theft, which is prohibited in Islam. He explains that when a man steals monies, it is *haram* but if the family knows about the stolen monies and yet uses it, the author is perplexed, how it can be rationalized to be *halal*. He highlights an analogous point that if under the *fatwa* the source of compensation is unnecessary, then it could very well be argued that a blind eye be turned to how the insurers deal and invest their funds and concentrate only on compensation.
The author explains further that until the compensation is paid off, it could be very well possible that the tortfeasor will be in prison (of course this depends on which jurisdiction but in most Islamic jurisdictions such as in Saudi Arabia, the tortfeasor would face sentence until the penalty is paid off). This in essence makes not only the innocent victim's family to suffer from unable to obtain the requisite compensation in the right time but also, the tortfeasor's family, who are innocent as well, suffer. This cannot be in good conscience being just & fair and to restrict a scheme which would have allowed such injustice and

Additionally, Aleem Khan Falaki refers to an article from The Milli Gazette (dated 1-15 April 2002), which made reference to an important *hadith* of Prophet Mohammed (pbuh) about doing one's best and then relying on God, which supports the acceptability of insurance in Islam. The *hadith* quoted that: "*Anas Bin Malik reported that one day a Bedouin came to the Prophet on a camel and asked him: 'Can I leave the camel alone (without tying it to any tree) and trust in Allah?' the Prophet said: 'Tie your camel first, then put your trust in Allah' (Tirmizi).*"[231] Comparably, Syed Othman Alhabshi and Shaikh Hamzah Razak also related the same *hadith* in their article and exemplified the need to make arrangements to avoid risks.[232] Also, The Milli Gazette cited the authority of Imam Ibn Rajab, who confirmed that putting trust in God deos not mean that one avoids doing the basics as God ordained but doing so, following God's laws and trusting in Him alone.[233]

They went further to state that Prophet Mohammed (pbuh) had taken steps in his lifetime to avoid risks as well, which included the time when he hid in a cave initially to avoid a conflict during his migration from Makkah to Medina, when he split his companions in separate battalions rather than a whole troop and also when he used to wear body armour during wars for protection. Also, citation was made from Dr. M. Najatullah Siddiqui who commented that Muslims are required to have patience and submit to God alone, but that does not reflect that they should not take steps to avoid disasters. He continued that it is compliant within *Sharia* rules that actions be taken "*to avoid risks and financial losses individually as well as collectively. It is obligatory on him to take precautions against every kind of risk...*" As the above commentaries suggest, it has been encouraged that steps be taken to avoid risks in this lifetime in a *halal* manner, either solo or as a group.[234]

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unfairness to take place cannot be accurate. Aleem Khan Falaki, supra at Chapter 4 Article 5; <http://li.aleemkhanfalaki.com/chapters/arab-website/> accessed 7 February 2014

[231] Aleem Khan Falaki, supra at Chapter 9 Article 3 <http://li.aleemkhanfalaki.com/chapters/adil-salahis-views-on-insurance/>; accessed 10 February 2014

[232] Syed Othman Alhabshi and Shaikh Hamzah Razak, supra at pp. – 191- 193

[233] Aleem Khan Falaki, supra at Chapter 9 Article 3 <http://li.aleemkhanfalaki.com/chapters/adil-salahis-views-on-insurance/> accessed 10 February 2014

[234] Ibid

Also, scholars such as Syed Khalid Rashid noted that Muslim scholars had diverging views with some approving insurance, others not, while the remainder approved limited insurances. Interestingly, he points out that the famous *Shi'a* jurist, Ayatollah Khomeini, has approved insurance as sufficing a simple offer and acceptance, on the basis that the necessary contract basics are satisfied such as subject, parties, risk and premium payment.[235] Another well-known *Shi'a* jurist, Ayatollah Muhammad Vahidi, who supported the sanctity of the insurance contract, shared a similar view.[236] However, the *fatwa* Committee in Malaysia 1972 declared that the way life insurance was conducted in Malaysia was non-Islamic as it had *riba*, *gharar* and *maisir* in it. Syed Khalid Rashid maintained a neutral ground on his argument and emphasised that insurance is essential for daily life and the alternative *takaful* created may influence other jurisdictions to consider Islamising the insurance sector.[237]

Likewise, author Muhammad Anwar explains the historical basis when the 1972 meeting of Islamic Studies Conference (ISC) considered 80 opinions on insurance but remained deadlock with a decision about legitimising insurance. He noted that the Council of Islamic Ideology Pakistan (CIIP) decided insurance illegitimacy in Islam, but intellectual Abdul Malik Irfani disagreed with others in this decision.[238] Muhammad Anwar pointed out that insurance is rejected under *gharar* due to event uncertainty, claimed amount uncertainty and time of claim uncertainty. Yet, uncertainty exists on an individual level but not on a collective level, as per the law of large numbers and should be allowed under *darura,* i.e. necessity, and *masalahah,* i.e. public interest. *Maisir* is another reason for discrediting insurance as, like gambling, the insured is betting on event occurrence in order to claim. However, it is counter argued that, in gambling, either party can win or

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[235] Ayatollah Khomeini, *Tawzih al-Masayd* (1979), (Problem No. 5, 2863 to 2865) cited in S.H.Amin, 'Islamic Law in the Contemporary World', (Glasgow 1985) p. 79 mentioned in Syed Khalid Rashid, 'Islamization of Insurance – A Religio-Legal Experient in Malaysia', in the Textbook: Editors: M.Kabir Hassan and Mervyn K.Lewis, *Islamic Finance* (Edward Elgar Pulishing 2007), pp. – 408, 419

[236] Ayatollah Muhammad Vahidi, *Al-Masayil al-Mustasdaha* (1978), 11-13 cited in S.H.Amin, 'Islamic Law in the Contemporary World', (Glasgow 1985) p. 80 mentioned in Syed Khalid Rashid, supra at p. - 419

[237] Syed Khalid Rashid, supra at p. - 418

[238] Muhammad Anwar, 'Resource mobilization through the Islamic voluntary sector in Southeast Asia; Islam and the economic development of Southeast Asia: The Islamic voluntary sector in Southeast Asia' (1991) Institute of Southeast Asian Studies, p. – 423

lose, but in insurance there is uncertainty whether the event will happen in the first place, so there is nothing to lose. Also, with compensation capped to the amount of loss, unlike gambling, there is nothing extra to win. Gambling creates new risks that one willingly takes on, but with insurance it is management of existent risks, which one cannot avoid.[239]

Muhammad Anwar goes further to state that *riba* is a reason for insurance unacceptability as premium and compensation (if claimed) are never the same amount, so there is an increase without doing any labour and the insurer invests funds in *haram* activities. However, it is responded that compensation claimed is on the loss sustained and the intention of the premium payment is not to increase with time alone, but for cover. He cites Omar Farrukh, who commented that insurance is similar to a contract of guarantee between the parties, but he pointed out that Afzalur Rahman mentioned that the insurer's motivation of making "*profit out of the weakness of individual insurees*" damages insurance credibility in Islam. Hence, mutual insurance is approved, but Muhammad Anwar argued that making profit in Islam is acceptable and opined that the insurer's duty is similar to *zakat* managers for the sake of public security.[240]

Muhammad Anwar concludes that assurance aspect of *takaful* needs to be amended and recommended that, where compensation is received the insured and his heirs, in the event of a fatality, should continue making added payments, net of contributions paid, until the balance is cleared off. This extra payment received by the insured from compensation would be treated as *quad hasan*, with the aim to avoid claims exaggeration, risk transferring incentives and bypassing *gharar*. In cases where it is not possible to clear off this debt, relief could be provided from the *tabarru* fund or even cover the remainder from the insurer's *zakat* fund, the former being used to cover needy non-participants as

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[239] Muhammad Anwar, supra at p. – 424; Also see footnotes 190, 211, 218 and 223

[240] *Zakat* is the compulsory charity of 2.5% that every Muslim is required to give each year (as long as they meet the minimum possession criteria) to assist the poor and needy, so as to allow wealth distribution among society rather than funds remaining only with the rich. *Zakat* are generally provided to set up Islamic organization that collects the funds and manages the charity for appropriate allocation and for their management services it is natural that they charge a fee. Muhammad Anwar, supra at pp. – 425 - 427

well.[241] However, opinion differs with this recommendation of the author as, whilst it may appear to be a well-known moral dogma, it is not commercially viable particularly from an insurance business perspective. Whereas, avoiding the incentive for fruitless claims is certainly needed, but asking the insured to continue paying as if it is a debt is contrary to the idea of having insurance/*takaful* in the first place. If the insured is going to be liable to pay it off as a debt, it seems meaningless to waste costs to obtain cover, as he/she would have a better management of funds, if they used that fund for investment and made returns. Added that willingness to waive off the debt would become a norm rather than an exception on the implementation of such an approach, and assisting even non-participants from the *tabarru* fund is clearly contrary to business and legal ethics of insurance, as non-parties are taking a share of funds on which they have no claims at all.

Muhammad Anwar gives his second recommendation that indemnity should be set on actual lossess suffered and not on monetary set indemnity limit. This he argues that to avoid *riba* by indemnifying with a similar kind rather than exchanging premium money for compensation money and reduces the effect of inflation. This will also reduce *gharar* and *maisir* as indemnification is on real terms other than on set insurance limits.[242] Once more, the researcher disagrees with the author, since without a set limit, the insurer would not be able to analyse risks and to set the premium amount. With such an approach, the insurer faces unlimited risks and, on occasions, it will not be possible to replace the insured goods like for like, perhaps because of its value, rarity etc.

Alternatively, modern-day author Aly Khorshid stated that *gharar* is the central argument against the validity of insurance in Islam as he considered the insurance contract is an onerous contract (*muawada*) since parties have strict obligations, rather than voluntary contract. He pointed out the various cons of insurance by scholars, that the uncertainty of the insured paying without knowing whether the defined peril will ever occur has *gharar* present.[243] Also, the compensation is determined on the level of damage, as and when and if such event takes place, which goes contrary to the prohibition of *gharar* in a sales

[241] Muhammad Anwar, supra at pp. – 432 - 435
[242] Ibid
[243] Al Masri 1987b; Aly Khorshid, supra at p. – 61

contract in Islam, and thus has *gharar* present.[244] Islam is strictly against conditional and uncertain transactions so as to avoid disadvantage to any party.[245] Yet, Aly Khorshid counter argues that this is a farfetched interpretation of *Sharia* as, in Islamic law, validity is provided to some uncertain activities, e.g. wills, guarantees, etc. He agrees that insurance has uncertainties, but insurance provides the financial security in return for a premium; as such, uncertainties are acceptable for other Islamic instruments, therefore it should be no different for insurance. He refers to the well-known scholar Ibn Taymiyyah, who concurred that *gharar* is applicable to situations where uncertainty has prejudicial adverse effects on a contract by disturbing the balance of parties' rights and duties.[246]

Aly Khorshid goes along with the pros for insurance, in that *gharar* is pertinent in exact counter value exchanges rather than to a promissory financial cover from a contributed fund situation alone. He goes on to argue that an insurance contract deals with risks and so does not fit in with a goods or services sales contract in Islamic law. Before disregarding insurance, it is relevant to consider its functions of risk dealings and the prejudice it creates. He examines the *hadith* of Prophet Mohammed (pbuh)[247] and explains that the *hadith* referred to the aim of *gharar,* that is to avoid upsetting the parties' relation by any unjust capital enrichment. He mentioned that State and mutual insurance also has *gharar* but those are still considered as valid since the insured's funds are considered as a donation, a fact that is approved by *Sharia*.[248] He goes on to state that the reason *gharar* is present is to avoid prejudice and, other than the amount of compensation to be paid, which would depend on the level of losses, the parties' obligations are clear from the onset. The uncertainty is dependent on the occurrence of an insured defined peril, which is not the functional uncertainty *gharar* as indicated. He refers to established scholar, Mustafa Al Zarqa, who stated that security and peace has a price to pay[249] and it could be that insurance gives peace of mind, which calls for a

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[244] Al-Hafiz 1984: 2: 426-31; Ibid
[245] Khater 1985; Ibid
[246] Shalaby 1960; Ibid
[247] Aly Khorshid refers to the *hadith* of Prophet Mohammed (pbuh) in Book 9, Hadith 3675 of Sahih Muslim where Prophet Mohammed (pbuh) mentioned that:
"*Do not sell the fruit until their good condition becomes evident*"
[248] El-Atar 1978: 112; Aly Khorshid, supra at p. – 62
[249] Al-Zarqa 1984: 47; Aly Khorshid, supra at p. – 63

payment of price, the premium. In insurance, Aly Khorshid states that there are no unjust profits as compensation only covers the losses sustained and, if there is no claim, then the insured do not get any funds, which should demonstrate that *gharar* is inapplicable to insurance.[250]

Aly Khorshid goes further to point out that various scholars have disapproved insurance on the grounds of *riba,* stating that the fund difference between premium and compensation is an unjustified increase.[251] Other scholars have attempted to compare insurance with *sarf* (currency exchange)[252] and to show that *riba* exists in insurance as the instalment paid and compensation return is much higher.[253] Also, he pointed out that some scholars tried to argue under *maisir* that insurance is just like gambling, which depends on pure chance,[254] while others see insurance as an unnecessary voluntary act that is taken to enter a game of risk to make yields.[255] He mentioned various other reasons that different scholars have stated over time, justification of which does not hold up to scrutiny.[256] He stated that The Mufti of Jordan, Sheikh Abdullah El-Galgeily, decided that all types of insurances are invalid, that insurance is unlike traditional sales and not without gambling, usury or temptation and cheating, along with the insurer's tendency to put their own favourable terms and conditions. Equally, author Siddik Mohammed El-Amin El-Dareir argued that necessity of insurance did not make it illegal under *Sharia,* but supported cooperative insurance so that temptations can be avoided.[257]

Aly Khorshid concludes by attempting to keep a neutral view, but did not approve of the arguments discarding insurance. He opined that, whilst most *Sharia* scholars disapprove traditional insurance, they encourage mutual insurance, even though the same elements are present in the latter, by covering it in a different analogy of cooperativeness. He goes on to argue that the operational concept between traditional and mutual insurance is

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[250] Aly Khorshid, supra at pp. – 61 to 63
[251] Qadi 1984: 2:499; Aly Khorshid, supra at pp. – 63 - 64
[252] Muslehuddin 1966: 177; Aly Khorshid, supra at p. – 64
[253] Al-Dasuqi 1967: 177; Ibid
[254] Uways 1970: 98; Ibid
[255] Nejatullah 1985: 15; Ibid
[256] Aly Khorshid, supra at pp. – 64 - 67
[257] Aly Khorshid, supra at pp. – 67 - 68

hardly any different at all except with the argument of cooperativeness. He points out that, even if mutual insurance is considered to be more acceptable or profitable, it does not mean that commercial insurance is not allowed in *Sharia*.[258]

Consequently, authors such as Mohamed Akoob recognise that, under the concept of *ikhtiar,* i.e. preventative steps for the avoidance of possible hazards, these are allowed in *Sharia*. However, he cited that, in conventional insurance, risk handling by risk transfer takes place, which is seen as an exchange transaction and the insured obtains his uncertainty of events security by paying a premium, which is unacceptable in Islam. He mentions the presence of *riba*, *gharar* and *maisir* in insurance contracts as an exchange of monies taking place but for different amounts, with the uncertainty of an event occurring and the insurer trying is grow its business fortune on the insured's luck. Mohamed Akoob confers about the alternative to *takaful,* which works on cooperativeness so as to avoid *dhulum,* i.e. injustice, one of the important aspects of Islam.[259]

Additionally, some scholars have raised concerns about the rigidity of the arguments of *Sharia* restrictions of *gharar* and *maisir* that are suspected to hinder traditional insurance being considered acceptable in Islam. Author Oliver Agha mentions, in a similar mind-set as other scholars, that he does not opine that *gharar* has been interpreted in the correct manner and should not be applicable in the case of traditional insurance.[260] He argues that *gharar* relates to subject matter but, in the case of traditional insurance, the aspect is clear in that the insurer would have to pay if there is an accident. The only issue that is in doubt is whether the accident will happen or not and it is undisputed that the insurer will pay in the event of the incident.[261] Oliver Agha further argued that uncertainty in terms of the compensation payment is not within the remits of concern of *Sharia* restrictions, as the insurer is always there to make the payment in case of losses under insured perils, so in

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[258] Al-Fangari 1984: 55; Aly Khorshid, supra at pp. – 68 - 70

[259] Mohamed Akoob, 'Reinsurance and *Retakaful*' (2009) in the Textbook: Simon Archer, Rifaat Ahmed Abdel Karim and Volker Nienhaus (eds), *Takaful Islamic insurance: Concepts and Regulatory issues* (John Wiley & Sons Asia Pte.) pp. 151 – 154

[260] See footnote 250

[261] Oliver Agha, supra at pp. – 72 - 73

context there is no uncertainty as to the insurance contract itself.[262] However, it would be stated there are uncertainty of whether a payment needs to be made or not, depending on whether defined perils take place or not, leaving *gharar* within the scholarly debate ambit. In essence, the uncertainty in traditional insurance contracts relates to the subject matter itself on the ambiguity of occurrence of insured perils, which brings on the *Sharia* restrictions.

Oliver Agha also mentions different *Sharia* scholars' concerns about the presence of *maisir* in insurance and states that *maisir* relates to making money without labour by speculation. However, in the case of insurance, it is necessary to consider the mental element, which deals with the intention for protection rather than speculative fund maximisation and the business purpose of having insurance in the first place. He strongly disagrees that blanket denial of insurance without full consideration of all factors is unacceptable and asserts that insurance does not have the *maisir* element.[263]

Nevertheless, before concluding this section on various reviews, it is necessary that there be an opportunity to put forward independent views to argue back on some of the concerns raised by the scholars, to demonstrate a different picture. It would need to be stated that, as some scholars have already mentioned, they do not opine *takaful* contracts attract the restriction of *maisir*[264] as, unlike in games of chance such as gambling, where the probability of getting the hand is uncertain, the chances of a defined peril taking place are not the same. It can also be viewed that in *takaful* the risks taken are that of business risks, which is allowed in *Sharia* law as opposed to considering this equal to games of chance. The parties in *takaful* contracts are simply unaware of whether the insured perils would take place or not and it is a risk that both parties are taking on their assets, i.e. in the case of the insured, his funds and, in the case of insurer, his efforts. Whilst the above analogy may appear to be similar to a game of chance, if *maisir* is simply viewed alone objectively then it can also be construed that the outcome unpredictability is equal to the

[262] Oliver Agha, supra at pp. – 83 - 84
[263] Oliver Agha, supra at pp. – 72 - 73
[264] See footnote 223

various business venture risks that are taken with transactions, e.g. as in the event of a general *mudarabah* contract.

Additionally, *maisir* applies to games of chance rather than serious business, such as in *takaful,* and it could be argued that the hypothesis should not be applicable in such cases. However, this argument may not be very forceful as the application of the hypothesis may be applicable in all analogous matters irrespective of strict elucidation of the same. Nevertheless, it could also be argued that this paradigm can only work when *maisir* is viewed on its own; but when taken together with the restrictions of *riba* and *gharar*, taking *takaful* as a whole, the argument fails as then it stands to show that the parties are, in fact, entering into a transaction where there is no certainty of who comes out with what at the end of the day.

It is appropriate at this section to put in the researcher's analogy of his own views of the current *takaful* of utilising cooperativeness as the concept. Almost all scholars unanimously opine that a cooperative theme, in principle, is the acceptable way forward for structuring a traditional insurance alternative. However, most of them debate on whether, beside the cooperative concept, the remainder of the workings are set appropriately at all, in the existing *takaful* models.[265] A similar view is shared along with various scholars about different existing *takaful* models possessing a number of issues, which will be discussed in the next chapter. However, it is also asserted that the cooperative concept in itself can be the cause for concern from an insurance perspective. The way it stands at the moment is that cooperativeness is used in *takaful* with the principal aim that all the participants would contribute to a pot and, as different participants suffer specified perils (as may be the case), he/she can resort to the joint pot, where the collective funds are available to compensate them. So far, the idea is startling, with everyone working together on a common notion that is no different than mutual insurance that exists in the Western community, or from a marine insurance perspective,

[265] Restrictions of *riba*, *gharar* and *maisir* are the principle blockers. As would be witnessed in the next chapter where the researcher talks about the various existent *takaful* models on how they themselves are in contradiction of certain *Sharia* restrictions.

similar to P & I insurance clubs.[266] However, the Muslim society cannot consider mutual insurance or P & I insurance as they view the operations of these organisations are in contravention of the restrictions of *riba*, *gharar* and *maisir*, as discussed earlier.[267] To differentiate *takaful* from falling under the same problematic restrictions, the funds provided to the *takaful* operator are considered as *tabarru,* i.e. charity.[268]

However, the crucial aspect that is of concern is that, in both cases, the insureds/participants are putting funds in one pot with the aim of pulling out the funds as required. With P & I insurance in the Western community, at least it can be much more regulated as the fund provided is actually a premium from the insured with legal obligations and consequences, but in *takaful* it is simply a donation, which has hardly any legal or even *Sharia* standing for operation. Once provided, the giver of the donation has pretty much lost all rights of control over the fund. As a moral scheme, this can be fascinating, but it does not stand strong as a commercial venture. A commercial venture needs to have well-built foundations with control. To make matters worse, this *tabarru* when provided to the *takaful* operator by the participants is then intended to increase the funds and, as such, is then considered as an investment with only a portion fulfilling the intended destiny of cooperativeness.[269]

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[266] P & I insurance stands for Protection and Indemnity Insurance, which is similar to traditional mutual insurance where different ship owners, operators and charters come together to insure their trade mutually by putting funds in one joint pot. Where there is a loss by an insured perils to one of the insured ship owners, he / she can take the funds out of the joint pot to cover up for his losses i.e. compensate him / her for the damages suffered due to the insured perils. As per Professor Rhidian Thomas on a short seminar on 20/11/13 at Bangor University he opines that more than 90% of the world's international trading risks are covered nowadays by way of P & I insurance clubs.

[267] With the risk of repeating any of the points that the researcher has mentioned previously, the Muslim society sees that traditional insurance companies may be it orthodox insurance, mutual insurance or P & I insurance, all takes the funds of various insureds and invest in different projects to maximise the funds and get a good return. In the course of doing so, they would invest in projects which they think would make the highest return and this could include gambling, wines, swine meat etc., things which are prohibited in Islam under *Sharia*. At times, the insurers may even provide the finance as loans with mandatory returns, which in itself breaks the *riba* restrictions, as explained in details in previous chapters. Additionally, the insurer and insureds are entering contract which is *gharar* i.e. uncertain and even be considered *maisir* i.e. game of chance, which brings back to the same restrictions as mentioned earlier, why traditional insurance cannot be considered to be compliant with Islamic principles.

[268] There are some significant issues about considering the payment from participants as *tabarru* i.e. charity which has been discussed later in grave details.

[269] The researcher talks about this dilemma in more details in the next chapter as it doesn't make any sense that a charity contribution can be considered as an investment fund, which as such follows the investment principles of sharing and while a part of the fund is actually used for the principal aim of cooperativeness.

Even worse, following the researcher's own analysis, it is opined that existent *takaful* models are advancing some of the *Sharia* contraventions, which were intended to be avoided in the first place, as shall be witnessed in this section. For the sake of argument, if consideration were provided briefly on the working structure of lottery (which is a form of gambling), it would give more insight into the analogy. In lottery, various individuals purchase lottery tickets with different numbers, all of whom have one common objective of winning the funds from the jackpot. The total jackpot is determined on estimated regular sales by the lottery company and winning numbers are selected at random. Subsequently, the chances of winning are uncertain and an individual purchaser enters into a number of uncertain pacts with the lottery company. For example, the individuals simply does not know whether they will win or not, or even how much they will win, or whether part of their monies that will be used to purchase the lottery tickets would go to good causes and, if so, how much. Subsequently, the lottery company announces the winners and uses the remainder of of funds to invest and increase the funds with only a portion of that possibly going to good causes.[270]

As per the researcher's own perspective, there seem hardly any differences between how the *takaful* companies operate and the working mechanism of general lottery companies. All of them have a common pot from where the final withdrawals take place and this common pot was wholly filled by funds from various individuals who came together. Both of them are providing funds to individuals depending on uncertain events and happenings. Both of them are investing monies obtained from various individuals/participants to increase the accumulated funds and both of them provide only a portion of the monies that come in, for good causes.[271] The only difference that can be

[270] National Lottery website, 'Player' (national-lottery.co.uk) <http://www.national-lottery.co.uk/player/p/lotterydrawgames/lotto.ftl> accessed 22 November 2013

[271] The concept of good cause would no doubt be argued by *takaful* operators that it is for good causes and participants are covering each other for good cause out of kindness in their hearts. This, the researcher opines is a similar analogy of good cause stated by lottery companies as well of setting aside part of the monies obtained. Of course, even on a far fetched argument, it can be argued that in *takaful* companies, the good cause i.e. the cooperativeness, is the primary concern of *takaful* whereas in lottery companies, the good cause e.g. assisting of poor individuals and /or projects is a secondary concern. However, for a moment, if both the whole concepts are looked at objectively, in lottery case it can be stated to an extent that the good cause is secondary objective but it is not possible to state that the good cause is primary in

witnessed between the *takaful* operation and the lottery business is that the *takaful* operation masks the monies that are initially coming in from the participants, describing them as charity; but once it reaches the *takaful* operator by some unexplainable phenomenon, a portion of it then becomes an investment fund, which is simply farcical.

If the above analogy is considered, then the most distressing part of all this is that the *takaful* operation, under the facade of cooperativeness, has been conducting transactions containing significant amounts of *gharar* and *maisir*, the exact restrictions which were initially intended to be eliminated in the first place and the main reasons for discrediting traditional insurance. If the restrictions cannot be eliminated, then it is believed that either traditional insurance be embraced or a model be created distinct of cooperativeness so that these precincts can be overcome, as it is neither in the interest of law nor commerce to perform such unwarranted gymnastics with insurance structures. Having argued the above point, it is necessary to make it clear that it can be set explicitly that cooperativeness is certainly a great ideology and certainly is extremely beneficial in community and social building. The underlying principles of having a *halal* insurance product under Islamic law needs to be based on two concrete ideologies. The first is that, for business practice mainly of Islamic insurance and finance, emphasis on social welfare is necessary. The second, Islamic law encourages the fair distribution of wealth among parties. As Professor Tom Baker explains, the theoretical difference between traditional insurance and Islamic insurance is that the former is for individual risk abolition, whereas the latter is for risk abolition of a defined social group.[272] However, it is questionable whether the existent *takaful* models actually meet the requisite demands as expected.

Therefore, perhaps it becomes arguable whether existent *takaful* is the best paradigm to be used to create an alternative to traditional insurance, to take the place of a commercial venture. It is felt that, if there is to be expectation for improvement for a *halal* variety in economic advancement, it needs to start with modification from the core, i.e. with some

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takaful operation, as there is no legal or *Sharia* standing of *tabarru* when that *tabarru* turns to investment fund. There is no way to determine what portion is for cooperative assistance and what fund is for investment, when the initial payments are coming in as donations only.

[272] Hania Masud, '*Takaful*: An innovative approach to insurance and Islamic finance' (2010-2011) 32 U. Pa. J. Int'l L. 1133, pp. – 1141 - 1142

modification on how cooperativeness is structured with elements more advanced for commercial use. Nevertheless, as the current position stands among Muslims, it has become an acceptable norm that they consider traditional insurance to be objectionable. It is opined that, whilst there are arguments on both sides, for and against traditional insurance as witnessed above, it is most probably the case that the Muslim community desires a safer analogy by denying the whole traditional insurance as *halal*. It could well be the case in reflection of one of the *hadiths* of the Prophet Mohammed (pbuh), where it is mentioned in Book 34, Hadiths 267 of Sahih Bukhari that:

- *"Narrated An-Nu'man bin Bashir: The Prophet said 'Both legal and illegal things are obvious, and in between them are (suspicious) doubtful matters. So who-ever forsakes those doubtful things lest he may commit a sin, will definitely avoid what is clearly illegal; and who-ever indulges in these (suspicious) doubtful things bravely, is likely to commit what is clearly illegal. Sins are Allah's Hima (i.e. private pasture) and whoever pastures (his sheep) near it, is likely to get in it at any moment.'"*[273]

As it is quite apparent from the above *hadith*, Muslims are being warned to keep a safe distance from things that can be considered a mixture of *halal* and *haram* as per *Sharia* laws and guidelines. Islamic scholars are considered to be the authority in determining the permissibility of concepts that are a combination of halal and haram and it is considered orthodox that Muslims stay away from such things to keep their faith clean.[274] Without criticising scholars who are against insurance, as mentioned above,[275] it could be very well that the Islamic society considers insurance as a mixture of components of both *halal* and *haram*. Although it is recognised that insurance is a necessity, e.g. international trade marine insurance is obligatory, which in essence makes it a *halal* requirement to have for trade advancement, but the way traditional insurance is structured means it

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[273] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=34&translator=1&start=0&number=0> accessed 23 November 2013

[274] 40 Hadith Nawawi, 'Hadiths' hadith 6 (40hadithnawawi.com) <http://40hadithnawawi.com/index.php/the-hadiths/hadith-6> accessed 23 November 2013

[275] See footnotes 185, 213 and 214

contains a number of *haram* components, as mentioned earlier. This may have been discouraged, even considering that *halal* substitutes can be created. It is also important to point out another important *hadith* of the Prophet Mohammed (pbuh), which is mentioned in Book 40, Hadiths 4590 of Sunan Abu-Dawud, where the Prophet Mohammed (pbuh) mentioned that:

- "*...I enjoin you to fear Allah, and to hear and obey even if it be an Abyssinian slave, for those of you who live after me will see great disagreement. You must then follow my sunnah and that of the rightly-guided caliphs. Hold to it and stick fast to it. Avoid novelties, for every novelty is an innovation, and every innovation is an error.*"[276]

The part to focus on is the Prophet Mohammed's (pbuh) warning to avoid creating new practices that would distract from the original religion of Islam. It is asserted that this could be another reason why the Muslim community are concerned with making major developments. This has led to the society even unable to comprehend models, which could be within the usual acceptable norms. There is no doubt that all these are creating significant problems as they impede the economic advancement of Islamic community within the rest of the world. A clearer alternative, which would be more obvious as complying with the *Sharia* principles, would bring confidence in the Islamic society in accommodating insurance as acceptable within the religious boundaries. However, a view that is shared with the scholar, Hania Masud, is that the advancement of Islamic finance principles to on-going economics presents exceptional challenges.[277]

6. Conclusion - The future of *takaful*:

The main countries to welcome *takaful* include Malaysia, Pakistan and the Gulf States with expansion opening in South East Asia and in the West, possibly due to Muslim

[276] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=40&translator=3&start=0&number=4590#4590> accessed 6 February 2014
[277] Hania Masud, supra at p. - 1133

population expansion.[278] Although the *takaful* industry has been expanding, its growth has not been as great as expected, mainly due to lack of investments and regulatory requirements hindering competition. There is a market to be tapped into, as Muslims with strong beliefs should instantly be interested in purchasing this service in comparison to traditional insurance. However, for some reason or another, Islamic financial institutes have not proactively pursued this course of action,[279] which could be attributed to the attractiveness of the *takaful* models as operations.

The principle ideology that the *takaful* relationship between the *takaful* operator and the participants are by cooperation, which isn't dispusted among the scholars but the models of cooperativeness certainly need upgrading and perhaps even amending to an extent.[280] The reason for such a suggestion is because the ways the existent models are structured have a significant number of flaws present in them, as discussed in the next chapter. One of the central concepts of all the *takaful* models that are in use to date is the concept of *tabarru,* i.e. contribution provided by the participants counted as charity to work alongside the cooperativeness paradigm. The problem is that the concept of *tabarru* is considerably bungled and has lost its primary context, which simply does not fit in with the big picture of having an effective insurance alternative model. It is commonly agreed between the various scholars that one of the main reasons that traditional insurance is not even considered to be *Sharia*-compliant is because of the restrictions of *gharar* and *maisir*,[281] in terms of the fact that the insured is paying a premium for events, which may or may not happen and for an unknown amount of monies; as such, the outcome is unknown at the time of conclusion of the contract between the parties. *Sharia* scholars have, as mentioned earlier, introduced *tabarru* concept clothing the fund as a charitable payment; as such, restriction arguments are inapplicable for charitable payments. However, it becomes very dubious as to whether that is sufficient and, with the greatest respect, even valid or justified. The later chapters go into great detail on the deficiencies of present-day *takaful* models.

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[278] Haemala Thanasegaran, supra, pp. – 104 to 106
[279] Muhammad Ayub, supra at pp. - 428 - 431
[280] Ibid
[281] These restrictions have been talked in significant details in the previous chapters.

In summary, as can be witnessed from the paragraphs above, Islamic scholars have aimed to devise an instrument, i.e. *takaful*, which is geared to doing a similar action as traditional insurance. During the process of structing of such alternatives to traditional insurance, may it be a rash decisions or neglected errors, the *takaful* models have been inflicted with various lackings, which are detailed later on in the next chapter. It is not possible or relevant to dwell on the cause of the same as this would hinder commercial advancement, but these concerns have been echoed by other authors as well. Alongside the fact that Islamic finance have been running to grasp up with traditional finance to make like for like products, this is resulting in risking bigger and bigger hazards on unsuitable and inflexible instruments.[282] Dressing up Islamic products like traditional products might not be the best solution; having said that, however, it is not felt that there is any harm in doing so, as long as the *Sharia* rules are complied with and errors can be reduced to the minimum, as much as possible.

In conclusion, it is relevant to cite from Aleem Khan Falaki, author of "*Life insurance and the Muslims*", where he highlights his opinion on reasons for contradictions among Muslims about insurance. One major point is that authors of most of the literature are predominantly from Islamic states, e.g. Pakistan, Egypt, Saudi Arabia, who lack the experience of multi-religious, multicultural societies and, therefore, lack the application knowledge of providing a practical solution in such cases that would cater to everyone's needs. As circumstances are different, thus the application of any Islamic opinions would be different as well. Islamic states such as Saudi Arabia have strict laws and citizens follow the law well otherwise the punishments are severe, but the same is not applicable in mixed societies. Application of Islamic opinions of important concepts such as insurance is not a simple aspect, particularly where Muslims may be among the minority in a multicultural community.[283]

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[282] Oliver Agha, supra at pp. – 69 to 70

[283] The author gives an interesting example about Muslims celebration of Eid, when the date of Eid is determined on the sighting of the crescent shaped moon. As an instance, although a crescent shaped moon may be seen in Saudi Arabia at night configuring that Eid determined to be celebrated on the next day at Saudi Arabia that does not mean that Muslims in India would also follow the crescent moon sighting of Saudi Arabia. The latter would want to wait until the crescent moon is seen on their land before

Aleem Khan Falaki goes on further to mention that, at present, there are no simple Islamic insurance texts that give a straightforward answer to whether insurance is acceptable in *Sharia*. The majority of books start with Islamic models without much justification of their authenticity lineage and he noted that the readers are faced with dead ends, making them more confused than when initially started and their questions remain unanswered. Most scholars have adopted a theoretical approach to these perplexities in complex wording, without providing a practical solution that resulted in "*Islam's real teachings remain on the dusty shelves next to the antiques*".[284]

It is strongly agreed with the comments of Aleem Khan Falaki and it is maintained that any proposed models need to comply with *Sharia* rules, but at the same time must have the flexibility to adapt to different environmental circumstances. It is correct that, from land to land, residents are different and, whilst in Country A most individuals may not be concerned about insurance much but it could be in Country B most individuals have iniquitous attitude of making various insurance scams.[285] Models need to be created that meet at least the minimum requisite of both worlds. In this respect, a proposed *takaful* model needs to configure and include the vital elements of premium, risks, excess and compensation, which form the contract construction framework of insurance. These elements needs to be designed to work in a proposed *takaful* model in their right characteristics rather than disguising them into something else, e.g. as in present day

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determining the Eid celebration date. The point that the author attempted to make is that, it is is not possible to have Universal application of Islamic law opinion, just basing the conditions of Islamic dominant state but rather an open minded approach needs to be adopted to make a suitable and flexible model.
Another example, the author gives which is quite distinctive in Islamic dominant countries and multicultural countries, where to get daughter married in Saudi Arabia, the father does not have to worry about finance and knows that the prospective son-in-law would take care of such expenses. Whereas, countries such as India and Bangladesh, the father of an unmarried daughter faces significant hurdles as without finance he will not be able to secure a good hand in marriage for his daughter. Although under Islamic law, the men is supposed to protect and provide, but, may be cultural or otherwise, a different trend had emerged and that is how the system is following differently in multicultural country. The aspect once more is that, it simply does not make sense to make *fatwas* and apply universally without considering the circumstances fully. Aleem Khan Falaki, supra at Chapter 10 Article 5 <http://li.aleemkhanfalaki.com/chapters/vague-literature-on-insurance-issue/> accessed 6 February 2014

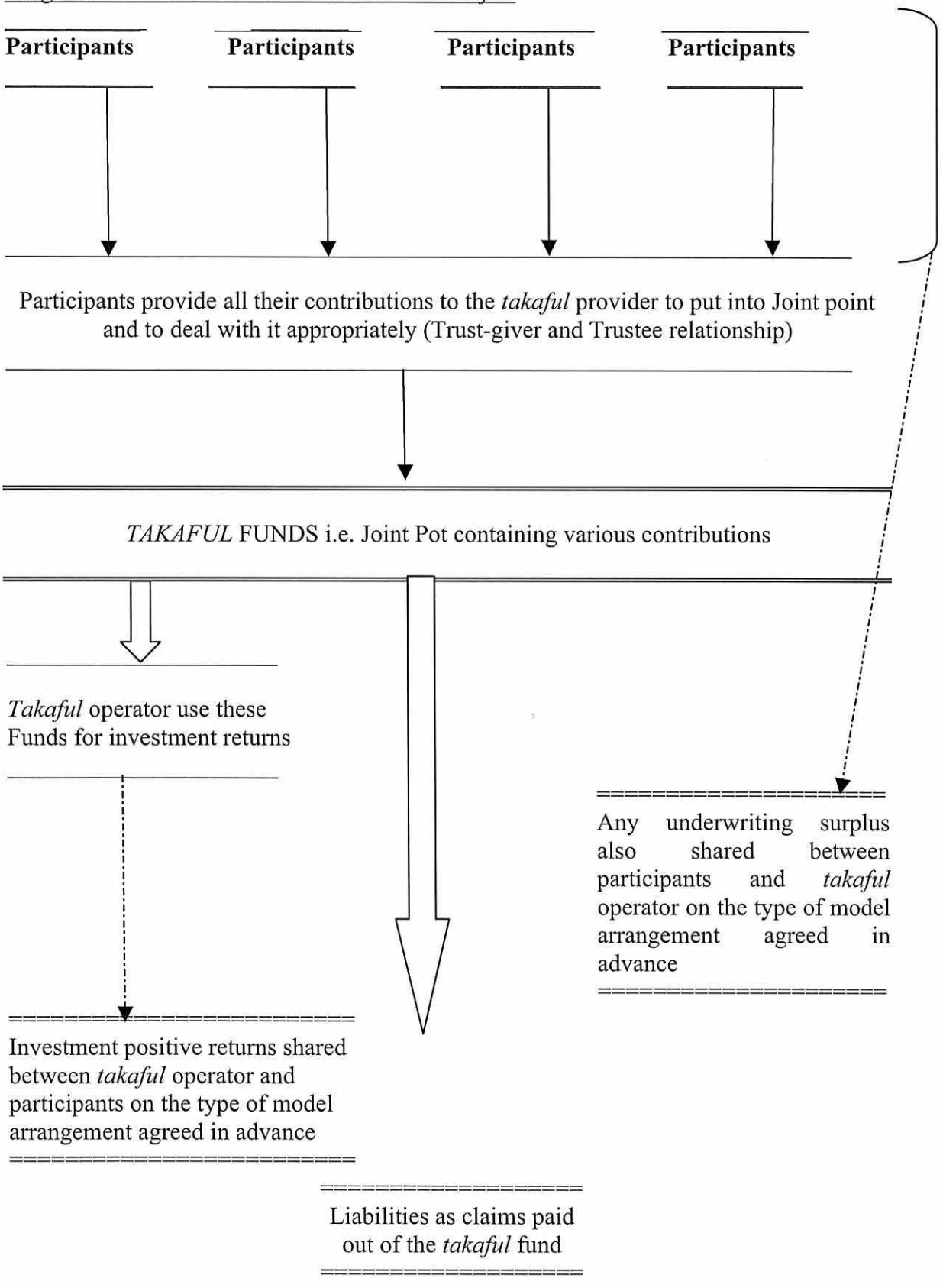
[284] Aleem Khan Falaki, supra at Chapter 10 Article 6 <http://li.aleemkhanfalaki.com/chapters/if-but-can-and-should-philosophy/> accessed 7 February 2014

[285] Of course, this is for illustrative purposes but it is no secret that in insurance, false claims are a calculated risks that is on the books of insurer, they are bound to face

takaful camouflaging premium as a donation payment. The presence of relevant elements in their correct working manners in a new *takaful* model could pave the way forward.

In the previous chapter, the configuration of a premium payment and risks in a proposed *takaful* model have been presented. As this research revolves around the marine insurance of goods, additional elements such as excess payment may be configured to act as payment in return to the insurer, which could resolve the issue of excess payment, in a proposed *takaful* model. Also, if a proposed *takaful* model can be configured that, when the risk becomes adverse, it can be offset with a security payment of compensation, might pave a way forward for the creation of an ideal new type of *takaful* model. This thesis continues the journey with searching for and discovering such a *takaful* model in mind.

Diagram 5.1: General overview structure of *takaful*:



Part III

The basics of Islamic Insurance

Chapter 6: The various models of *Takaful*

1. Introduction:

This chapter will talk about various models of *takaful* that are being practised presently with the aim of giving efficiency to insurance from a *halal* perspective. There are a few models that have been established in practice, which will be considered in detail in this chapter.

The general Islamic *fuqaha* maintains that anything that works with unity among parties is an acceptable form of *takaful*. Therefore, *takaful* models being made with *Mudarabah, Wakalah*, hybrid of *Mudarabah* and *Wakala* along with the new model of a hybrid of *Mudarabah*, *Wakalah* with *Waqf* appear to be the most popular at the present moment. This thesis shall go into more detail about each of these models and point out the incompatibility aspects that restrict the same into being utilised into the UK marine insurance sector. It is important to note that there are hardly any textbooks that discuss in detail the model itself; rather, in most cases, the facts are restricted to free scale illustrations of the models.

2. *Takaful* models:

As outlined, there are a number of takaful models in existence. However, the model discussed appears to be divided depending on the region. The South East Asian jurisdictions, such as Malaysia, primarily utilise the *mudarabah* model, whilst the GCC

countries,[286] i.e. jurisdictions in the Arabian Peninsula such as Saudi Arabia, primarily utilise the *wakala* model. It appears to be more a personal choice of the governments of each jurisdiction. In any event, it is opined that, despite the utilisation of different models, there is much that is lacking in the present models, which do not have a sufficiently strong foundation to withstand the practicality of entering and serving the UK marine insurance. Author Mohd Ma'sum Billah considered three different *takaful* models that are present throughout the world, namely *ta'awuni* as practised in Sudan, *wakala* as practised in Bahrain and *tijari* as practised in Malaysia.[287]

It is necessary to mention that, despite the complexity illustrated by the various names, the operation of *takaful* is very straightforward. It is actually similar to working results of traditional insurance that is seen in Western society, as demonstrated by diagram 6.1 in the annex.

As can be witnessed from the diagram, the working structure of both traditional insurance and *takaful* is very much the same, with the end result being that of risk coverage. However, a distinctive factor of *takaful* is that the relationship between the *takaful* operator and participants is determined on whichever *halal* vehicle the parties intend to utilise, may it be *mudarabah*, *wakala* or any others that have been developed. In traditional insurance, this problem does not arise, as the contracts are straightforward and do not have the *riba*, *gharar* and *maisir* restrictions holding them back. Nevertheless, all the various *takaful* models practised are considered in detail below. It is necessary to point out that, due to limited scope of this thesis, analysis would be constricted to consideration primarily about the various models of general *takaful* and not family *takaful*. This is because the former deals with everything other than life insurance, which is the subject of the latter, and the aspects are different, calling into account different types of analyses and models, including different Sharia issues.

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[286] GCC i.e. Gulf Cooperation Council countries includes Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, UAE, the last of which includes the territories of Abu Dhabi, Ajman, Dubai, Fujairah, Ras al-Khaimah, Sharjah and Umm al-Quwain.

[287] Mohd Ma'sum Billah, 'Islamic banking and the growth of *takaful*' (2007) in the Textbook: M. Kabir Hassan and Mervyn K. Lewis (eds), *Handbook of Islamic Banking* (1st edn, Egward Elgar Publishing Limited 2007) p. – 406

3. *Mudarabah*, the concept:

3.1. Introduction:

Before looking in detail at how *mudarabah* has been circumvented to make *takaful*, it would be necessary to give some insight into the concept of *mudarabah* itself. *Mudarabah* is a concept of an investor/entrepreneur relationship, where the investor gives the whole funds for the project and the entrepreneur gives his labour for the project. The investor is known as *rubb ul mal* (also known as *sahib al mal*)[288] *and* the entrepreneur is known as *mudarib*. When *rubb ul mal* invests the money, it is defined in the contract whether the *mudarib* has the flexibility to invest in a particular business or to invest in any business.[289] A lengthy authoritative definition of *mudarabah* was provided by Imam Quduri, the relevant part of which he mentioned "*Mudarabah is a contract of partnership in profit by doing business with the capital of one partner and the action of the other partner. Mudarabah is not valid except with such capital with which partnership is valid...*"[290]

The agreed portions of the profit outcome of the project are predetermined in advance between the *rubb ul mal* and *mudarib;* however, in the event of a loss, *rubb ul mal* carries the financial liability of the loss, whilst *mudarib* bears no income from the failed project. The analogy behind this is that the investor bears the risk of the business. The profit distribution percentage is negotiated between the parties depending on the transactions they are entering into, as long as it is not a lump sum amount or figures tied to capital.

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[288] Yusof M F, 'Fundamentals of Takaful' (Kuala Lumpur: IBFIM, 2011) <http://www.islamicbanker.com/education/takaful-%E2%80%93-mudarabah-model> accessed 31 January 2014

[289] Muhammad Taqi Usmani, *An introduction to Islamic Finance* (1st edn, Maktaba Ma'ariful Quran 2007) pp. - 47 – 50;
In the context of the *mudarabah* based *takaful* model, the participants and the *takaful* operator enters the *mudarabah* contract that the *takaful* operator as the entrepreneur has the flexibility in any kind of *halal* business that the *takaful* operator feels appropriate

[290] Justice Dr. Munir Ahmad Mughal, 'Mudarabah in the light of the Holy Qur'an and Sunnah of the Messenger of Allah' pp. – 3 - 4
<http://www.academia.edu/1645410/Mudarabah_In_the_Light_of_the_Holy_*Quran*_and_Sunnah_of_the_Messenger_of_Allah_> accessed 31 January 2014

The parties can conclude the business relationship whenever they feel it is convenient, unless it has been agreed specifically in the agreement, at any fixed period.[291] *Mudarabah* has been used as various methods of financing, including as an alternative to traditional banking, where the banks give interest instead of *mudarabah,* therefore it has been used to justify monies paid into account holders. However, the aim of this thesis is to concentrate on the aspect of insurance only and hence emphasis would be made on the concept of *mudarabah* in connection with *takaful* alone.

3.2. Religious law:

Mudarabah arrangement has been considered *halal* in Islam and the word *mudarabah* finds its roots from the term "*darb fi al-ard*" meaning to "*to travel the land*".[292] To understand the meaning of this further, it is necessary to look at the Holy *Quran* in *Surah Al – Muzzammil* (Chapter 73), Verse 20:

- *"Indeed, your Lord knows, [O Muhammad], that you stand [in prayer] almost two thirds of the night or half of it or a third of it, and [so do] a group of those with you. And Allah determines [the extent of] the night and the day. He has known that you [Muslims] will not be able to do it and has turned to you in forgiveness, so recite what is easy [for you] of the Qur'an. He has known that there will be among you those who are ill and others traveling throughout the land seeking [something] of the bounty of Allah and others fighting for the cause of Allah. So recite what is easy from it and establish prayer and give zakah and loan Allah a goodly loan. And whatever good you put forward for yourselves - you will find it with Allah. It is better and greater in reward. And seek forgiveness of Allah. Indeed, Allah is Forgiving and Merciful."*[293]

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[291] Muhammad Taqi Usmani, supra pp. - 50 - 53
[292] Justice Dr. Munir Ahmad Mughal, supra at p. - 7
[293] Holy *Quran*, '*Surah Al – Muzzammil*' Chapter 73 Verse 20 (quran.com) <http://Quran.com/73> accessed 24 April 2013

To understand the meaning of the verse, the whole paragraph needs to be considered, but the part to emphasise are lines 6 and 7, where God has allowed people to journey to find the rewards of God, which is what allows the *mudarib* by working and travelling in such transactions. It is noted that *mudarabah* has been practised since the early Babylonian times. It is noted by scholar Ebrahim (2011. p. 2-5) where he mentioned that: "*This financial arrangement was known and practised in the Near East as early as the Babylonians (see Udovitch, 1965), is known and discussed in the Talmud and later Rabbinical literature (see Jackson, 1980), and various forms of it were practiced by Meccan merchants preceding Islam (see again Udovitch, 1965), which explains its employment in early Islam.*"[294]

Similarly, in the *Sunnah* of the Prophet Mohammed (pbuh) before his marriage to Hazart Khadijah, he had a trading relationship with Hazart Khadijah when she offered finance and he would travel far distances in caravans, selling goods on her behalf and she would take his share from the profits of the sale.[295] As mentioned in the previous chapter 5, cited by Afzal-ur-Rahman, that an incident took place where Prophet Mohammed (pbuh) donated, along with others, to a contributory fund when an accident took place with camels and goods were lost in the desert.[296]

Also, according to an 11th-century Hanafi jurist, al-Sarakhsi, he mentioned an incident when the two sons of Umar, Abd Allah and Ubaydullah, came to stay with Abu Musa Ash`ari, who provided them with funds from the treasury to trade with, asking for the return of the capital but retaining the profits for themselves. When Umar found out, he demanded the return both of the capital and returns to the public purse; following a discussion, however, it was decided that Abd Allah and Ubaydullah were considered to be acting in the capacities of *mudarib*s so could retain half of the returns made.[297] Despite

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[294] Justice Dr. Munir Ahmad Mughal, supra at p. - 7

[295] Brian Kettell, *Islamic finance in a nutshell* (1st edn, John Wiley & Sons 2010), p. - 41

[296] See Chapter 2 footnote 1. Quoting from the author, Afzal-ur-Rahman who mentioned "*...Muhammad, who was trading with the capital of Khadijah, had also contributed to that fund from his profits*". This confirms that not only Prophet Mohammed (pbuh) was trading on someone else namely, Hazart Khadijah's funds but also he made profits with that and from which he had retain a portion as his share, that's because he was able to donate to the contribution fund from that of his profits.

[297] Justice Dr. Munir Ahmad Mughal, supra at pp. – 8 - 9

the restrictions mentioned in the previous chapters, particularly that of *riba* and *gharar*, *mudarabah* is considered as acceptable to these effects as the parties are entering a relationship of trading.

3.3. *Mudarabah* based *Takaful* model:

The general *mudarabah*-based *takaful* model works in line with the concept of *mudarabah*, as mentioned above. The concept of *mudaraah* is implemented into the foundation of *takaful* concepts of mutuality. To start with, the formula that is intended to represent such model, for ease of understanding, would be as follows:

Takaful Mudarabah = *Mudarabah* (contract) + *Tabarru* (fund/charity) + Cooperative loss sharing (principle)

The concepts of this formula will now be discussed in detail below. In a *mudarabah*-based *takaful* model, the prospective policyholder enters a *mudarabah* contract with the *takaful* operator, where the policyholder provides funds similar to a premium. The policyholder is considered as the *rubb ul mal* and the *takaful* operator is considered as the *mudarib*. This is because the policyholder is providing the capital solely by himself/herself, whilst the *takaful* operator is considered to be doing the labour of underwriting and asset management. When the premium is provided, the parties arrange in advance a fixed profit sharing ratio, when a profit takes place from the returns of premium investment. In *takaful* operations, a close eye is kept on the point of *riba* restrictions on the premium, since there is a possibility that the policyholder might claim for a compensation amount which would be a much higher sum than the premium paid, in the event of a defined casualty, without doing anything in return.[298] Therefore, the premium is fashioned as being considered as *tabarru,* i.e. donation, gift or charity, that is provided by the policyholders to the *tabarru* fund.

[298] As mentioned earlier, see Chapter 2 above

The prospective insured is considered as a participant as opposed to the assured, given his charitable contribution going into the joint pot where the funds are being kept. It is relevant to mention at this stage that *gharar* is allowed as an exception in *tabarru* activities due to the charitable nature of *tabarru*. Otherwise, the *takaful* is threatened to be prejudiced, being eligible *halal,* as *gharar* would be considered to be present since funds are being invested by participants in a contract on which neither parties have specific knowledge about what the respective obligations would be in the future, as none of them can define the outcome at this stage. The idea of considering payment as *tabarru* is, in essence, not just a way to side step the various restrictions mentioned earlier, as are applicable to contracts in Islam, but also to raise an obligation on each one of the participants to assist his fellow participants in the case of the defined catastrophic losses under the concept of mutual cooperative loss sharing.[299] Therefore, when the payment is made as *tabarru*, the *takaful* operator is under no obligation to give the fund back to the participant, while the participant relinquishes their respective rights of return of the fund as it has been provided as a donation, as mentioned by other scholars.[300]

In *mudarabah* based *takaful,* when the funds are provided by the participants to the *takaful* organisation, the *takaful* operator acts in two capacities within the organisation. On the one hand, the *takaful* operator takes responsibility for the investment of these funds under *Sharia* rulings, to run the insurance business as the entrepreneur on behalf of the participants, so as to be compliant under the *mudarabah* arrangement. The aim is that, as under orthodox *mudarabah* agreement, the investor will be the participant and the entrepreneur will be the *takaful* operator, the latter investing the former's funds to increase the funds. On the other hand, the *takaful* operator takes responsibility for ensuring that the funds are handled appropriately for the management of the risks as they arise in the *takaful* business and have enough underwriting proceeds coming in, to balance the risks, which in essence is similar to how traditional insurance works. Nevertheless, in a *mudarabah*-based *takaful* model, the core idea is to have a *Sharia*

[299] Islamic Insurance, '*Mudarabah* snapshot' (2008 takaful-insurance-system.blogspot.co.uk) <http://takaful-insurance-system.blogspot.co.uk/2008/12/mudharabah-model-profit-sharing.html> accessed 28 February 2013

[300] Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, pp. – 71 - 72

compliant sustainable business insurance model, and profits are counted on investment returns and on the surplus made from underwriting from the joint *takaful* fund.[301] This is the principal working structure of a *takaful mudarabah* model and diagram 6.2 below explains the working flow further.

Now that the participants have provided the funds to the *takaful* operator, the latter now aims to increase these funds by generating revenues. These funds used are considered as an investment that would be used to create a return, if any. Therefore, as per the *mudarabah* principle, it will be shared between the *takaful* operator, being the entrepreneur and the participant, who is the investor of those funds. However, the idea of assisting the fellow participants in case of need, as may be the circumstance, is not abandoned. Therefore, the returns along with the principal funds find their way back to the joint *takaful* fund, which would be used to cover the insured peril needs as well.[302] The level of sharing of the investment between the parties, on the percentage basis, are fixed in advance, following the covering of operational disbursements such as paying off the claims made to the *takaful* provider. Subsequently, the *takaful* provider takes the prearranged percentage of the funds minus operational costs, as profits for their work in investment management. Before the funds go to the shareholders, they are subjected to an administrative disbursement of the *takaful* such as management expenses. In the event, the investment of the funds does not make a profit, which results in no additional monies being raised. As stated by Saiful Azhar Rosly, significant amounts of income of the *takaful* operation are, in fact, generated from the collection of these underwriting activities.[303]

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[301] Mohd Fadzli Yusof, 'Fundamentals of Takaful' (Kuala Lumpur: IBFIM, 2011), pp. 29 to 44 <http://www.islamicbanker.com/education/takaful-%E2%80%93-mudarabah-model> accessed 21 October 2014

[302] Mohammad Ayub, 'An Introduction to *Takaful* – An Alternative to insurance' (2009), Islamic Economics & Finance Pedia, page 2, <http://www.iefpedia.com/english/wp-content/uploads/2009/09/An-Introduction-to-Takaful-%E2%80%93-An-Alternative-to-Insurance-by-Muhammad-Ayub1.pdf> accessed 5 September 2013

[303] Saiful Azhar Rosly, *Critical issues on Islamic banking and financial markets* (1st edn, AuthorHouse 2005) p. - 496

Likewise, after payment of the *takaful* operational expenses, such as claims, the *takaful* operator takes his percentage from the surplus and the remainder percentage of the surplus is paid back to the participant, subjected to the respective participant's history of whether they made a claim. It should be noted that the investment made from each individual participant finds its way back to the participant under the *mudarabah* arrangement, even if the participant did not make a claim under the policy. Whenever claims are made under the policy, it is unlikely the participant would be entitled to his portion of the investment return. This, of course, does not affect the *takaful* operator's return on the policy.[304]

In the case of a deficit, i.e. circumstances where the expenses exceed the contributions and investment returns from the contributions,[305] the *takaful* provider has the sole responsibility of making a *quad hasan* loan; in other words, a gratuitous interest-free loan to cover the deficit. Over time, year on year, when a *quad hasan* loan has been utilised by the *takaful* operators, the books can be balanced by taking off the surpluses created in the *takaful* business, over the subsequent years. It is necessary to note that, even though the *takaful* operator takes on the responsibility of providing the *quad hasan* loan, the liability for the losses of the *takaful* operation remains with the participants. This remains the same until the *takaful* operator provides the *quad hasan* loan to discharge the participants' liabilities.[306] This is because it is the participants who are the investors in the business and the *takaful* operator is merely an entrepreneur, who had been requested by the investors to manage their funds. Therefore, any accountability and burden in the *takaful* business is a concern for the fund owners who are the principals.

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[304] Hania Masud, '*Takaful*: An innovative approach to insurance and Islamic finance' (2010-2011) 32 U. Pa. J. Int'l L. 1133, pp. – 1144, 1163

[305] This kind of circumstances could easily occur especially at the initial life span of the insurance or *takaful* company, where there are too many claims to pay out or the reinsurance or *retakaful* premiums are too high or even where the overheads of the business are too much for the year compared to the income raised by premiums received and investment income, as it is a start up business which would need to lift off and become a popular service provider.

[306] Insurance Finance Info, *'Takaful* models concisely' (islamicfinanceinfo.com.my) <http://www.islamicfinanceinfo.com.my/discover-takaful/takaful-models-mudharabah-wakalah> accessed 9 September 2013

This, no doubt, would be considered to be an unusual paradigm in the sight of prospective individual participants, who would be considering insurance to cover themselves against uncertainties. As far as the participants are concerned, the idea of taking a cover under *takaful* is to relieve them from such uncertain liabilities in a *halal* fashion. As per the *mudarabah*-based *takaful* model, it would appear that the participants would be in danger of accruing further liabilities than they initially considered themselves to be in originally. It would appear that, not only would individual participants be liable for risks concerning their own losses, but also for the losses of other participants, since *takaful* has been designed as a cooperative mechanism. Prospective participants would simply, have no clue as to the amount of liabilities they are signing up to, as they would have no knowledge of the same, when they initially signed up for the *takaful* policy. Undoubtedly, this would be viewed as a negative aspect when considering *mudarabah*-based *takaful* as an alternative to insurance.[307] However, the principle behind this, as discussed above, is that the participants had entered a contract with a *takaful* operator to manage their funds and make returns. The aim is to use those funds and returns to cover the various liabilities on behalf of participants, but not to stand in place of the participants. The whole liability at all times remains with the participants and such liabilities cannot be delegated.

However, as mentioned earlier, in the *takaful mudarabah* model, the *takaful* operator steps in to save the situation by paying a *quad hasan* loan to cover the shortfall, which alleviates the participants from further liabilities for that trading year. The analogy behind providing the *quad hasan* loan is not just to protect the interest and to have sustainable businesses, which are requirements mostly set by respective regulatory bodies, but perhaps also so that the *takaful* operator will keep the participants interested in getting repeat business for next year. As a final note, to avoid confusion during perusal, there are some perplexities among the various texts and articles about the working structure of a

[307] In fact, the researcher strongly opines that this would be final nail in the coffin and can be viewed as the straw that breaks the camel's back. It is simply impracticable to expect any insured to wilfully take on an insurance policy where at the end it could be very well possible that they would be liable for losses of which neither they knew of or could afford to handle or pay. This simply defeats the whole objective of taking insurance and puts the analogical set of cooperative structure of *takaful* as an extremely questionable proposition.

mudarabah-based *takaful* model, which is mainly because the *takaful mudarabah* model is being applied slightly differently from the normal general *takaful* activities as opposed to family *takaful* activities, as warned above. However, with family *mudarabah*-based *takaful*, one of the major differences is that the participants' funds on receipt by the *takaful* operator are split, which does not take place with a general *takaful mudarabah* model.[308]

Diagram 6.2 shows the General *Mudarabah* based *Takaful* model. For analysis of this diagram, the following variables are used, keeping in line with the examples given in this thesis: £x = Premium/Contribution/*Tabarru* paid by the participant to the *takaful* operator. The diagram shows the working principal of the *mudarabah*-based *takaful* model that is being used by *takaful* operators. As can be seen, the fundamental concept of the model is to invest the funds of the participants in order to have a return on investment, thus to increase the funds as much as possible. The diagram below speaks for itself, as following the investment of the funds, the return is set back to the originating account only for it to cover different purposes of the *takaful* operation.

Conversely, the *takaful* risk pool is a common account for all participants, which has been designed to cover the liabilities arising out of the risk coverage for all fellow participants under the principal of mutuality and solidarity. Mohammad Ayub gives a very interesting terminology on his article, about viewing the *takaful* contract as both protection and saving of investment aspects. One part of the *takaful* contract is being geared so that the participants are protected from the insured perils, while part of each of the participants' contributions are used in that perspective. The remainder of each of the participants' contributions are, as mentioned above, put onto the open market to get a *halal* return, which is shared between the participant and the *takaful* provider.[309] The funds from the *takaful* risk pool are used for settlement of the operational expenses such as claims settlement, *re-takaful* and such others.

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[308] Hasan Z, 'Islamic Law of Banking and Takaful' (2008) pp. - 4 – 8 <http://zulkiflihasan.files.wordpress.com/2008/06/takaful-model1.pdf> accessed 4 November 2013

[309] Mohammad Ayub, supra at p. 2, <http://www.iefpedia.com/english/wp-content/uploads/2009/09/An-Introduction-to-Takaful-%E2%80%93-An-Alternative-to-Insurance-by-Muhammad-Ayub1.pdf> accessed 5 September 2013

3.4. Problems with *Mudarabah* based *Takaful* model:

The *mudarabah* based *takaful* model is an intriguing invention; however, it lacks an underlying basis, as the various concepts appear to conflict with each other. A number of authors have already pointed the gaps in the paradigm, which this thesis will discuss.

Firstly, some authors view that *mudarabah* is a concept that should have best stayed within the banking parameters and not in the insurance field. In the *mudarabah* model, the various costs and liabilities associated are drawn from different parts of income such as the participants' contributions, and investment returns deal with the payment of primary liabilities i.e. claims. Additional liabilities such as *retakaful* expenses and claims handling expenditures are managed from the general *takaful* fund. Beside these, any associated expenditures such as management and marketing costs come out of the shareholders' funds, which in a sense affects the profits for the *takaful* organisation.[310] However, in practice, some *takaful* organisations cover the management costs from the *takaful* fund instead of the shareholders' funds, as such safeguarding the profits, which in a strict sense does not comply with the rules of *mudarabah*. In other instances, some *takaful* operators even reward themselves if the underwriting targets are met from the contribution funds. Again, this is not how a *mudarabah* based *takaful* is supposed to work, as the contribution funds are to be used for the payment of liabilities and later distilled through the process to be considered for calculation of profits and rewards for the *takaful* operator.[311]

Beside the point mentioned above, scholars have noticed a number of specific problems with the *mudarabah* based *takaful* contract itself. These problems are discussed below.

Secondly, a significant number of *Sharia* scholars agree that the income mechanism of the *mudarabah* based *takaful* model has a considerable black hole in its centre. When the

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[310] Muhammad Ayub, *Understanding Islamic finance* (1st edn, John Wiley & Sons 2007), p. - 426
[311] Ibid

participants are invited to make their respective payments to the *takaful* fund, these are made in the form of contributions in light of *tabarru,* i.e. charity, so that the restriction of *gharar* can be side-stepped. However, as soon as the contributions are made, the funds are processed in the form of a *mudarabah* contract between the *takaful* operator and the participants. This raises the inevitable query: how is it that monies that enter into the system with a moral ideology of being *tabarru*, almost instantly turn into a financial mechanism of *mudarabah*? The definition of a charity is one of assisting fellow people and expecting no return, whereas the whole idea of *mudarabah* is that the funds are invested to generate profits and that will be shared between the investor and the entrepreneur.[312] The funds simply cannot fluctuate both ways as willed and clearly this significantly undermines the whole of the working model of a *mudarabah* based *takaful* model, as donations cannot become an investment capital in this respect.[313] Along the same lines, other scholars argue that the *tabarru* concept lacks the foundation and enforcement basis included under *Sharia* law, and compensating participants in return for charity provided in essence have damaged Islamic ground from an insurance perspective.[314]

Thirdly, another aspect that is considered to be a problem for a *mudarabah* based *takaful* model is the risk taking by the *takaful* business. *Takaful* operators, as such the shareholders, take the profits generated from the Underwriting sales of the policies, which are basically similar to what one may witness in traditional insurance. This is not really how it was supposed to be, as the *takaful* operators' aim should be operation of the *takaful* fund effectively, not risk-taking and gaining profits.[315] *Mudarabah* based *takaful* is set as a cooperative device by which various participants comes together and cover each other from the joint pot, where their monies are put. It is asserted that the *takaful* operators' work is nothing other than being a referee to make sure that the device is handled properly and accurately. On the process of providing the service, it is reasonable

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[312] Ibid
[313] Abdul Rahim Abdul Wahab, 'Takaful Business Models - Wakalah based on WAQF: Shariah and Actuarial concerns and Proposed Solutions' <http://www.baj.com.sa/takaful/Presentations/PanelFour/Takaful%20Models%20Based%20on%20Waqf%20by%20A.%20Rahim%20Abdul%20Wahab.doc> accessed on 13 January 2014
[314] Oliver Agha, supra at p. - 72
[315] Ibid

for the *takaful* operator to be remunerated for the labour. However, that does not appear to be the case with *mudarabah* based *takaful,* where the *takaful* operator's objective is to make yields, as mentioned by Oliver Agha.

Fourthly, unlike traditional insurers, who take risks with Underwriting losses, *mudarabah* based *takaful* operators do not in essence take such responsibilities, ~~possibilities~~ as the losses of Underwriting remain with the participants. The *takaful* operator's role in such a case appears to provide a *quad hasan,* i.e. gratuitous loan, for which there are no strict obligations.[316] To top this, *mudarabah* contracts are not designed to have the *mudarib,* i.e. entrepreneur, to stand as guarantor when the *mudarabah* business heads rock bottom. Getting a surety involved in *mudarabah* based *takaful* is simply introducing unauthorised concepts in a set *Sharia* instrument.[317] Unfortunately, the attitude of the *takaful* operator providing a *quad hasan* from the common perspective is simply viewed as nothing short of taking the place as a guarantor.

It is viewed that one may, of course, argue that the *takaful* operator providing *quad hasan* is taking a risk, but it is actually a double-edged argument. On one hand, providing a *quad hasan* loan itself brings to mind the analogy that the *takaful* organisation, i.e. the shareholders, is taking risks, which is not what it is supposed to be, as the shareholders are there to manage and the risk-taking should be done by the participants, who came together in the first place to cover the unforeseen risks. On the other hand, if one argues that *quad hasan* is a discretionary loan, which is not mandatory for the *takaful* operator to pay, this creates new challenges of the predatory risks that participants would have to face, in such absence, leading to a poor business model and one that is extremely unlikely to be approved by any regulatory body in the world because of the substantial consumer risk that it creates and on the sustainability of the business. Therefore, as much as it may appear discretionary, the payment of *quad hasan* can be seen as an obligatory condition on the part of the *takaful* policies. In light of the above argument, it may be considered as non-Islamic.

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[316] Ibid
[317] Abdul Rahim Abdul Wahab, supra at p. 5

Fifthly, another drawback that has been detected is that the premiums or contributions that are being paid by the participants, as mentioned above, go through the *mudarabah* cycle, of participants being the investor and the *takaful* operator being the entrepreneur. When there is a profit of that collected contribution that is invested as capital, then all is well as far as the sharing of funds under the *mudarabah* principle is concerned; but if and when there is a loss, the capital takes the hit. As Mohammad Ayub pointed out, with general *takaful* the contributions are never paid back to the participants.[318] It is important to note at this stage that the underwriting business and investment business are two separate aspects of *takaful* operations, which act as two sides of the same coin. One may argue that, given that these are two separate operations, it is possible that the contribution investment business may be shrewder than the underwriting business of *takaful* and, as such, the capital should not take a hit. However, it may be possible that *takaful* operators are so oriented towards making trade from an Underwriting business that the investment aspect suffers, leading to a hit on the capital. In any event, the participants will not benefit, which is not what *mudarabah* contracts are designed for, while the *mudarabah* based *takaful* model, in essence, is contrary to the initial outcome focus of what *mudarabah* was aimed to do.

A sixth point that is being raised by academics is the aspect of providing *quad hasan* in the event of a deficit. As it is a *mudarabah* contract, which is circling the *takaful*, it is crucial to note that *mudarabah* is a profit-sharing contract and not a contract of providing one another with *quad hasan,* i.e. gratuitous loan agreement. The whole idea of *mudarabah* is that the investor will invest and the entrepreneur would attempt to use the funds to make a profit and then share it. Instead, in the *mudarabah* based *takaful* model, the investor, i.e. the participants, is investing and the entrepreneur is running the show, but when there is a deficit, the entrepreneur is in essence becoming a guarantor to the investor. This goes against the whole fundamental pillar of the *mudarabah* as it really should be the investor who should bear the loss in the event of a deficit of his invested

[318] Oliver Agha, supra at p. - 72

funds.[319] Of course, the contrary has been argued above as well and it is likely that such practices of *quad hasan* are maintained to keep a live insurance business.

A seventh point is that, in an orthodox *mudarabah* contract, the profits are those which are the return from the investment of the primary capital, and it is from those returns that the *rubb al mal* and *mudarib* should share their percentages. However, the circumstances in a *mudarabah*-based *takaful* model are that the profits are considered after whatever surplus is left when the *takaful* operator had settled off the operational liabilities, such as claims and *retakaful*. The concepts of surplus are not the same as profits and the *mudarabah* concept is undermined once more in this regard.[320] It is opined that this demonstrates that the sharing of the funds is not being done equally or correctly in line with the *mudarabah* concept and damages the working ideology of *mudarabah* based *takaful* model.

Eighthly, this thesis would also point out a few independent reservations on the *mudarabah* based *takaful* model. The idea of *tabarru* is indeed a good idea to start with. However, in light of the above points and considering back to the principles of *tabarrru*, it is a donation, gift or charity given by someone to another with the aim of assisting only. That being so, *tabarru* really then can be used in the assistance of any kind of need of another, as it is something which has been provided and one cannot really define how the other may use a donation that has been made for the needy. However, in the *mudarabah* based *takaful* model, the *tabarru* covers the participants for specific circumstances; in other words, to cover certain insured perils. In a sense, the provider of the donation is restricting the utilisation of the donation for aspects of his choice rather than the needs of the receiver of the donation. This clearly goes against the whole ideology of making *tabarru* in the first place.

Similarly, as raised by academic Mohd Ma'sum Billah, Dr. Qaradawi (1989, p. 275) mentioned that, when potential participants are buying *takaful* to cover their risks, they

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[319] Ibid
[320] Abdul Rahim Abdul Wahab, supra at pp. - 4 – 5

are not aware that the premium is a donation, which is given for mutual help, and that "*...such a thought never occurs to them...*"[321] Similarly, Afzalur Rahman (1979, vol. 4, p. 224) argues strongly against the fact that it is simply incorrect to give a blanket explanation of all types to be considered as mutual insurance. This is because the mutualness itself is likely to be unknown to either or both parties, or being unaware of the financial dependence between the parties, or even being aware that such reliance exists in that insurer and insured relationship.[322] Abdul Rahim Abdul Wahab considers that mutuality has hardly any presence in the way a *mudarabah* based *takaful* model functions. This is because *takaful* shareholders appear to be "*risk takers*" like traditional insurance rather than "*risk managers*", as was initially intended, which is apparent in how the former consider the underwriting profits, monopolising to cover the deficits by showing off as *quad hasan*.[323]

Whilst there are certain reservations on the comment of traditional insurance being a "*risk taker*", which is discussed below, the gist of the argument is that the *takaful* operator, like general insurers, uses the funds from Underwriting to manage *takaful* operations. Whereas, such would not be the case if the model was purely based on cooperativeness, which would have resulted at least in an ideal world, with each participant covering each other mutually for the risk. On the point of "*risk taker*", it is not opined that even traditional insurers are "*risk takers*" rather than "*risk managers*". This is because, in any given insurance contract, the risk at all times remains that of the insured and does not pass on to the insurer simply due to the existence of an insurance contract. The insurer is there to deal and settle claims on the best possible terms, as the insurer is the one who becomes ultimately liable to reimburse under the insurance contract obligations. Even with subrogated claims, when the policy is initially incepted, the risk is with the insured as subrogation could have taken place until a defined peril took place. However, it is agreed that if the "*risk taker*" term is considered loosely by the author, then the unspoken idea can be understood of the comparison between cooperative insurance and traditional insurers, with the latter being considered as risk takers.

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[321] Mohd Ma'sum Billah, supra at p. – 409
[322] Ibid
[323] Abdul Rahim Abdul Wahab, supra at p. 5

Finally, revisiting the concept of the participants' responsibilities on the *takaful* operation, it is asserted that a major contractual issue exists at heart, which becomes evident when there is a deficit. When the participants obtain their policy under the *mudarabah* based *takaful* model, they are signing up to a policy that will cover them for insured perils. Under the concept of cooperativeness, each individual participant is also signing up to cover themselves against the risk of losses. The raising issue is that individual participants are simply unaware of the extent of the risk of losses of others that each of them are covering. Neither are each of the individual participants aware of how big the risk of the others is, nor how much value the risk of others amounts to, which they are opting to cover mutually. One may argue that the *takaful* operator is delegated with that duty, but the argument backfires as mentioned earlier, in that the *takaful* operator is primarily for the management of *takaful* fund. It is the responsibilities of each individual participant to know the extent of the risks that they are aiming to cover mutually.

To make matters worse, this lack of knowledge deprives the participants from assessing whether they really want to cover any certain risk of loss from a specific individual.[324] Therefore, it can only be interpreted that the participants denied their right of freedom of contract. Freedom of contract is considered to be one of the important keystones of Islamic contract law[325] and has been set beautifully in the Holy *Quran*, where God mentioned clearly that trading must be based on mutual consent, in *Surah An Nisa* (Chapter 4), Verse 29 that:

[324] This could very well be the case, where a particular individual participant have a history of making vexatious claims or even worse have issues with honesty about making claims (which really should not be a surprise in insurance sector) or even the fact that the risk of loss might be too great for the participants to handle or not confident about to take on as it might be disproportional in the circumstances, as it is the participants who ultimately is responsible under contract laws for any deficiencies.

[325] Youcef Maouchi, 'Freedom of contract in Islamic contract law: An economic analysis' CERGAM-CAE, Université Paul Cézanne Aix-Marseille III, Faculté d''économie appliqué, pp. – 7 – 9, 12 -13

- "*O you who have believed, do not consume one another's wealth unjustly but only [in lawful] business by mutual consent. And do not kill yourselves [or one another]. Indeed, Allah is to you ever Merciful.*"[326]

This affects the whole of the structure of the *mudarabah* based *takaful* model and its eligibility under Islamic law. In a similar context, it raises the aspect of lack of full and frank disclosure under insurance policy and attacks the concept of utmost good faith in insurance practice. The participants' lack of facts is an absence of total disclosure of material information in the insurance sector and undermines the *mudarabah* based *takaful* model even under jurisdictional law arguments. Given the various concerns regarding *mudarabah* based *takaful*, new entrants in this market aimed to use the *wakala* based model, as discussed below.

4. *Tijari* model:

Mohd Ma'sum Billah considered the *Tijari* model to be a relevant model for *takaful*, which is practised in Malaysia. Here, Mohd Ma'sum Billah makes a distinction between general *takaful* and family *takaful*. For the former, he refers to the plan of pure *mudarabah*, as mentioned above, where no deductions are made for the operational costs and the participants and *takaful* operator share the surplus. For the latter, however, he refers to the model of modified *mudarbah*. In essence, the *tijari* model mentioned by the author is actually a *mudarabah* model, which has a different title in Malaysia.[327]

5. *Ta'awuni:*

This is one of the initial types of *halal* models considered by Islamic scholars in 1979, which led them to determine that there was a need to create something with mutual benefit. *Ta'awuni* is defined as helping each other, which originates from the concept of cooperation, which itself includes working together, mutuality and joint effort. The

[326] Holy *Quran, 'Surah An Nisa'* Chapter 4 Verse 29 (quran.com) <http://*Quran*.com/4 accessed 1 February 2014
[327] Mohd Ma'sum Billah, supra at pp. – 413 - 414

concept of *ta'awuni* has been mentioned a number of times in the Holy *Quran* for avoidance of sin and enmity in society.[328] Hence, the introduction of *ta'awuni* or mutuality finds its roots in Saudi Arabia and Sudan. The aim of this instrument is to make donations, which are put in one pot, and clarifying the responsibilities of operator and contributor. Eventually, when the fund makes a profit, it is to be given among the participants.[329] Interweaved within *ta'awuni* are the aspects of *mudarabah* ideologies that allow for cooperative insurance to work on as discussed above.

The basic working principle of *ta'awuni* is simple with the basic idea that every participant shares everything equally, both surpluses and liabilities. Therefore, in the event of a defined casualty by any of the participants, he is entitled to make his claim from the joint pot and the others are in agreement to assist him. However, unlike other *mudarabah* models mentioned above, where the percentage distribution of the yield can be varied, in *ta'awuni* this tends to be fixed at sharing equally only. In the *ta'awuni* model, a percentage is kept aside to cover liabilities such as claims, *re-takaful* and such others, which are considered as *sadaqah,* whilst the remaining percentage is used to invest. Provided that the investment makes a return for the participants, who did not make a claim from the fund, they are given half of the yield. The *takaful* operator takes the remaining half to cover their administrative expenses, such as employees' salaries, following which, after deduction and subtracting *zakat* (compulsory annual charity of 2.5%), the balance is paid out to the shareholders of the *takaful* company.[330]

Upon perusal it would appear that the concepts of *ta'awuni* and *takaful* are similar and, to an extent, perhaps even interchangeable. However, as conveyed by scholar, Siddig Ahmad, the concept of *takaful* is based on the ideology of empathy rather than pure *ta'awuni,* which is based on the notion of sympathy.[331] The concept of empathy is set nicely in the hadith Book 32, Hadiths 6260 and 6261 of Sahih Muslim:

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[328] Siddig Ahmad, 'Generic skills from Qur'anic Perspective, International Journal of Islamic Thought' (2012) ISSN/EISSN: 22321314, Vol. 1, Universiti Kebangsaan Malaysia, 46
[329] Ibid., p. 408
[330] Ibid., pg. - 408 - 410
[331] Siddig Ahmad, supra at p. - 47

- *"Nu'man b. Bashir reported Allah's Messenger (may peace be upon him) as saying: The believers are like one person; if his head aches, the whole body aches with fever and sleeplessness."*[332]
- *"Nu'man b. Bashir reported that Muslims are like one body of a person; if the eye is sore, the whole body aches, and if the head aches, the whole body aches."*[333]

6. *Wakala*, the concept:

6.1. Introduction:

In a *wakala* model, the *takaful* operator acts as an agent rather than entering a partnership agreement, as mentioned in the above *mudarabah* model. *Wakala* is a principal and agent contract, where the principal is known as the *asil/muwakkil* and the agent is known as the *wakil.* Before explaining the *wakala* model, a narration on explaining *wakala* would assist. *Wakala* basically means entrustment of one's power of authority on a matter so as to act on another's behalf on that concern. In short, it means "*protection, delegation or authorisation*".[334]

The *wakala* model would cover a number of scenarios, where delegation of power takes place and could include such circumstances from buying and selling on one's behalf to acting as a representative of another in a matter. The whole aim is to get an additional party involved in the chain to be the link between the principal and the third party. This could be for any number of reasons including lack of expertise, distance or for any reason the principal feels he/she is unable to act individually in that transaction. The *wakil* duty is to do the best for the *asil* in the task provided using his skill. At the end, when the *wakil* completes his work, he would be remunerated for his work by commission from the *muwakkil*. In the event the contract does not mention payment, then references would be

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[332] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=032&translator=2&start=0&number=6260#6260> accessed 5 November 2013

[333] Ibid

[334] Muhammad Yusuf Saleem, *Islamic Commercial Law* (1st edn, John Wiley & Sons Singapore Pte. 2013) pp. - 68 - 69

made on the market rate for the same work conducted. The *wakil* being empowered with the agent's responsibility has the authority to make and engage deals on behalf of the principal, but at the same time can raise liabilities as well for the principal.

There are a number of requirements that have been set by the *Sharia* for a *wakala* contract to be in existence, which are as follows:[335]

i. The principal must have the legal capacity to enter into a *wakala* contract. It is asserted that, in the absence of the approved capacity, the principal is not able to pass the requisite authority to the *wakil* to represent him and make contracts on his behalf. Delegation of authority can only take place when the *muwakkil* had authority in the first place to pass on to the *wakil.*

ii. The *wakil* must have the necessary legal capacity to understand and enter into a *wakala* contract. Once more, it is opined that it is due to the fact that the agent would not have the necessary authority to make a *wakala* contract on behalf of the principal. Asking someone to represent the *muwakkil* who does not understand his/her responsibilities is simply fruitless.

iii. To avoid the elements of *gharar*, the parties must know each other and the *wakil* needs to be clear on what are the responsibilities.

iv. To keep matters *Sharia* compliant, the work that the agent is required to do needs to be *halal.*

v. The work that the *wakil* is being asked to do by the *muwakkil* must be legally allowed and it is a matter that can be delegated to be done on behalf by someone else.

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[335] Ibid

It is felt that a concise pictorial diagram would assist in understanding and remembering the working *wakala* arrangement for this thesis (see diagram 6.3). As can be quite easily relayed from the diagram below, the *wakil* is being instructed and assigned by the *asil* to assist in dealing with the third party. This is rather a similar situation as in the English law of Principal and Agency relationship, where the agent represents the principal.

6.2. Religious law:

The religious standing of *wakala* can be tracked from both the Holy *Quran* and the *hadith* of the Prophet Mohammed (pbuh). In the Holy *Quran*, Allah has allowed the delegation of work from one to another, as stated in *Surah Al Kahf* (Chapter 18), Verse 19 that:

- "*...so send one of you with this silver coin of yours to the city and let him look to which is the best of food and bring you provision from it and let him be cautious...*"[336]

This verse is related to the incident where one of the companions of the cave was asked to go to the city to purchase food on behalf of another, as the former would be in danger if he was seen in public. Similarly, in the Holy *Quran* in *Surah Yusuf* (Chapter 12), Verse 93 it is mentioned that:

- *"Take this, my shirt, and cast it over the face of my father; he will become seeing. And bring me your family, all together."*[337]

In this verse, Allah tells about the incident of Prophet Yusuf, who told his brothers to take his shirt on his behalf to his father, as he was separated from his father following an evil plot. As can be witnessed, the delegation of tasks is something that has been practised and allowed in context in the Holy *Quran*. A more explicit illustration of this can also be

[336] Holy *Quran,' Surah Al Kahf'* Chapter 18 Verse 19 (quran.com) <http://*Quran*.com/18> accessed 3 August 2013
[337] Holy *Quran, 'Surah Yusuf'* Chapter 12 Verse 93 (quran.com) <http://*Quran*.com/12> accessed 3 August 2013

derived from the practices of Prophet Mohammed (pbuh) as such from the *hadith*, which would show that Prophet Mohammed (pbuh) had utilised representatives during his lifetime for various purposes. According to Book 24, Hadith 3625 of Sunan Abudawud, it has been narrated by Jabir ibn Abdullah that:

- *"I intended to go (on expedition) to Khaybar. So I came to the Holy Prophet (peace_be_upon_him), greeted him and said: I am intending to go to Khaybar. He said: When you come to my agent, you should take from him fifteen wasqs (of dates)..."*[338]

Likewise, under a number of sections in the *sahih hadith* of Malik Muwatta, it has been written that the Prophet Mohammed (pbuh) had assigned tasks to others, as agents. One of the incidents mentioned in Malik Muwatta from Book 31, Hadiths 31.12.20 and 31.12.21 includes:

- Prophet Mohammed (pbuh) mentioned "*...'Dried dates for dried dates is like for like.' It was said to him, 'Your agent in Khaybar takes one sa for two.'...*". Prophet Mohammed (pbuh) asked his agent about this, who responded, "*...'Messenger of Allah! Why should they sell me good dates for assorted low quality dates, sa for sa!' The Messenger of Allah, may Allah bless him and grant him peace, said, 'Sell the assorted ones for dirhams, and then buy the good ones with those dirhams.'*"[339]

- Prophet Mohammed (pbuh) "*...appointed a man as an agent in Khaybar, and he brought him some excellent dates. The Messenger of Allah, may Allah bless him and grant him peace, said to him, 'Are all the dates of Khaybar like this?' He said, 'No. By Allah, Messenger of Allah! We take a sa of this kind for two sa or*

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[338] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=agent&translator=3&search=1&book=&start=0&records_display=10&search_word=all> accessed 3 August 2013

[339] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=31&translator=4&start=19&number=31.11.19> accessed 3 August 2013

two sa for three.' The Messenger of Allah, may Allah bless him and grant him peace, said, 'Do not do that. Sell the assorted ones for dirhams and then buy the good ones with the dirhams."'[340]

The above incidents refer to the situation of the Prophet Mohammed (pbuh) having an agent and delegation of some of his responsibilities in order to act on his behalf, which carried both benefits and burdens. However, interestingly, the above also reiterates the concept of *riba* on which a detailed analysis had been written in the previous chapter in light of the above *hadiths*.[341]

6.3. *Wakala* based *Takaful* model:

The *wakala* based *takaful* model has a similar working structure as the *mudarabah* based *takaful* model mentioned above, except that, in the *takaful wakala* model, the *takaful* operator acts as a *wakil,* i.e. an agent. As such, the participant is considered to the *muwakkil*. Similar to the above, it is opined that a straightforward formula would assist with the understanding of the *wakala* based *takaful* model, which is as follows:

Takaful Wakala = *Wakala* (contract) + *Tabarru* (fund/charity) + Cooperative loss sharing (principle)

The *takaful* operator takes a percentage of the contribution upfront, which is paid by the respective participants as a *wakala* fee. In addition to this, the participants agree to pay *takaful* operations-related direct expenses.[342] This generally involves *takaful* functioning disbursements such as claims, reserves, *retakaful* and such others. The fee is justified in payment under a *wakala* contract as it is considered that the *takaful* operator is providing a management service of the *takaful* operation on behalf of the participants. This percentage amount is fixed at the beginning of the trading year for policies to be

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[340] Ibid

[341] See Chapter 2 to correlate the above incident of agent with *riba*

[342] Dr. Zulkifli Hasan, supra at pp. - 10 – 12 <http://zulkiflihasan.files.wordpress.com/2008/06/takaful-model1.pdf> accessed on 4 November 2013

considered in line with the *Sharia* advisory board of the *takaful* organisation. The idea is to cover the management-related expenses, such as salaries, of the *takaful* operation from the agency fee that is charged.[343]

The remainder of the contribution paid by the participant is used for investment, just as it would have occurred with an orthodox *wakala* contract, following deduction of the *wakil*'s fee. However, in the *wakala takaful* model, as the *takaful* operator has already charged a percentage of the contribution at the beginning as part of the agency work, funds that are generated from underwriting sales and investment of those funds now belong to the participants. As such, these extra funds can now be utilised in covering of necessary *takaful* operational liabilities such as claims, *retakaful* and such others. The joint pot, in essence, belongs to the participants and the *takaful* operator is simply working on fixed fee on this matter, which has already been settled at the start.[344] In practice, to encourage further development of the *takaful* business, portions of the Underwriting sales are taken by the *takaful* operator on meeting set targets but any Underwriting losses stays with the participants. As mentioned earlier, the *takaful* operator's administrative expenses at all times are covered by the *wakala* fees alone that are charged from the participants. Due to this aspect, the *wakala* based *takaful* model at times is viewed as a clearer model than the *mudarabah* based *takaful* model. A *wakala* based *takaful* type model is practised in the Sudan, United Arab Emirates and the United Kingdom.[345]

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[343] Mher Mushtaq Hussain and Ahmad Tisman Pasha, 'Conceptual and Operational differences between general Takaful and conventional insurance' (2011) Vol. 1 No. 8 [23-28] Australian Journal of Business and Management Research, p. - 24

[344] The researcher feels that he can draw something from his own experience in the legal practice in England and Wales of working on various methods of funding, which can be made an analogous connection to *wakala* contract, where the researcher had acted as the *wakil* i.e. agent, on behalf of clients, as their lawyer. At times, the researcher has undertaken different types of cases on fixed fee basis for the convenience of both parties. In those cases, irrespective of how much effort the case required, the amount of fee was fixed in advance and so caused no prejudice to the clients that case went disputed for longer then initially expected or opposition raises issues which was not initially predicted. Such fixed fee arrangements, can be an effective way of commercial relationship but the *wakil* has to be cautious in underestimating the efforts or conversely, overestimating the effort, either of which will affect the relationship between the parties. In fact, it is considered to be one of the flaws of *wakala* based *takaful* model and is discussed in the part of Problems with *Wakala* model below.

[345] Haemala Thanasegaran, 'Making an entrance – Can Australia contribute to *takaful* (Islamic insurance) law reform?' (2013) 24 Insurance Law Journal, p. – 109. Although the author mentions UK in the article but at present there are no *halal* insurance companies in UK. The only *takaful* company in UK was *Salaam*

In any event, like the *mudarabah* based *takaful* model above, in case any deficits take place in the *wakala* based *takaful* model, the *takaful* operator faces a rather obligatory situation to bail out the organisation from red. The *takaful* operator does this by following a similar route as the *mudarabah* based *takaful* model, by providing a *quad hasan,* i.e. a gratuitous loan, which they can claim back over the following years providing the *takaful* business to go on to make profits. Just like a *mudarabah* contract, the liabilities for the losses remain with the participants until the *quad hasan* loan is provided to eradicate the participants' liabilities.[346] As one may recognise, there are a number of concerns with this model and, as such, *Sharia* scholars have reservations about this model, as discussed below.[347]

Diagram 6.4 shows a general *wakala* based *takaful* model. For analysis of this diagram, the following variables are used, keeping in line with the examples given in this thesis: £x = Premium/Contribution/ *tabarru* paid by the participant to the *takaful* operator.

6.4. Problems with the *Wakala* based *takaful* model:

Just like *mudarabah* based *takaful* model, the *wakala* based *takaful* model is also an intriguing attempt of circumventing against the *Sharia* restrictions set on traditional insurance. However, as with the *mudarabah* based *takaful* model, the *wakala* based *takaful* model also has a number of problems that hinder its advancement from being a mainstream working model for *takaful*.

Firstly, like the *mudarabah* based *takaful* model above, the *takaful* operators with the *wakala* model give an incentive to the shareholders by giving a portion of the

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Halal insurance which started trading in 2008 but closed in 2009 as they were unable to raise enough capital: <http://www.insurancedaily.co.uk/2010/04/28/second-wind-for-sharia-compliant-salaam-halal/>; accessed on 30 January 2014

[346] Insurance Finance Info, '*Takaful* models concisely' (islamicfinanceinfo.com.my) <http://www.islamicfinanceinfo.com.my/discover-takaful/takaful-models-mudharabah-wakalah> accessed on 2 September 2013

[347] Muhammad Ayub, supra at p. - 424

Underwriting sales when targets are met.[348] The issue starts with the fact that, beside the agency fee, which the *takaful* operator charges under the *wakala* model as operational costs, any surplus funds belong to the participants and the common pool. The agency fee is fixed as per the *wakala* agreement agreed in advance and additional funds are not part of that package. Authors such as Abdul Rahim Abdul Wahab state that this is contrary to mutual assistance principles and, as a trustee in a *wakala* contract, the *takaful* operator is under an obligation for a fair and better fund management. This would boost the underwriting sales and would assist the *takaful* operator by increasing the spread of risks. The *Sharia* scholars have considered that such incentive rewarding is not Islamic in nature.[349]

Secondly, author Abdul Rahim Abdul Wahab goes further to state that, in certain *takaful* organisations, the *takaful* operator takes the *wakala* fee as a fixed percentage from the *takaful* fund rather than initially taking from the contributions. Further, he argues that this upsets the risk-sharing balance between the participants, as various contributors would have different risks to consider, which is generally the case with larger bulk contributors. This, in essence affects the *takaful* fund on withstanding severity of claims risks.[350]

It is felt there is more to this point. One view is that the *takaful* operator should not be allowed to take a portion of Underwriting sales as incentive, as there is no prior agreement between the participants and the *takaful* operator, which makes this payment inaccurate. Another view is that, even if the *takaful* operator did establish an agreement to make extra funds on hitting the Underwriting sales target, it would be unlawful under Islamic rules as it would most likely invite the ingredients of *gharar* and *maisir*, as the parties' relationship is now involved in an uncertainty environment, where participants do not know the *takaful* operator's fee and the parties are unclear on the obligations and responsibilities. Therefore, such incentive payments are unlikely to be *Sharia* compliant.

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[348] Muhammad Ayub supra at p. - 426
[349] Abdul Rahim Abdul Wahab, supra at pp. 6 – 7
[350] Ibid

Thirdly, there are a number of other problems that have been identified by scholars about the utilisation of the *wakala* based *takaful* model. It is stated that the contributors' funds, although clothed as donation, remain the participants' property since the *takaful* operator is the agent who is using the primary funds of the principal, i.e. the participants interact with third parties and make returns on the fund. As such, the *tabarru* is viewed as a conditional gift rather than a basic donation unlike in a *mudarabah* based *takaful*. This questions the effects of what having a conditional gift will have on inheritance and *zakat* in the event of death of any one of the participants, as the conditional gift should find its way back to the donor, i.e. the participants. It also questions the relationship between the participant & *takaful* operator & amongst the participants themselves, due to the concern that a conditional gift contract damages the workability of the *wakala* based *takaful* to be a compensatory contract.[351]

This is because the monies become gifts with stipulations that need to be complied with, otherwise they should be returned; but under the *wakala takaful* model, it really should be a principal and agent relationship. It is opined that the nature of the conditional gift and the nature of *tabarru,* as sugar-coated in a *wakala takaful* model, are very different and it is not possible for the funds that enter the *takaful* system as one kind, to change to a different kind immediately without any valid fermentation process.

Fourthly, regarding the payment of *quad hasan,* which the *takaful* operator has to provide to cover up the deficit for a given trading year, the *takaful* operator is allowed to recoup the generous loan provided for the subsequent years; this, however, affects the future participants, since not all of them are the same participants as in the year that the *quad hasan* was provided. On a similar note, the *takaful* operator has the opportunity to increase the level of reserves for the subsequent years on the surplus generated each year, but as a new start-up venture this process would need substantial efforts in the preliminary years. However, this has a negative impact as well, as keeping higher reserves in the early years of the business as opposed to later years will not allow the distribution of the participants' division accurately, since it is argued that the *takaful* is a

[351] Abdul Rahim Abdul Wahab, supra at pp. 8 – 9

cooperative approach involving all the participants helping each other mutually and not at the cost of another. Likewise, due to the nature of *quad hasan*, a *takaful* operator in *wakala* based *takaful* would appear to have the status of a guarantor for the participants due to his keenness to assist whenever there is a deficit, but this is not the intention of *wakala* at all. This adversely affects the working principle of the *wakala* based *takaful* model.[352]

Fifthly, another issue considered by a number of academics, including Mervyn K. Lewis and Mohammad Ayub, is the charging of a fixed fee in the *wakala* based *takaful* model. The unique part of this model is that there is certainty of the *wakil*'s fee and follows the *wakala* contractual obligations, but setting a fixed *wakala* fee in advance for all participants, irrespective of sizes, is not the best commercial move. In today's world, customers obtain bulk prices but without the same flexibility; there is also a risk that the *takaful* operation will have limited funds to compromise against the risk of claims.[353] Conversely, differing premiums will upset the model, otherwise the *wakala* based *takaful* model would no longer be truly cooperative, as the playing field is no longer level. Nevertheless, Mohammad Ayub points out that the contribution element should be connected to risks undertaken and, for a large volume of customers, instead of amending the contribution amount, the *wakala* fee could be reduced.[354] This could result in certainty being compromised for the sake of commerce, but perhaps this would be a reduced price for the sake of advancement of *takaful*.

Finally, one of the points mentioned by Mervyn K. Lewis is about the reserves in the *wakala* based *takaful* model that are built up at the end of every year from the surpluses as a future contingency plan. However, this does not sit appropriately as participants will undoubtedly change every year, along with the contribution amount each year, and it appears to be similar to transferring funds in present day participants for future day

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[352] Ibid. For the concept of guarantee, there is the Islamic ideology of *kafala* exists separately which have no bearings with *wakala* or *mudarabah*. However, the way, the respective *takaful* models are structured they portrays an inaccurate reflection which is incorrect.

[353] Mervyn K. Lewis, 'The Evolution of *Takaful* products' in the textbook: Kabir Hassan and Michael Mahlknecht, *Islamic Capital Markets: Products and Strategies* (Wiley Finance 2011) pp. – 191 - 192

[354] Muhammad Ayub, supra at p. - 426

participants. The author states that, for each deficit, each generation needs to cover the shortages on a pro-rata basis.[355] However, it is admitted that this is another issue with the *wakala* based *takaful* model, but it is unlikely that the author's recommendation can work as it is becoming customary for the *takaful* operator to pay the *quad hasan* to cover the deficit. Moreover, it would neither be practical nor economically viable to ask the participants, who have already paid their contributions, to ask for additional funds for the survival of the *takaful* operator's business. As insurance business works, generally it is not a concern for the insured on how how the insurance business is managed by the insurer and on his solvency grades. Except the fact that the insured would simply be worried if the insurer would remain solvent enough to meet his/her claims, should a defined casualty take place and a claim needs to be made.

7. Hybrid variation *Wakalah* and *Mudarabah* based *Takaful* model:

7.1. The Concept:

A number of academics, including Mohammad Ayub, pointed to an introduction of a hybrid *wakala* and *mudarabah* based *takaful* model for the advancement of *takaful*. The aim of such a hybrid model appears to be for maximising the shareholders' fund of a *takaful* organisation. As both *wakala* and *mudarabah* are profit-making instruments, therefore the hybrid model created is also a profit-making instrument. This is achieved by the sharing of both the sales generated from Underwriting and from investment profits between the *takaful* operator and the participants.[356]

Such a model appears to have been used in Bahrain and Malaysia, where the *wakala* method is used for the underwriting aspects of the *takaful* and *mudarabah* method is used for the investment of funds of the *takaful*.[357] In the hybrid of the *wakala* and *mudarabah* model, the asset management may be considered separately, then the *takaful* organisation dealing with the underwriting. The plan is to make up for more transparency in the

[355] Mervyn K. Lewis, supra at p. - 192
[356] Muhammad Ayub, supra at p. - 424
[357] Haemala Thanasegaran, supra at p. – 109

system; as such, the model appears to be favoured by the Central Bank of Bahrain.[358] In keeping with the trend of this thesis, it is of interest to put forward a formula for such a hybrid *wakala* and *mudarabah* structure as follows:

Hybrid *Wakala* and *Mudarabah* = *Wakala* (fixed fee contract) + *Mudarabah* (return sharing contract) + *Tabarru* (fund/charity) + Cooperative loss sharing (principle)

The practical operational aspect of a hybrid *wakala* and *mudarabah* model is similar to what has been discussed above, except that, in this hybrid model, it is a new variation following a merger of the *wakala* model and *mudarabah* model. The whole process starts, similar to the other models, with the participant providing his/her contribution to the *takaful* operator. In this hybrid model, when the *takaful* operator receives the contribution, a percentage deduction takes place straight away from the participant's contribution as a *wakala* fee. This is justified by the *takaful* operator arguing that he/she is acting as a *wakil,* i.e. agent, for the participant in managing the participants' monies in respect of underwriting, administration, claims management and other *takaful* operations, under a *wakala* contract. The remainder of the contribution now goes to the joint *takaful* fund for further distillation.

The portion of the funds that make its way to the *takaful* joint pot is then invested by the *takaful* operator with the aim of making more money as an effective business development.[359] At this stage, the parties are considered to have entered a *mudarabah* contract with the *takaful* operator to take on the appointment as the *mudarib,* i.e. entrepreneur, for the investment and management of the funds in the joint pot in a *Sharia*

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[358] Zamir Iqbal and Abbas Mirakhor, *An Introduction to Islamic Finance: Theory and Practice* (2nd edn, John Wiley & Sons Asia Pte. 2011) pp. - 220 – 221

[359] The researcher finds this rather astonishing that whilst some Muslims argue that they do not want to consider traditional insurance because of traditional insurance primarily profit making etiquette (as mentioned above in chapter 4 (Similarities and Differences), as considered by author, Dr. Thanasegaran [Haemala Thanasegaran, supra at pp. – 104 - 109]) however, *takaful* organisations are following the same ideology with expansion in every available aspect to increase the funds and make profits. Therefore it would not be correct if traditional insurance are being discarded for the sole reason that traditional insurance are shroud business minded in making additional monies. Of course, the restrictions of *riba*, *gharar* and *maisir* (as discussed in previous chapters) still are valid grounds for rejection of traditional insurance but making aggressive profits on its own cannot be a sole reason for denial of the same.

compliant manner. Since the funds came from the participants, they are considered as the *rubb al mal,* i.e. investor of the respective funds. As the parties have entered a *mudarabah* contract, depending on the return (if any, as may be the case), the amount is shared between the participant and the *takaful* operator on percentages agreed in advance, under the *mudarabah* principles.

The returns that are made from the investment find their way back to the *takaful* joint pot and are combined with the principal amount. This remainder of the funds remains in the joint risk pot and continues to accumulate, which is counted as monies coming in from the Underwriting activities. As may be the case, if it appears that the funds in the joint risk pot are at surplus after the payment of *takaful* operational expenses such as claims, reserve, management, *retakaful* and such others, then the funds from this pot are shared between the participants and the *takaful* operator. This is in keeping in line with the *takaful* contract of mutual sharing so as to avoid unjust enrichment, *gharar* and *maisir* arguments as the participants are supporting each other by cooperativeness; as such, where the total amount in the pot remains in the black, there is no reason for withholding the return of the excess funds back to the respective participants. Also, this is in consideration of the fact that respective participants do not make a claim and the returns are made to those who did not make a claim, as under the similar ideology of a no claim bonus, as can be witnessed in Western traditional insurance. In a number of *takaful* organisations, the *takaful* operator takes a percentage of the surplus funds that remain in the risk pot, as an award of performance incentive.[360]

If in the event of a deficit, then strictly speaking the liability is for the participants to consider, as the participants are the ones who aim to work cooperatively and they bear the burden of losses. However, as with other models, the *takaful* operator relieves the liabilities by providing a *quad hasan,* i.e. gratuitous loan. Under strict contract law principles, the *takaful* operator is under no obligation to make this gratuitous loan to relieve the liabilities, but still does so, perhaps as a regulatory requirement or, more

[360] Oliver Agha, supra, pp. – 82 - 83

likely, to retain the customers for the forthcoming year.[361] A diagram on the structure of the hybrid *wakala* and *mudarabah* model is shown below (Fig……). In the case of a hybrid family *wakala* and *mudarabah* model, the analysis is very similar to that of the above, save that when the contributions are paid, it is split into two with one portion going to the participant's Special Account and another going to the participant's account. It is the fund in the participant's Special Account that goes through the same distillation process as mentioned in the general hybrid *wakala* and *mudarabah* model.[362]

An illustration has been enclosed in diagram 6.5 showing a hybrid *wakala* and *mudarabah* based *takaful* model. For analysis of this diagram, the following variables are used, keeping in line with the examples given in this thesis: £x = Premium/Contribution/ *Tabarru* paid by the participant to the *takaful* operator

7.2. Problems with the Hybrid of *Wakala* and *Mudarabah* based *Takaful* model:

It may appear to be a noble idea to have a hybrid of *wakala* and *mudarabah* to perhaps eliminate the flaws that exist in each of the instruments in the individual model singularly, while maximising the revenue of the *takaful* operator and shareholders at the same time by the merger. However, it has been noticed that such a hybrid model has fundamental problems with the arrangement, which affects the operational aspects of the model. The various defects with the hybrid model are discussed below.

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[361] As the researcher opines that the *takaful* operator simply does not have to make this *quad hasan* loan to save the participants. At the end of the day, it is in essence a problem for the participants to handle, as it is a liability for them to consider given that under the structure, it is the participants who opted to help each other mutually. As with any ventures, there is always a risk of success or failure, so when there is a deficit, then it is a failure, which is void that they should resolve. Now, from the business prospective it makes sense why the *takaful* operator would no doubt consider clearing up the liabilities otherwise he runs a risk of going out of business as participants would very unlikely favour a model of insurance where they become held personally liable for other risks. Irrespective of what one may argue, the researcher opines it is highly unlikely that any participant would gladly agree to take responsibility for risks of others despite how much cooperativeness they may have intended initially.

[362] Shafiel A.Karim, *The Islamic moral economy: A study of Islamic money and financial instruments* (BrownWalker 2010) pp. – 81- 84

Firstly, as with other models of *takaful* where the *takaful* operator provides *quad hasan,* i.e. gratuitous loan, to save the situation in the event of deficit of funds in the joint pot to meet with liabilities, there are doubts as to whether this practice itself is in fact *Sharia* compliant. The academic Oliver Agha voiced his concern in this respect about the *Sharia* legality of making a *quad hasan* loan as a condition subsequent to a *mudarabah* contract.[363] It is opined that this is because it cannot be part of any contract that the *takaful* operator must give a *quad hasan* loan when there is a deficit, as *quad hasan* loan is, by its nature, a gratuitous loan, which is not calling for anything in return except return of the principal sum, and even that is subjected to the debtor's financial condition. It simply does not make any logical sense to convince anyone to provide a gratuitous loan. The whole concept of cooperativeness is, no doubt, a plausible idea, but the way the hybrid *wakala* and *mudarabah* model is structured makes the participants individually responsible for the liabilities, in case of deficit in the fund for the *takaful* operation.[364]

It is felt strongly that it is rather strange that various scholarly papers do not seem to have considered this vital point of participants' personal liabilities in situations of deficit. It is maintained that it is likely because of the *takaful* operator's constant readiness to provide a *quad hasan* loan in such cases. However, it is necessary to note that the *takaful* operator's readiness is not setting matters as a strict requirement and, as such, exposing the insureds/participants to significant additional liabilities, much more than they had when they got involved in the *takaful* operation. This aspect of a *quad hasan* loan raises issues of being the flip side of the same coin.

On the one hand, the *takaful* operator providing of *quad hasan* loan is not a requirement that can be strictly set under *Sharia* perspective, as discussed above, because of the nature of the credit. It may be argued that the requirement of the *quad hasan* loan in cases of deficit can be a regulatory requirement, or even a statutory requirement in various

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[363] Oliver Agha supra p. – 82

[364] This major problem of participants being responsible for the liabilities is existent in various other models of *takaful* as well. The ones that are discussed above i.e. the *mudarabah* and the *wakala* model, it is already seen that the participants remains liable. The various other models those are existent at the moment leaves this same problem and *takaful* operator chipping in with *quad hasan* loan is not something, which is in strict sense *Sharia* compliant as mentioned in the main text above.

jurisdictions, and so should suffice in the safeguarding of insureds/participants. Therefore, on the other hand, this raises the argument that, if one is to depend on other resources besides *Sharia* law to support a vehicle, which was introduced to comply with Islamic law, then this defeats and significantly undermines the very necessity and purpose of construction of such difficult mechanics of an alternative to insurance, when the alternative itself does not have its own ground to stand on, in some parts at least.

Secondly, although not a major point, it is still an issue with the *takaful* operator taking a percentage of the funds from the risk pool in the event of surplus as performance initiative. This has been an issue with the other *takaful* models as well, as mentioned above and, reconsidering the same arguments, it appears that the *takaful* operators do not have any contract to reward themselves from the surplus of the risk pool. In the hybrid *wakala* and *mudarabah* model, the *takaful* operator has a *wakala* contract, for which he had already taken his fee at the start from the contribution. The *takaful* operator also has a *mudarabah* contract and takes his percentage as *mudarib* from the returns generated from the investment pot. Therefore, any extra fund allocation from the risk pot to the *takaful* operator is outside the remits of any agreed contracts. It is believed that this makes the hybrid *wakala* and *mudarabah* model to an extent to non-*Sharia* compliant operation due to the *takaful* operator's over-enthusiastic attitude of increasing the shareholders funds as much as possible.

Thirdly, another major issue with the *takaful* operational paradigm is that of masking the contribution payment as *tabarru*, which has been highlighted above for other models. With the risk of repeating, the concept of *tabarru* is clearly supposed to be a charity payment, where the donor, i.e. the participant, makes the payment to the donee, i.e. the *takaful* operator, with the former having no intention of seeing the fund back and, as such, does not hold any expectations of any profits or losses on that payment. It has been mentioned that:

- *"Ibn' Abbas reported that the Messenger of Allah said: 'He who takes his gift/ donation back is like a dog which takes back its vomiting."*[365]

Along the same lines, the *takaful* operator does not have any obligations to make returns on that fund, or even management of that fund, in a shrewd economical manner as the payment was just a donation. Other authors have raised concerns with the *tabarru* aspect of *takaful* which, although a pioneering approach, significantly lacks the necessary standing from both a *Sharia* and contractual perspective. The whole idea of compensating the participants are thrown into doubt with the *tabarru* concept, as the *takaful* operator is under no obligations and neither are the participants for asking the same, which undermines the *takaful* concept. Perusing this feature of *tabarru* is nothing other than being in breach of *Sharia* regulations.[366]

Fourthly, one specific concern with the hybrid *wakala* and *mudarabah takaful* model is the way the various disbursements of the *takaful* operation are dealt with. Considering the *mudarabah* aspect of the hybrid *takaful* model, the *takaful* operator being the *mudarib* is taking away the management expenses for the *takaful* operation from the *takaful* fund prior to the sharing of the profits. Strictly, they are not entitled to take from the *takaful* fund, save taking their share from the returns of being a *mudarib* and then paying off disbursements such as management fees from that. Conversely, from the *wakala* perspective of the hybrid *takaful* model, the *takaful* operator acts as the *wakil* on an upfront agreed fee and, therefore, under a *wakala* view they are entitled to take off disbursements such as management fees from the *takaful* fund, since no more funds could be earned as *wakil* and it becomes a concern for both *asil* and *wakil* in principle.[367] Given that both the *mudarbah* and *wakala* instruments have been utilised in the hybrid *takaful* model, both procedures are accurate individually; but when applied together in one model, they appear to be in direct contradiction with each other and this creates a major structural issue with the model.

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[365] 2 Mishkat-Ul-Masabih 316 (Al-Haj Maulana Fazlul Karim trans., 1938); Mentioned by Oliver Agha, supra, pp. – 71 - 72
[366] Ibid
[367] Muhammad Ayub supra at p. - 424

Also, on the hybrid *takaful* model, the payments of the management fees take place at the *mudarabah* part of the model. It is opined that, had the hybrid *takaful* model somehow been modified to have the *wakala* part later, then at least deduction of disbursements such as the management fees could have been justified. However, the way the hybrid *takaful* model has been structured means it is not possible to have the *wakala* part at the later end, and so the operation of the whole model is affected.

Fifthly, as mentioned with other models, the *takaful* operator in the hybrid *takaful* model is not responsible and does not bear any underwriting losses.[368] It is opined that this is contrary to the crux of *takaful* analogy of shared responsibility. One may argue that the shared responsibility element exists, in that the participants are mutually assisting each other cooperatively and does not concern the *takaful* operator itself. However, the fact that the *takaful* operator takes from the underwriting income a prearranged fee upfront immediately from the participants' contribution, even before the monies reach the *takaful* fund but would not take the responsibility of underwriting losses, raises concerns and adversely attacks the point of cooperativeness.

Sixthly, as mentioned above, there is the existing issue with the *wakala* aspect and *tabarru* in the hybrid *takaful* model. However, with the hybrid *takaful* model, it is considered from a draconian angle due to the mix of different instruments. With the risk of repeating, *wakala* is a two-way contract, where the principal, i.e. *asil,* instructs the agent, i.e. *wakil,* to act on his/her behalf while, in the hybrid *takaful* model, this is the participants and the *takaful* operator, respectively. Under the *wakala* part of the hybrid *takaful* model, it is the participants who delegate the authority to the *takaful* operator for operation of the *takaful* fund on their behalf. This creates a major issue with veiling the premium as *tabarru* since *tabarru* is a one-sided compromise; this leaves the *takaful* operator in complete control as to how the fund should be managed. This gives rise to a double-edged argument; in that, if the contribution is considered as *tabarru,* then the monies cannot be controlled by participants, since *tabarru* is a voluntary payment with no

[368] Ibid

intention of returns; as such, no power can be delegated by the participants to the *takaful* operator, as the participants would not have the power of authority to delegate in the first place. This would leave the *takaful* operator to deal with the fund in whichever way he feels, rather than dealing with it in the best interest of the participants.[369]

Additionally, this raises doubts as to whether the *wakala* agreement between the parties is, in fact, a valid *wakala* at all. Conversely, the matter takes a turn for the worse as, if the contrary is considered to give effect to the *wakala* agreement (which needs to be a two-sided contract), then it is stated that the contribution by the participants are not in fact *tabarru.* The funds are open to *Sharia* scrutiny of *riba*, *gharar* and *maisir* since now they are considered to be an investment, which calls for clarity of obligations and, therefore, defects the hybrid *takaful* model.

Finally, as author Oliver Agha pointed out, the definition of *tabarru* has been changed in the present day by fervent participants, the aims of whom appear not to make a charitable donation of the funds provided to the *takaful* operator, but to ensure cover of their assets from defined uncertain perils.[370] This thesis agrees with this view of Oliver Agha and this represents meanings that are not *Sharia* approved. However, it is asserted that the participants are not the only ones who appear to have broken the *Sharia* regulations, but mainly the shareholders of *takaful.* The models, so far witnessed, seem to have been driven with the principal aim of increasing the *takaful* revenue, where the representation of *Sharia* instruments can be utilised. This has led to the unfortunate consequence of cumbersome models and it is questionable as to whether they are *Sharia* compliant themselves.

As scholars have pointed out, *tabarru* used in the above context is a legal stratagem, which has gone wrong and the updated model mentioned is not up to the scratch. As Oliver Agha concludes, it is time to "*think outside the box and take up the challenge to create authentic and innovative shari'a compliant products*" as the ones in existence at

[369] Oliver Agha, supra, p. - 84
[370] Oliver Agha, supra, pp. – 84 - 85

present are not viable.[371] It is concurred that, so far, the crisis noticed in *takaful* comes down to the analogies made, which might not be the best for the advancement of Islamic finance. It is in this respect that this thesis aims to consider the various models and opines a new dynamic *takaful* model, which is believed will not only be fully *Sharia* compliant, but also less cumbersome and strong enough to survive, competing with the traditional insurance market, as will be discussed later in the thesis.

8. *Waqf*, the concept:

8.1. Introduction:

A new model that has been floating for some time and is slowing becoming an upcoming concept is utilisation of the *waqf* model for *takaful*. Before discussing the model, it is necessary to give some background information on the concept of *waqf*. To start with, it would need to be stated that *waqf* is a combination of Wills and Trusts, as viewed in English law.

Waqf, in a simple sense, is an endowment that can be considered as being similar to charity that is mainly used for the improvement of the community such as mosques, cemeteries, educational institutes and such others, which allows the rich to distribute wealth towards the needy in a defined *Sharia* manner.[372] The plural of *waqf* is *awqaf*, which is at times described in various Islamic texts. *Waqf* is an Arabic word meaning "*hold, confinement or prohibition*"[373] and the rudimentary literal meaning of the original word means "*stop, block or suspend*".[374] The legal definition of *waqf* is "*to protect*

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[371] Ibid

[372] Asmak Ab Rahman and Wan Marhaini Wan Ahmad, 'The Concept of *Waqf and* its Application in an Islamic Insurance Product: The Malaysian Experience', (2011) 25 Arab Law Quarterly 203, p. - 204

[373] Monzer Kahf, 'Waqf: A quick overview' (Issues 4 March 2012) Vol. 2 ISOC Focus Magazine, page - 12, <http://isocfocus.files.wordpress.com/2012/08/isocfocus_volume2_issue43.pdf> accessed on 16 January 2014

[374] Miriam Hoexter, 2005, 'Waqf"; "*Encyclopedia of Religion*' (2005) Ed. Lindsay Jones, 2nd edn, Vol. 14, Detroit: Macmillan Reference USA, 9676-9679, p. - 9679

something, by preventing it from becoming the property of a third person."[375] However, it originated from the Arabic word *waqafa,* which has two meanings, one "*causing a thing to stop and stand still*" and the second "*pious (charitable) foundations*".[376] In an Islamic context, *waqf* refers to the providing of either a moveable or immovable non-perishable asset from which benefit can be retained, without consummation of the same, for philanthropy purposes; its utilisation can be restricted within set boundaries and the purposes are within the realms of *Sharia.*[377]

The conceptual idea is that, on the endowment act, the item is legally halted from being involved in commercial dealings but its yields are utilised for charitable purposes, which attracts rewards from God, as mentioned in previous chapters where God has encouraged acts of charity.[378] The *waqf* item should attain the purpose of the *waqf* by derivation of the benefit from the item rather than utilisation of the item itself. Therefore, the endowed asset must be permanent, which derives benefits from the usufruct, however, cash *waqfs* are considered as an exception by most schools of thoughts and jurisdictions.[379] Imam Zufar, a prominent Islamic scholar, passed *fatwa* in the 8th century, approving cash *waqf* and confirming that it be utilised on the basis that the corpus of the cash *waqf* was provided to the entrepreneurs as in a *mudarabah* contract, with the return used for the *waqf* purposes; as such, the *waqf* fund would be acting as the *rubb al mal.*[380]

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[375] Al-Sarakhsi, al-Mabsut, Cairo, 1956, vol. 12, p. 27, http://feqh.al-islam.com/Books.asp; translation by Mohd. Zain b. Haji Othman, Islamic Law with special Reference to the Institution of Waqf, Kuala Lumpur: Prime Minister's Department, Religious Affairs Division, 1982, p. 21;
Mentioned in: Mohammad Tahir Sabit b. Haji Mohammad and Abdul Hamid b. Hj. Mar Iman, 'Obstacles of the Current Concept of Waqf to the Development of Waqf Properties and the Recommended Alternative' Department of Land Administration and Development, and Centre for Real Estate Studies, Faculty of Geoinformation Science & Engineering, Universiti Teknologi Malaysia, p. - 28 <http://eprints.utm.my/501/1/27-38.pdf> accessed 21 January 2014

[376] Murat Cizakca, 'Awaqf in history and its implications for modern Islamic economics' (1998) Vol. 6, No. 1, Islamic Economic Studies, pp. – 436 - 437

[377] Waqf Board, '*Waqf* summary' (tnwakfboard) <http://www.tnwakfboard.org/introduction.htm> accessed 22 January 2014

[378] Miriam Hoexter, supra at p. - 9676

[379] Imam Zufar and Maliki School allowed cash *waqf.* Ibn Taymiyah informs Imam Ahmad followers may approve cash *waqf* save Hanbali school followers. Cash *waqf* is allowed in Egypt, Iraq, Syria, Iran, Turkey, India, Pakistan, Burma, and Singapore. Mohammad Tahir Sabit b. Haji Mohammad and Abdul Hamid b. Hj. Mar Iman, supra at p. - 33

[380] Murat Cizakca, supra at pp. – 446 - 452

A *waqf* can be categorised as being a specific *waqf,* where the purposes of the *waqf* are made specific at the time of creation, and general *waqf,* where the *waqf* can be used for any legitimate *Sharia* approved purposes.[381] The valid purpose for which the derived benefit is utilised of the endowed asset is called *qurbah*. Non-Muslims are allowed to create *waqf* and are allowed to have valid *qurbah* as long it is within the *Sharia* remits.[382]

It is considered that the earliest *waqf* relates to the Holy *Kabah*, the sacred worship house in Saudi Arabia, which was built on Prophet Mohammed's (pbuh) arrival in 622.[383] In *Sharia* there are three different types of *waqf*, the first being the religious *waqf* such as funds kept in *waqf* for the development of mosques. The second type is the philanthropic *waqf,* which is set aside for the assistance of the poor and factors that are beneficial for society at large, e.g. library, hospital, research, education, etc. The third type is posterity/family *waqf,* where the owner of the asset assigns a certain portion of the *waqf* for the benefit of his/her descendants, the rest being distributed to the poor.[384]

Assets given to *waqf* must have perpetuity and be given off on a permanent basis and created by someone with legal capacity, e.g. not a minor or someone who is incapable. A *waqf* must be a charitable act and viewpoint of *Sharia,* and the founder and beneficiaries must be alive. The founder is known as the *wakif,* who determines the management and the *waqf* manager, known as *Mutawalli*, is the executor and is responsible for administering the *waqf* in the best interest of the beneficiaries.[385] The *mutawalli* is allowed to take a percentage of the benefit derived from the endowed asset, which is generally about 10% of the remuneration of his/her labour.[386] However, the executor of the *waqf* must be a Muslim with adult capacity, both mentally and legally, with

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[381] Mohamed Ariff, 'Resource mobilization through the Islamic voluntary sector in Southeast Asia; Islam and the economic development of Southeast Asia: The Islamic voluntary sector in Southeast Asia' (1991) Institute of Southeast Asian Studies, pp. – 423 – 435

[382] Miriam Hoexter, supra at p. - 9677

[383] Hamari Web, '*Waqf* on Islamic Perspective' (hamariweb.com) <http://www.hamariweb.com/articles/article.aspx?id=4236> accessed on 23 January 2014

[384] Monzer Kahf, supra at pp. – 12 - 13

[385] Monzer Kahf, supra at p. – 14

Murat Cizakca argued that there had been confusion in the Anglo-Saxon law about distinguishing the nature and function of the owner and trustees but under Islamic law, the *mutawalli*'s job is simply one of that of management of the asset that he had been entrusted with; Murat Cizakca, supra at pp. – 445 - 446

[386] Miriam Hoexter, supra at p. - 9678

knowledge and ethics of Islamic law, and the organisation must be an Islamic *waqf* institution.[387] A *waqf* has certain characteristics that need to be considered before considering the *waqf* based *takaful* models. *Waqf* nature remains the same, irrespective of where it is based in the world, as it is a religious instrument that is dictated under religious guidelines.[388] The relevant characteristics of *waqf* are as follows:

i. It is important to note that, unlike charitable foundations, there is no specific ownership of *waqf* as the individuals who created the *waqf* cannot dispose or change the founding conditions of *waqf*, if wanted upon creation.[389] However, the ownership of *waqf* is generally considered to belong to God. This was mentioned by Justice Whitley's decision in the case of *Haji Salleh Bin Haji Ismail & Anor v Haji Abdullah Bin Haji Mohamed Salleh & Ors* that "*The ownership of the thing immobilised is transferred to God; which means that such object ceases, for men, to be subject to the right of the private property, and that it henceforth belongs neither to the founder nor to the beneficiary.*"[390]

Similarly, in the case of *Re Dato Bentara Luar Decd Haji Yahya Bin Yusof & Anor V. Hassan Bin Othman & Anor,* where Salleh Abas FJ mentioned explicitly that *waqf* "*takes effect immediately from the moment of its creation. The ownership of the wakaf property is in law immediately vested in God Almighty.*" He went further to state on this case, which revolves around the conduct of the founder, Dato, who took the position of *mutawalli* as well in absence of the appointment of an executor, that any wrongdoings by the *wakif* do not invalid a *waqf*, when the intention at the time was clear to create the *waqf*; rather, such actions breach the *watif*'s duty as the *mutawalli*, as he had

[387] Amanah Awqaf, 'The Sunnah & Conditions of Awqaf' (amanahawqaf.org) <https://www.amanahawqaf.org/sunna-conditions/> accessed on 23 January 2014
[388] Murat Cizakca, supra at pp. – 443 - 446
[389] Monzer Kahf, supra at p. – 13
[390] Haji Salleh Bin Haji Ismail & Anor v Haji Abdullah Bin Haji Mohamed Salleh & Ors [1935] 1 MLJ 26; Mohammad Tahir Sabit b. Haji Mohammad and Abdul Hamid b. Hj. Mar Iman, supra at p. - 28

assumed the position and responsibilities of the same.[391] Therefore, this makes the *waqf* upon creation irrevocable, as ownership is no longer in the control of any mortals.[392]

ii. *Waqf* has a lifeline of infinity as, unlike charitable foundations, assets designated for a *waqf* cannot be taken off, unless in very exceptional situations they can be replaced by another, which is exactly specific in value and community service to the former for the same purpose and beneficiaries, along with a court's approval.[393] However, the orthodox position is that *waqf* assets are for perpetuity and cannot be for a limited period, which is in line with the outcome of the *Re Dato Bentara Luar* matter above.

iii. The conditions set by the founders of a specific *waqf* must be followed exactly to the word so long it follows *Sharia* rules and is feasible. In such cases, neither managing authorities nor court has the power to amend *waqf* conditions. In the event that the purpose becomes unfeasible, then the benefit should be spent on the closest purpose intended or otherwise given off to the poor.[394]

iv. The *waqf* asset upon endowment becomes alien to all commercial transactions and so cannot be sold, mortgaged, become long term or permanently leased and it falls outside the author of the *wakif* and *mutwawalli* to do the same.

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[391] Re Dato Bentara Luar Decd Haji Yahya Bin Yusof & Anor V. Hassan Bin Othman & Anor [1982] 2 MLJ 264, 1 LNS 16; Mohammad Tahir Sabit b. Haji Mohammad and Abdul Hamid b. Hj. Mar Iman, supra at pp. – 28 - 29

[392] This concept of irrevocability also finds it support in the Selangor state in Malaysia where under sections 4(1) and 4(2) of Enactment No 7 of 1999 Wakaf (State of Selangor) Enactment 1999 which states about the commencement of *waqf* as follows:
"*(1) A wakaf shall immediately come into effect once all the requirements and conditions of the wakaf had been fulfilled, unless it is expressly provided that it shall commence only after the death of the waqif.*
(2) A wakaf which has come into effect cannot be sold or transferred by the waqif or be inherited by any person."
E-Syariah, 'Selangor state statute' (esyariah.gove.my)
<http://www.esyariah.gov.my/portal/page/portal/Portal%20E-Syariah%20BI/Portal%20E-Syariah%20Carian%20Bahan%20Rujukan/Portal%20E-Syariah%20Undang-Undang/Portal%20E-Syariah%20Undang2%20Selangor> accessed on 25 January 2014

[393] Monzer Kahf, supra at p. – 13

[394] Ibid

However, only in exceptional cases, e.g. where the *waqf* asset is at risk of becoming dilapidated, can it be long leased or exchanged but only with the court's authority.[395]

v. The individuals who are setting up the *waqf* cannot create a valid *waqf* until debts are cleared or if it needs the debtor(s) approval. Clearing of outstanding debt is considered compulsory and takes priority, compared to *waqf,* which is considered an act of voluntary donation.[396] Similarly, the *waqf* asset must be from privately owned capital.[397]

8.2. Religious law:

Waqf has been considered in a number of places in the *hadiths* of the Prophet Mohammed (pbuh) and is considered to be a fundamental part of *Sharia* law. There are some disagreements amongst different schools of thought on aspects of *waqf* but, due to the limited scope of this thesis, it must concentrate on the mutually acceptable concepts. As mentioned above, one of the first *waqf* in history is considered to be the Holy *Kabah* itself. However, one of the significant *hadiths* on *waqf* dealt with the circumstance when Ibn Umar obtained a piece of land in a place called Khaibar, when he approached Prophet Mohammed (pbuh) for advice and this has been mentioned in Book 13, Hadiths 4006 to 4008 of Sahih Muslim. In the relevant Hadith 4006, Ibn Umar reported that:

- "... *He said: Allah's Messenger, I have acquired land in Khaibar. I have never acquired property more valuable for me than this, so what do you command me to do with it? Thereupon he (Allah's Apostle) said: If you like, you may keep the corpus intact and give its produce as Sadaqa. So 'Umar gave it as Sadaqa declaring that property must not be sold or inherited or given away as gift. And Umar devoted it to the poor, to the nearest kin, and to the emancipation of slaves,*

[395] Miriam Hoexter, supra at p. - 9678
[396] Amanah Awqaf, 'The Sunnah & Conditions of Awqaf' (amanahawqaf.org) <https://www.amanahawqaf.org/sunnah-experience-of-awqaf/> accessed on 23 January 2014
[397] Murat Cizakca, supra at p. - 446

aired in the way of Allah and guests. There is no sin for one, who administers it if he eats something from it in a reasonable manner, or if he feeds his friends and does not hoard up goods (for himself). He (the narrator) said: I narrated this hadith to Muhammad, but as I reached the (words) 'without hoarding (for himself) out of it' he (Muhammad' said: 'without storing the property with a view to becoming rich.' Ibn 'Aun said: He who read this book (pertaining to waqf) informed me that in it (the words are) 'without storing the property with a view to becoming rich.'"[398]

As the *hadith* makes it apparent, the ideology of *waqf* is to assist the poor by making the endowed asset a charity, from which those in need can use the derived benefit. The maintainer of the *waqf* and his/her associates can have reasonable recourse as remuneration, but the *waqf* asset should never be kept and utilised to become wealthy.[399] Additionally, in Book 38, Hadith 507 of Sahih Bukhari, it has been narrated by Amr in relation to the *waqf* of Umar, again echoing the analogous message to avoid having the mindset of building riches using *waqf*. It is stated on this respective *hadith* that:

- "*It was not sinful of the trustee (of the waqf) to eat or provide his friends from it, provided the trustee had no intention of collecting fortune (for himself). Ibn 'Umar was the manager of the trust of 'Umar and he used to give presents from it to those with whom he used to stay at Mecca.*"

Similarly, in another important incident relating to the rise of *waqf* as discussed in Ibn al Athir 1976, v. 8, pp. 637-8, and 642, when one of the companions of the Prophet Mohammed (pbuh), Uthman Ibn Affan, brought the Romah Well in Medina, at a time when water was sold at very high price. He purchased the well and made the well free for

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[398] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=waqf&translator=2&search=1&book=&start=0&records_display=10&search_word=all> accessed on 24 January 2014

[399] As readers will note later that the researcher would argue that the hybrid *waqf takaful* model introduced does exactly that, in contravention of *Sharia* rules as *takaful* is a commercial venture to make money and this raises doubts on the workability of hybrid *waqf takaful* model in attaining *halal* status and meeting economical objectives at the same time.

everyone to enjoy the water from within it.[400] *Waqf* has been viewed essentially as an important charity and the significance of charity have been noted in Book 13, Hadith 4005 of Sahih Muslim, by Abu Huraira, when Prophet Mohammed (pbuh) mentioned that:

- "*... When a man dies, his acts come to an end, but three, recurring charity, or knowledge (by which people) benefit, or a pious son, who prays for him (for the deceased).*"[401]

Additionally, in connection with *waqf* as providing charity, it has been mentioned in a number of the verses of the Holy *Quran* including 2:215, 2:264, 2:270, 2:280, 3:7, 111:92, 58:12, 58:13,[402] and one of the relevant sections mentioned in the Holy *Quran* is in *Surah Ali Imran* (Chapter 3), Verse 92 that:

- "*Never will you attain the good [reward] until you spend [in the way of Allah] from that which you love. And whatever you spend - indeed, Allah is Knowing of it.*"[403]

8.3. Hybrid of *Waqf, Wakala* and *Mudarabah* based *Takaful* model:

In the recent times, it is considered that the final two models mentioned above would assist in the advancement of *takaful*.[404] Therefore, jurists have come up with the introduction of a combination of the *wakala*, *mudarabah* and *waqf* model for *takaful*. It was the brainchild of leading Islamic scholar, Justice Mohammad Taqi Usmani (Abdul

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[400] Amanah Awqaf, 'The Sunnah & Conditions of Awqaf' (amanahawqaf.org) <https://www.amanahawqaf.org/sunnah-experience-of-awqaf/> accessed on 23 January 2014
[401] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=13&translator=2&start=10&number=3996> accessed on 23 January 2014
[402] Murat Cizakca, supra at pp. – 441 - 443
[403] Holy *Quran*, '*Surah Ali Imran*' Chapter 3 Verse 92 (quran.com) <http://*Quran*.com/3> accessed on 24 January 2014
[404] Muhammad Ayub, supra at p. - 423

Jalil and Abdul Rahman, 2011; Raj, 2007);[405] but, as will become clearer, it is somewhat of a hodgepodge of various models discussed above. This appears to be favoured in Pakistan and the underlying idea is that the donations that are provided would be under the *waqf* principles that are to be used for the participants' benefit. The profit generated through investment of these donations would be used to pay liabilities such as claims, whilst preserving the rest of the characteristics of the model in line with the remainder of Islamic instruments.[406]

However, before proceeding further into the operational details of this model, it is intended to lay down a formula for the assistance of perusal, as follows:

Hybrid *Waqf* model = *Waqf* + *Wakala* (fixed fee contract) + *Mudarabah* (return sharing contract) + *Tabarru* (fund/charity) + Cooperative loss sharing (principle)

The conceptual idea of this hybrid *waqf* model commences with the *takaful* shareholders making a preliminary donation to create a *waqf* fund, with the intention of assisting individuals against defined casualties.[407] This fund, provided by the shareholders, is considered as "seed" money, which is lost forever to give life for the creation of the *waqf* fund.[408] This *waqf* fund will act in accordance with the *waqf* deed that is created and comes into existence. The *takaful* starts its business by inviting prospective participants to pay *tabarru* into the *waqf* fund. In principle, the *waqf* fund now becomes the owner of all contributions and deals with investments, claims and such others (Yusof, wan Ismail & Mohd Naaim, 2011).[409]

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[405] Apnizan Abdullah and Hakimah Yaacob, 'Legal and Sharia issues in the application of Wakala-Waqf model in Takaful industry: An analysis' (2012) 65, 1040 – 1045, Procedia – Social and Behavioral Sciences, p. – 1042 <http://www.sciencedirect.com/science/article/pii/S187704281205224X#> accessed 25 January 2014

[406] Haemala Thanasegaran, supra at p. – 110

[407] If the shareholders want to cover different types of insurance products then they can create different types of *waqf* based *takaful* fund in this model to cover bigger market.

[408] Yusof M F, 'Fundamentals of Takaful' (Kuala Lumpur: IBFIM, 2011) <http://www.islamicbanker.com/education/takaful-%E2%80%93-waqf-model> accessed 21 January 2014

[409] Apnizan Abdullah and Hakimah Yaacob, supra at p. - 1042

As participants would be making payment of their respective donations, the monies would be split into two, with one part going into the *takaful* fund for the sole aim of dealing with cooperative loss sharing. The other part goes into considering as investment under the principles of a *mudarabah* contract. However, before the splitting of the funds, the *takaful* operator would take a percentage of the participants' contributions that are put into the *waqf* fund, as part of their fees under the *wakala* contract. The *takaful* operator acts as *wakil* in the management of the fund that has been provided by the participants.[410]

Subsequently, the part that is separated for the purpose of investment is invested and the returns made from that investment are shared between the *takaful* operator and the participant under the *mudarabah* contract. The remainder of the part of the contribution stays in the *waqf* fund and, along with the percentage return of the participant, is used for the operational costs of *takaful* such as claims, *retakaful,* etc. Following these deductions, the surplus is paid back to the participant. Conversely, the remainder of the *mudarabah* share of the *takaful* operator, along with the *wakala* fee collected, are used to pay off management-related expenses of the *takaful* organisation, following any profits that are provided to the shareholders of the *takaful* organisation. In circumstances where there is a surplus of the underwriting sales that can be used for the benefit of the *waqf,* as the generated fund belongs to the *waqf,* this may be kept in the *waqf* fund, but in the event of deficit, the shareholders of the hybrid *waqf* based *takaful* provide a *quad hasan* to save the *takaful* entity from adverse liabilities.[411]

It is relevant to state that, whilst in all the other models, the concept of *tabarru,* i.e. donation, was basically the driving force for the progression, the hybrid *waqf* model *waqf* itself is a legal entity and the central idea is the concept of joint guarantee instead. This is because, unlike other models, in the hybrid *waqf* model, the association between the participants and the *takaful* operator is the *waqf* itself and they both coexist because of this connecting chain, where the *takaful* operator acts as *waqf*'s agent initially.[412]

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[410] Muhammad Ayub, supra at pp. – 424 - 426
[411] Ibid
[412] Yusof M F, 'Fundamentals of Takaful' (Kuala Lumpur: IBFIM, 2011) <http://www.islamicbanker.com/education/takaful-%E2%80%93-waqf-model> accessed 21 January 2014

Diagram 6.6 shows the hybrid *Waqf, Wakala* and *Mudarabah* based *Takaful* model. For analysis of this diagram, the following variables are used, keeping in line with the examples given in this thesis: £x = Premium/ Contribution/*Tabarru* paid by the participant to the *takaful* operator.

8.4. Problems with the hybrid *Waqf, Wakala* and *Mudarabah* based *Takaful* model:

The concept of using *waqf* is surely another creative innovation, which is a further progression of Islamic finance into the insurance sector. Although the model may appear intriguing in an effort to reach the same conclusion as traditional insurance, even with the hybrid *waqf* model, there are a number of factors which simply make it unworkable.

Firstly, *waqf* is an Islamic social instrument that aims to assist others from a humanitarian perspective. As has been discussed above, the conceptual texts and religious references made demonstrate that the paradigm of a *waqf* creation is to improve the overall fabric of the society. The aim was not meant at assisting the founder, i.e. *wakif,* or the *waqf* fund itself to make its riches by running the *waqf* as a business. This is a view also considered by scholar, Aly Khorshid, who states that the idea of *waqf* is to get closer to God by making it as a *sadaqa,* i.e. non-obligatory sacred donation. Whereas, in a hybrid *waqf* model, the participants' central idea is to cover the loss of his property against unknown calamities, the shareholders of the *waqf* make profits from running the *waqf* as a commercial venture, which lacks the primary intention of piety as is required in a true *waqf.*[413]

Similarly, author Miriam Hoexter states that the notion of having a *waqf* is for redistribution of funds from rich to poor and states that the basic foundation of *waqf* is for

[413] Aly Khorshid, *Islamic insurance: A modern approach to Islamic banking* (1st edn, Routledge publications 2004) p. - 21

"*charity, piety, and the hope for recompense in the world beyond*".[414] It becomes questionable how that can be ever attained in a hybrid *waqf takaful* model, as the mental motivation of the *waqf* created, has hardly anything to do with the aims mentioned but, as Aly Khorshid states, is simply for own safeguard and benefits.[415] Along the same lines, a *waqf* that is contingent on events, save when the *waqf* becomes effective upon death of *wakif,* would be considered not as a valid *waqf.*[416] This creates a major problem for the hybrid *waqf* model as the whole idea of having the *waqf* model is that it becomes effective when the participants are subjected to defined casualties, and this could risk the model falling foul of *Sharia* rulings.

Secondly, one of the major issues with using *waqf* as a model for *takaful* is that *waqf* is a creation of religious law, whereas the *waqf* is being implemented into different jurisdictions, which have their own jurisdictional laws. When *waqf* is considered similar to a Trust, there is a possibility that the Trust law of a particular jurisdiction may conflict with *Sharia* law, which in itself raises a risk. As an example, under Malaysian law the State's Religious Council (SRC) becomes the sole trustee of any *waqf* in Malaysia; however, with cash, it is unclear whether the same would breach any of the Malaysian laws and execution of the same for liquid *waqf.* In addition, it becomes a concern that the SRC and *waqf* fund are separate legal entities, which makes the perpetuity of the *waqf* maintenance an issue. Also, in the hybrid *waqf* model, the shareholders using the *waqf* deed execute the *waqf*; as a result, this throws doubt on the legal status of the *waqf* deed in terms of the whole model in consideration of the above case.[417]

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[414] Miriam Hoexter, supra at p. – 9677

[415] This raises additional question on any possible scope of determination by the *takaful* whether any prospective participant making claims under the policy is in fact in need, as is required by *waqf* principles. It could be argued that the *waqf* is regulated under the *waqf* deed, which stipulates that the participant suffering defined losses are in fact needy. However, it could be very well possible that same participant might have enough wealth and have recourse to additional funds without any difficulty whereas another participant who also made the claim might not have the same recourse. This creates the concern on how to determine whether someone is needy or not and up to how much funds does anyone have to have to qualify for compensation under the policy. In such circumstances, accepting both claims creates the difficulty that *waqf* principles of assisting poor and needy is not followed appropriately but on the other hand, accepting one claim and rejecting another creates the difficulty that the *waqf* deed conditions are not followed appropriately. This creates a significant issue with using a socially responsible instrument as a commercial instrument to make riches, when it was not designed in that fashion.

[416] Aly Khorshid, supra at p. - 20

[417] Apnizan Abdullah and Hakimah Yaacob, supra at pp. – 1042- 1043

Thirdly, continuing with the above point of perpetuity, as in *takaful* the shareholder would appoint the *takaful* operator to administer the *waqf,* but this may be in conflict with the national laws of each jurisdiction. Therefore, in the event where there is direct conflict of administration of the *waqf,* the hybrid *waqf takaful* may be held invalid; this raises serious concerns as to the condition of the *waqf* fund, as to whether it can survive the perpetuity as required.[418] It is questionable what will happen to the funds already provided and it is not farfetched to visualise there may be a conflict of laws if the hybrid *waqf* model is applied under English law jurisdiction.

Fourthly, returning to the point of cash *waqf* mentioned earlier, although it has been approved by most schools of thought, there are concerns as to whether the dogma of cash *waqf* actually follows the principles of irrevocability, perpetuity and inalienability of *waqf* because of the liquid nature of the cash *waqf.* On one hand, most scholars have approved the cash *waqf* by practice and custom.[419] One famous Islamic scholar, Ibn Abidin, confirmed that the dirham and dinar are acceptable, provided they are invested, and the capital along with profit are returned back to *waqf.* He argued that cash *waqf* has perpetuity as the value of the cash remains at all times, which determines the amount and exists forever in time. Some scholars argue that it is the benefit of the *waqf* asset and not the *waqf* asset itself that needs to have perpetuity.[420]

However, there is a concern about the perpetuity of the profit derived in a hybrid *waqf takaful* model, as not all the profits generated from the *waqf* in reality finds its way back to *waqf.* As noticed from the model above, the profits derived are split into percentages under the *mudarabah* agreement, with the *takaful* operator taking their share before going through distillations of paying for various disbursements; the profits eventually find their way to the shareholders. This creates the dilemma of whether the whole of the funds generated from the *waqf* asset actually find their way back to the *waqf* fund and, as such, raises the question as to whether it is a valid *waqf.* It also differs to the latter view as,

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[418] Apnizan Abdullah and Hakimah Yaacob, supra at p. – 1043
[419] Ibid; The authors refers to the concept of *u'ruf,* which is an Arabic word meaning customary rules
[420] Mohammad Tahir Sabit b. Haji Mohammad and Abdul Hamid b. Hj. Mar Iman, supra at p. - 35

without the source of benefit derivation, the benefit risks coming to an end after a while, which attacks perpetuity. Also, the ideology of *waqf* relates to the fact that the *waqf* assets are to be preserved carefully so as to prevent them from being mismanaged, which will be hindered if the focus is on the benefit derivation concept and the *waqf* asset itself is ignored.

On the other hand, Muslim followers of the Hanbali school of thought are strictly against the use of cash *waqf* and they do not accept it as being a valid *waqf*.[421] This risks a significant portion of the Muslim community themselves from considering the hybrid *waqf takaful* to be an acceptable insurance model, when the whole notion of going through these many hoops is to introduce a *Sharia* compliant model. Aly Khorshid continues his argument that cash *waqf* has other issues when used in a hybrid *waqf takaful* model as, to keep in line with the *waqf* principle, the *waqf* asset cannot be lost but only its benefits. Therefore, any claims for compensation must come from the return on investment of the *waqf* cash, which undoubtedly has to be substantial and cannot come either from the cash *waqf* of the shareholders, or from the contribution provided by the participants. This creates a significant and challenging gap in pure returns only, which is quite impracticable as, for the first few years of trading the *takaful* operator would have that huge amount of capital which would make that much significant returns to handle all the claims made.[422]

Fifthly, there is another major issue about the operation of a hybrid *waqf takaful*, which is reinsurance. The ownership of *waqf* is considered to belong to God alone and there are very few providers of reinsurance that are *Sharia* compliant. This raises the question of whether such reinsurance is acceptable as reinsurance is a very important concept in insurance business. To circumvent reinsurance, some scholars state that, if the investment from a *waqf* fund is appropriately managed, then it will generate profits.[423] It would be counter argued that there is always a possibility that, even with the best management of the investment, there is always a risk of loss of investment as market results are simply

[421] Aly Khorshid, supra at p. - 20
[422] Aly Khorshid, supra at p. - 21
[423] Apnizan Abdullah and Hakimah Yaacob, supra at pp. – 1043 - 1044

unpredictable, as seen in recent years. Furthermore, avoidance of reinsurance may not be always feasible as there could be regulatory requirements of various jurisdictions, which might require new entrants such as a hybrid *waqf takaful* to have additional cover, for the safeguard and best interests of its consumers.

This relates to the concept of maintaining a solvency margin of the *takaful* operation to ensure that it can meet the prospective claims of participants. With a hybrid *waqf takaful*, the *waqf* fund is considered to be similar to a trust fund and is not designed to act as an account, which sets aside solvency margin monies.[424] The *waqf* fund is there, as mentioned earlier, to assist from the derived benefit the specific group of beneficiaries and keeps aside funds to stay afloat; due to the operational structure of a *takaful* business it is likely to take the matter out to remit of being a valid *waqf*. This creates a double-edged sword, as the hybrid *waqf takaful* model is at risk of being insolvent if there is not a sufficient solvency margin; conversely, application of the same risk could be a different concept than the instrument actually intended.

Sixthly, in each trading year, various participants will move in and out of the *takaful* as is natural with insurance business. This creates another issue, as the beneficiaries of the *waqf* are constantly changing; this is forbidden under the Hanbali school of thought and affects the validity of the *waqf*. On a similar note, payment of claims under the *waqf* are dependent on unforeseen defined calamities taking place, and would likely face criticism of its validity by the Hanbali school of thought.[425]

In addition to all the points mentioned above, it is felt there are a few minor views that attack the credibility of the hybrid *waqf takaful* model. Without repeating the problems mentioned above about the specific problems with *wakala* and *mudarabah* features in *takaful* models, concentration should be given to cover the aspects of the new element, *waqf*.

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[424] Ibid
[425] Aly Khorshid, supra at pp. – 21 - 22

Seventhly, the *waqf* has been created to solely assist the beneficiaries, i.e. in this case, the participants. However, in a hybrid *waqf takaful* model, during the various processes it may be impossible to subsequently determine the initial money provided by the shareholders to start the *waqf* fund. This creates the risk that, ultimately, when the shareholder take funds out of the hybrid *waqf takaful* model as profit, they could have been taking their own funds as the various funds had commingled in the process.

Eighthly, any *waqf* beneficiaries can be chosen by the *wakif,* but one excluded segment of the beneficiaries of *waqf* are those who are at war with Muslims; nevertheless, scholars stated that non-Muslim citizens of an Islamic state can be beneficiaries.[426] However, it is opined that this creates concern, as non-judicial political aspects appear to control and prejudice the regulation of private individual law on whether the participant would get compensated under the terms of a valid indemnification policy in the event that the war had not started at the time the policy was taken.

Along the same beat, some scholars orate that executors of *waqf* must be a Muslim which, although not followed by the Hanafi school of thought,[427] raises some concerns as to whether a hybrid *waqf takaful* model can be operated in Western jurisdictions. While it is natural for qualified non-Muslims to be executors for the best management of organisations, this can hinder development, particularly in non-Muslim countries. At the same time, it is noted that the founder of the *waqf* must not leave Islam, otherwise the basis of *waqf* is considered invalid and the *waqf* passes to the founder's successors.[428] Without reiterating the stated argument, it simply does not appear to be a sustainable model, as business needs to transact with both Muslims and non-Muslims in this world.

Ninthly, *waqf* as an instrument does not have a niche in jurisdictional laws, as it has characteristics of various components and requires special regulations for *waqf*, particularly in non-Islamic countries. For example, in India the **Wakf Act 1954** was

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[426] The Pious Waqf, '*Waqf* requirements' (piouswaqf.org) <http://www.piouswaqf.org/whatiswaqf.php> accessed 28 January 2014

[427] Ibid

[428] H.A.R. Gibb and J.H. *Shorter Encyclopedia of Islam*, (E.J. Brill, Leiden Netherlands 1953) pp. – 624 - 625

enacted and later updated by the **Wakf Act 1995**. The Central Wakf Council oversees the respective Union Minister of Law that manages the *waqf*s in different states. Similarly, in Kenya the **Wakf Commissions Act** of 1951 was enacted, which has various rules on the administration of *waqf* in Kenya. In Europe, Australia and USA, the *waqf* fund is administered by using a not-for-profit organisation, which owns the *waqf*.[429] However, so far, no legislation or framework has been set up in the UK, which means there is no statutory protection of such a financially delicate instrument. A not-for-profit organisation registration would not have adequate legs to stand on, as would be expected of an insurance business, and is unlikely to have the regulatory bodies such as the Financial Conduct Authority and Prudential Regulation Authority, approval since it would not appear as a sustainable business when the same, by its nature, is simply a registered charity and not financial in principle.

Tenthly, another critical point to reconsider is that the fundamental *hadith* of *waqf*, as mentioned above, repeats that:

- "*"without hoarding (for himself) out of it," he (Muhammad' said: "without storing the property with a view to becoming rich."*"[430]

This makes it very clear that the objective of *waqf* cannot be for increasing one's wealth. However the conceptual diagram of hybrid *waqf takaful* is nothing other than a commercial venture to increase funds so that the shareholders can make a profit. Scholars consider Islamic contracts as either "for consideration" or "not for consideration" and consider *waqf* as falling under the latter. This is because a *waqf* founder is considered to be an ideal Samaritan who unreservedly donates to others simply for the sake of pleasing God, whether it be persons, groups or society. Various examples of *waqf* have been provided, which included assisting the newly qualified entrepreneurs, building schools and clinics to help educate and help the sick, and helping the very vulnerable like orphans

[429] Monzer Kahf, supra at pp. – 14 and 15
[430] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=waqf&translator=2&search=1&book=&start=0&records_display=10&search_word=all> accessed 23 January 2014

and the eldery. The whole aim is to assist individuals and society to improve and grow in a positive manner by reducing poverty and effective wealth distribution, but none of these aspects relate to the founder of the *waqf* wealth improvement.[431] The hybrid *waqf takaful* model is a business project where the shareholders are not there to make pure non-returnable investment, while the policyholders' aim is to cover their own assets and nothing else. It is asserted that the two arguments conflict head on and that it is unlikely to be *Sharia* compliant, otherwise it would result in one of the instruments being unacceptable.

Finally, *waqf* allows its *mutwawalli* to take remuneration from the proceeds made from the derived benefits of the *waqf* asset. However, in the hybrid *waqf takaful* model, it appears that the designers failed to consider any remuneration of that aspect. This raises doubts as to whether the model could have been made more financially stable or worse, whether once more, the meaning *waqf* is satisfied to the fullest and if this really is a valid *waqf,* as such whether this *waqf takaful* model is actually a fully *halal* model. Even if the remuneration of *mutwawalli* was set as negligible to nil, it would have sufficed rather than not considering the issue at all.

In consideration of the above points, it becomes doubtful whether a hybrid *waqf takaful* model has the potential to move up the insurance sector. The problem with a hybrid *waqf takaful* model is not simply restricted to legal concepts of insurance, the aspects of which are cumbersome, but the internal concepts clash with each other from a *Sharia* perspective as well; the definition of *waqf* itself is not satisfied to the fullest and this prevents the whole model from progressing any further. The central paradigm is to create a *halal* insurance model; however, if it cannot be fully *Sharia* compliant, as noted from the points above, it is unlikely that it can be a sustainable model from the business-wise, legal-wise and religious-wise perspective. The attempt of using a social model as a commercial venture is not something that can be utilised.

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[431] Dr. Muhammad Sharif Chaudary & Mr. Hafiz Mujeeb Baig, 'Waqf – Concept and Integration in Islamic financial system' pp. – 2 - 3 <http://www.kantakji.com/fiqh/Files/Wakf/b105.pdf> accessed 24 January 2014

9. *Takaful* settlement of claims:

It is felt that, before concluding this chapter, it is best that the processes of settlement of *takaful* claims are dealt with. Dealing with *takaful* claims is similar to the Western traditional insurance claims procedures, as the underlying ideology is one of contract law. Mohd Ma'sum Billah sets out four different steps in relation to dealing with *takaful* claims, which he sets out in a tabular format in his essay.[432] However, to be precise, the analogy of payment of *takaful* claims is a lot simpler.

The initial aspect to consider is that, when a claim is made, whether the policy is still valid at the time the claim was made, i.e. the policy had not expired, as otherwise there is no ongoing contractual obligation between the parties. The next aspect is consideration of the risk coverage by the *takaful* operator, i.e. whether the catastrophe for which indemnity is asked for is one of the insured perils. Mohd Ma'sum Billah emphasises the position where a fatality has taken place; the reason for the cause of death would not be one of the determining factors, irrespective of whether the same has occurred,[433] keeping in line with the wording of the Holy *Quran* as mentioned in *Surah Ali Imran* (Chapter 3), Verse 145 that:

- *"And it is not [possible] for one to die except by permission of Allah at a decree determined..."*[434]

This point correlates with the fact that, when a claim is made, liability does not appear to be an argument, from the *takaful* operator's perspective. This would be a rather exceptional approach to deal with claims as, in Western traditional insurance practice, liability disputes appear to be a common point of concern.[435] Another point to consider is the aspect of warranty in the making of *takaful* claims. The term warranty in this regard is

[432] Mohd Ma'sum Billah, supra at pp. – 414 - 415
[433] Ibid
[434] Holy *Quran*, *'Surah Ali Imran'* Chapter 3Verse 145(quran.com) <http://*Quran*.com/3> accessed on 3 August 2013
[435] The researcher feels from his experience that Insurers tend to raise arguments of liability in significant number of matters even when liability can be apportioned at the start of the claim, which could save a lot of time and costs.

different from the warranty concept understood under English insurance law or English marine insurance law, where warranty is deemed to be a stipulation of the insurance contract. In *takaful* claims, as Mohd Ma'sum Billah mentions, warranty in *takaful* aims to deal with the limitations on the *takaful* policy on pay-outs of valid claims, due to the constitution of the *takaful* company. The idea is to control the amount of funds going out of the *takaful* organisation on liabilities.[436]

The final part is the consideration of excess, i.e. the amount of funds that the participant would have to pay towards a claim, should a claim be made. The aim is to control claims of diminutive value so as to avoid rattling the *takaful* fund as little as possible. Along the same lines is the issue of quantum on consideration of a claim made, whether the quantum amount asserted is in fact adequate.[437] The objective once more is to control the impact on the *takaful* fund so that it is not disturbed by small value claims. Where the quantum claimed amount is little and within the excess amount, the amount that is fixed in advance at the time of contract, the *takaful* fund would not get involved in payment of it; rather, the participant pays for it himself, as it is outside the ambit of the *takaful* contract that had been agreed between the parties. As can be witnessed, the working method itself is not very different from traditional insurance. The only dilemma is still the search for a model that will fit in with the orthodox insurance sector, but it must comply with *Sharia* provisions at all times.

10. Conclusion:

In conclusion, it is safe to say, in consideration of the above *takaful* models, that there are major concerns about their present stability. The analysis portrayed demonstrates that, not only are the internal applications of *takaful* models clashing and incompatible with each other, but they themselves are breaching various *Sharia* provisions. These issues attack the heart of the working principle of the creation of an alternative to traditional insurance and the outcome is nothing short of discontent. Any satisfactory *halal* model must not

[436] Mohd Ma'sum Billah, supra at pp. – 414 - 415
[437] Ibid

only comply with *Sharia* provisions, but also with the respective jurisdictional laws, an evident fact that has been noted by other scholars as well.[438]

This causes a domino effect when there is a conflict of laws between jurisdictional law and *Sharia* principles. A common case law that was presented before the English Court of Appeal was in the matter of *Shamil Bank of Bahrain EC v Beximco Pharmaceuticals Ltd*,[439] where the court had to determine whether English or *Sharia* law applied when the governing law paragraph of contract between the parties stated that "*Subject to the principles of the Glorious Shari'ah, this agreement shall be governed by and constructed in accordance with the laws of England*". The court determined that English law applied for the determination of the parties' liability and the *Sharia* obligations only related to the bank's operation. A similar situation was faced in Malaysia in the cases of *Bank Islam Malaysia Berhad v Adnan bin Omar*,[440] and in *Dato' Nik Mohmud bin Daud v Bank Islam Malaysia Berhad*,[441] where the Malaysian court determined that the civil law of mercantile applied rather than *Sharia* law. The Malaysian former Chief Justice of Federal court, Honourable Tun Dato' Seri Abdul Hamid Bin Haji Mohamad, noted with concern that cases with *Sharia* law issues require special knowledge of Islamic finance by judges, and the judges in Malaysia were urged to refer such matters to the National *Shari'ah* Advisory Council (NSAC) at Bank Negara Malaysia to assist in the formation of a decision.[442]

However, Malaysia no doubt is an exception where there are parallel laws present for catering needs. However, for the majority of countries, such as the UK, it is necessary to devise a *takaful* model, which can subsist with both *Sharia* law and jurisdictional law,

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[438] Madzlan Mohamad Hussain, "Legal issues in *Takaful*", in the Textbook: Editor: Simon Archer, Rifaat Ahmed Abdel Karim and Volker Nienhaus, 'Legal issues in *Takaful*' in the Textbook: Simon Archer, Rifaat Ahmed Abdel Karim and Volker Nienhaus (eds), *Takaful Islamic insurance: Concepts and Regulatory issues* (John Wiley & Sons Asia Pte. 2009), p. - 72

[439] Shamil Bank of Bahrain EC v Beximco Pharmaceuticals Ltd (No 1), 2004 EWCA Civ 19; [2004] 1 WLR 1784; [2004] 4 All England Law Report 1072; [2004] 2 All England Report; Madzlan Mohamad Hussain, supra at pp. – 72 - 73

[440] Bank Islam Malaysia Berhad v Adnan bin Omar [1994] 3 CLJ 735; [1994] 3 AMR 44; Madzlan Mohamad Hussain, supra at p. – 73

[441] Dato' Nik Mohmud bin Daud v Bank Islam Malaysia Berhad [1996] 4 MLJ 295; Ibid

[442] Ibid

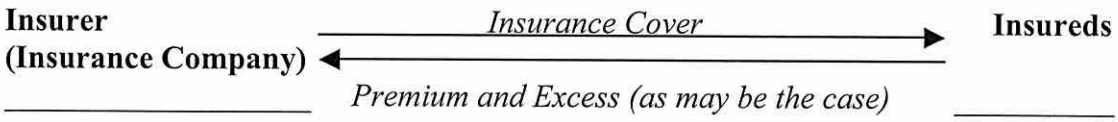
e.g. English law, at the same level without contradicting each other. As an illustration, it could quite easily be the case that, if the latest model of *takaful,* i.e. the hybrid *waqf, wakala* and *mudarabah* based model, is implemented in the UK, English law is very likely to apply trust law to analyse *waqf* related disputes.[443] This is because *waqf* is an endowment, which had been established by a settlor, with executors executing the *waqf* for the benefit of the stated beneficiaries. This could become a major cause of concern, if and when trust law is applied, as to whether it would sit well with *waqf.* To make matters worse, *waqf* itself may also not sit well with *Sharia* rules, as its nature has changed in the *takaful* model. This challenges the whole viability of *takaful* models that are in operation at present and there is a dire need for a new improved model that will be compatible with *Sharia* rules. To avoid such disorder, it would not come as a surprise for even a devout Muslim to feel discouraged by *takaful* and would consider turning to traditional insurance for aid instead. At the end of the day, as witnessed above, existing *takaful* models are not providing a fully *Sharia* compliant solution.

As mentioned earlier, the important concepts this thesis relates to are premium, risks, excess and compensation. It is intended that the premium and risks can be assorted with some sort of trading relationship, either in labour or goods. The excess needs to be covered in a payment return relationship and compensation needs to represent a situation, which is paid out to offset risks when they turn adverse. The analogies may remain separate, but all the compounds need to fit in, in one big structure, that will make a proposed *takaful* model. Therefore, with these issues in mind, the next chapter will introduce some new elements available in Islamic finance, which will be acceptable by everyone. To date, however, these elements do not appear to have been scrutinised from a *takaful* perspective and it is suggested that these, perhaps, hold the key to unlocking an innovative *takaful* model, which may combine the best of both worlds.

[443] Madzlan Mohamad Hussain, supra at p. – 75

Diagram 6.1: A concise pictorial comparison:

Western traditional marine insurance:



***Takaful* insurance:**

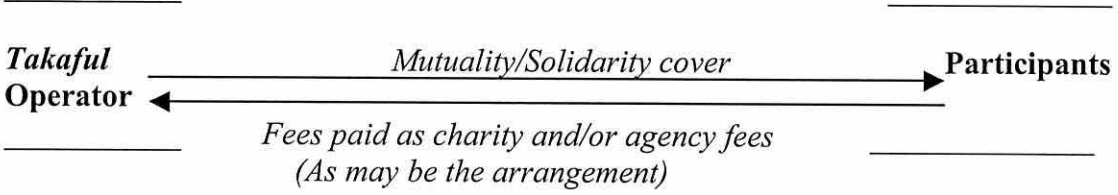
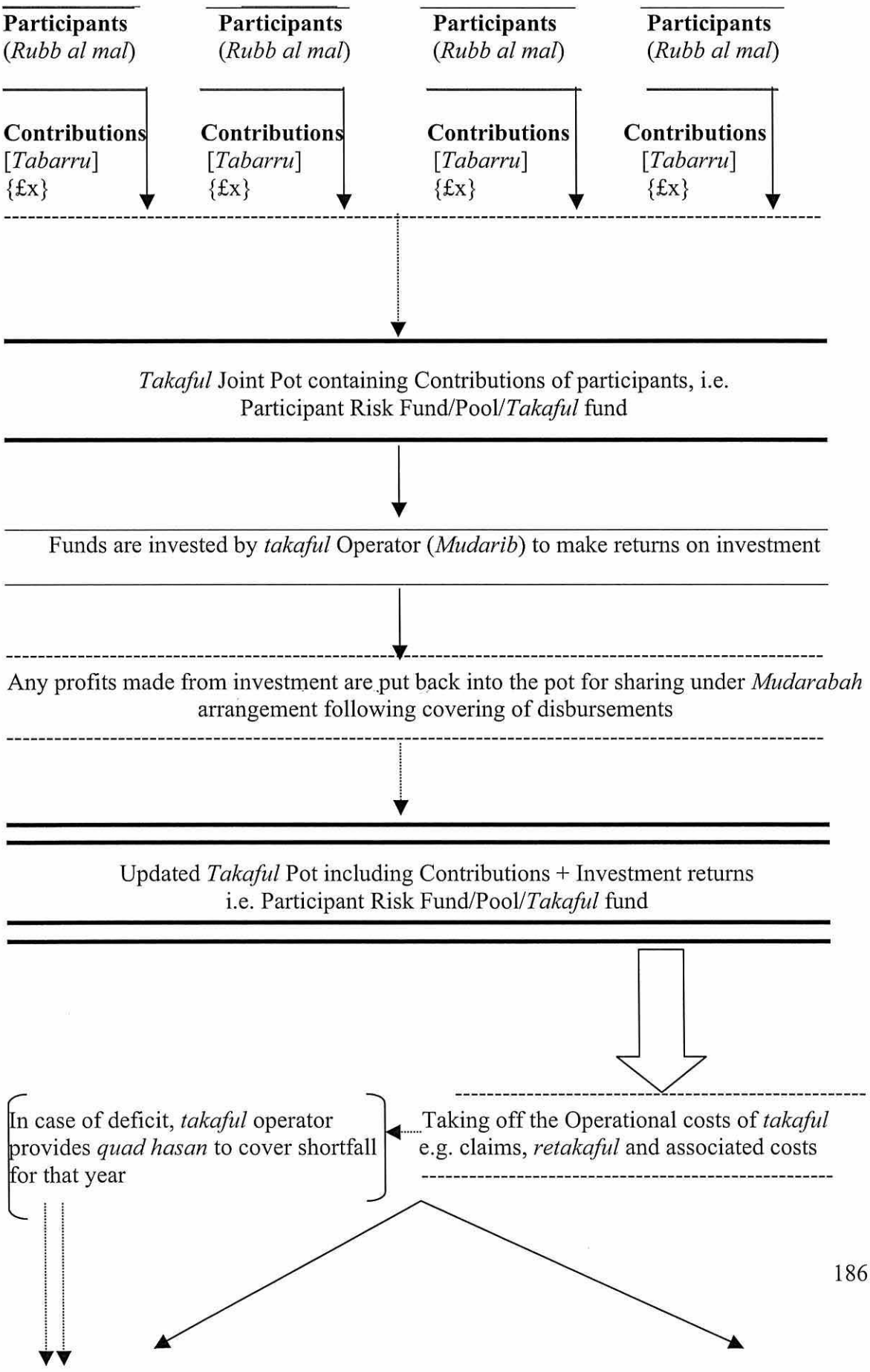
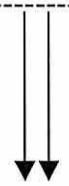


Diagram 6.2: Existing General *Mudarabah* based *Takaful* model illustration:



Takaful operator uses funds they obtained from the *Mudarabah* agreement for payment of running *takaful* expenses, e.g. tax, management expenses and other associated costs



Remainder of the fund now finds it way to the shareholders as profit in the venture

Participants take remaining % of the surplus of this venture under agreed *Mudarabah* arrangement

Diagram 6.3: *Wakala* arrangement:

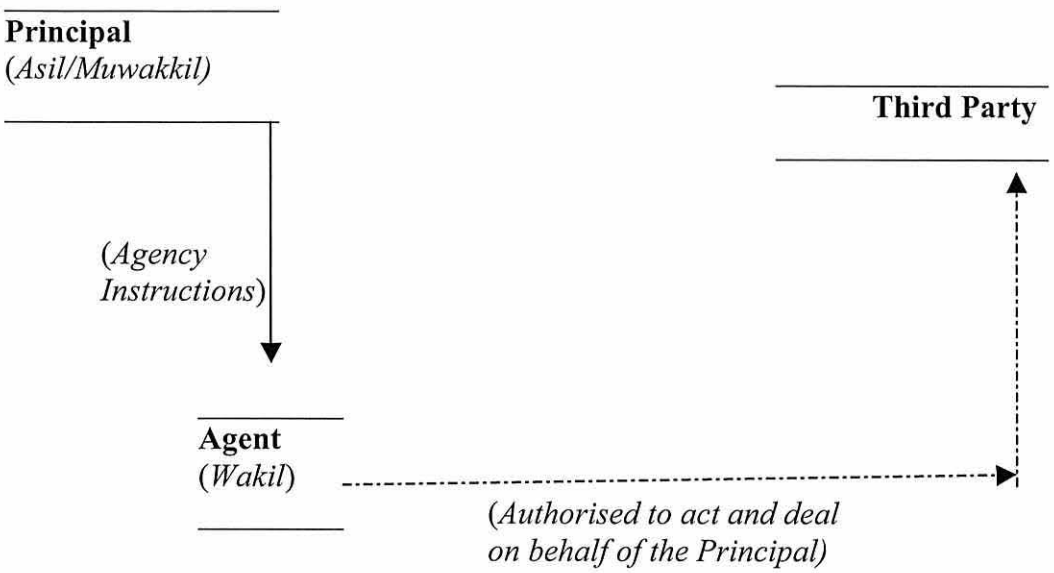
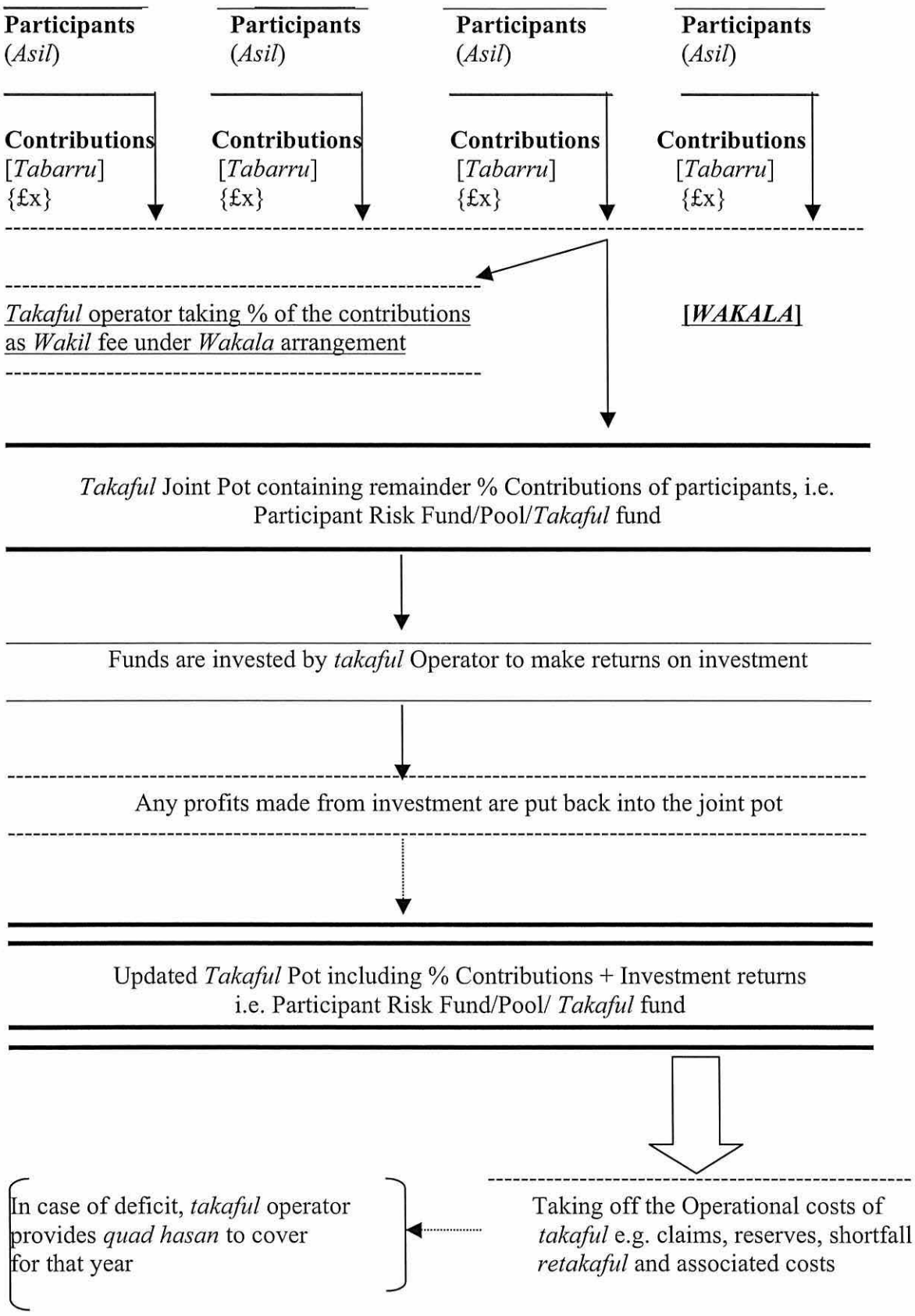


Diagram 6.4: Existing *Wakala* based *Takaful* model illustration:



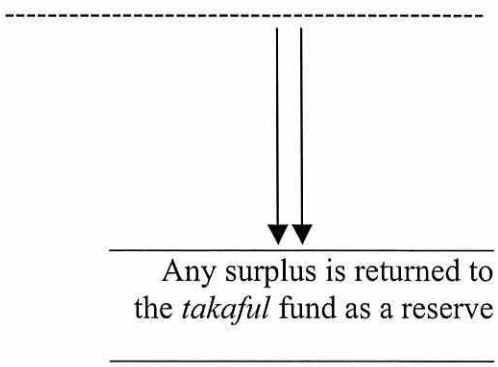
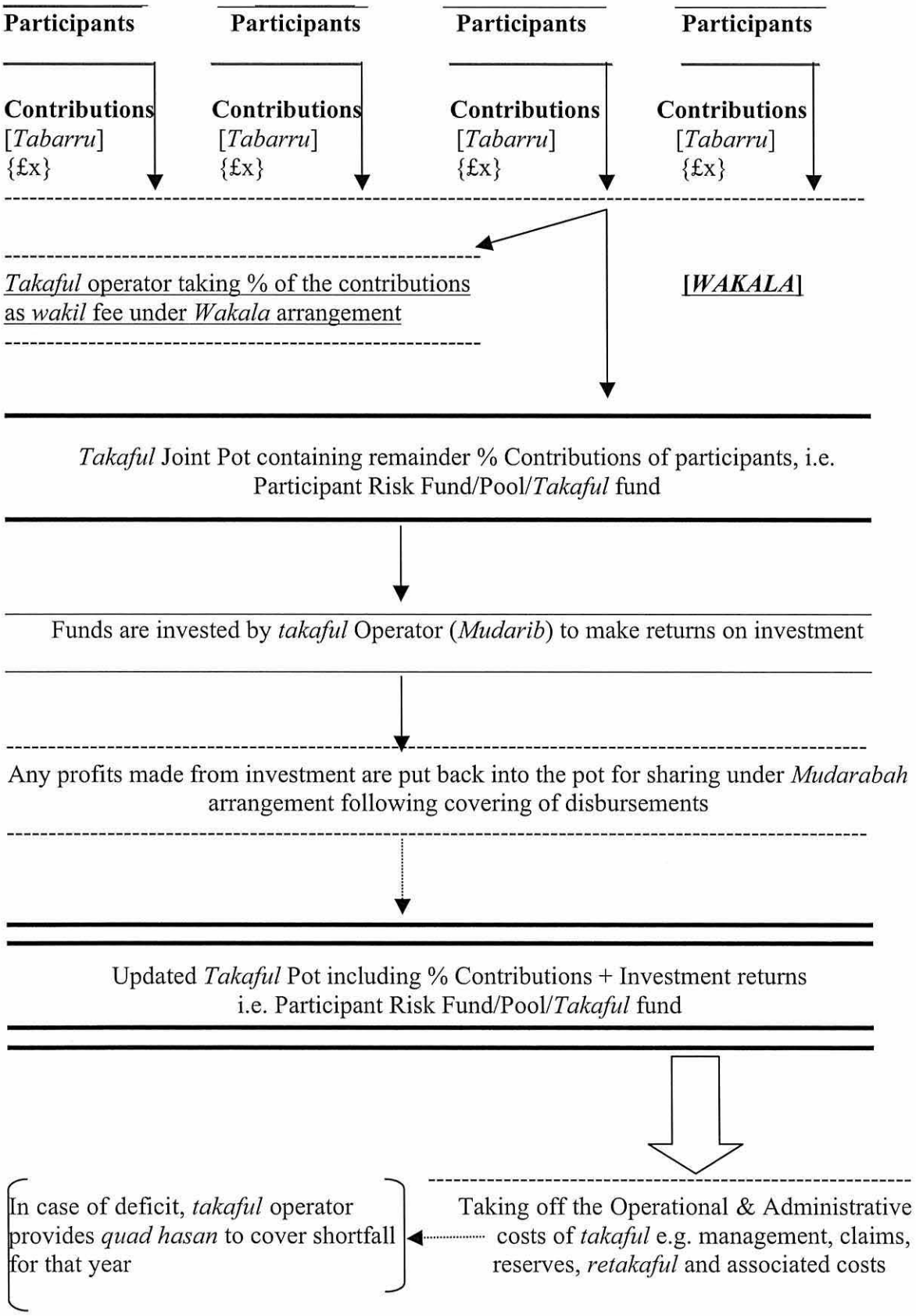

Any surplus is returned to
the *takaful* fund as a reserve

Diagram 6.5: Existing Hybrid *Wakala* and *Mudarabah* based *Takaful* model illustration:



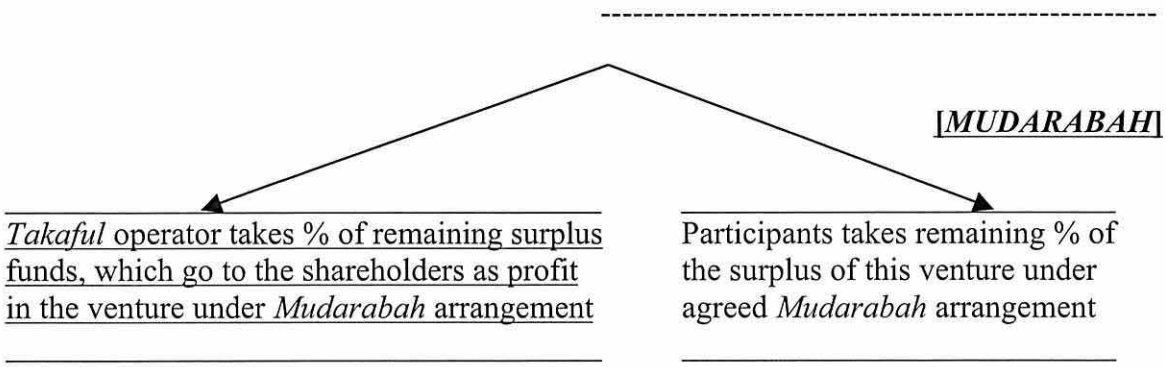
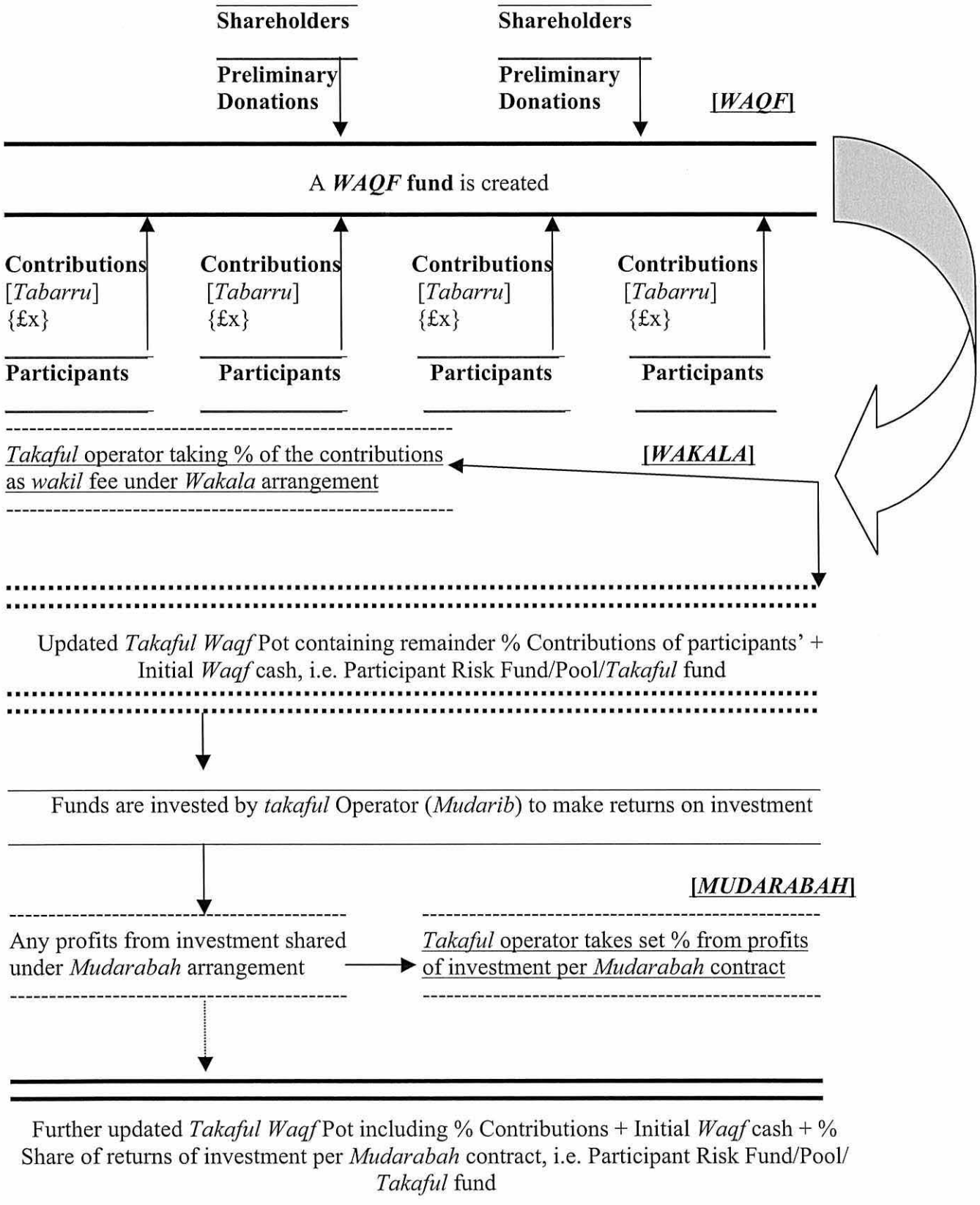
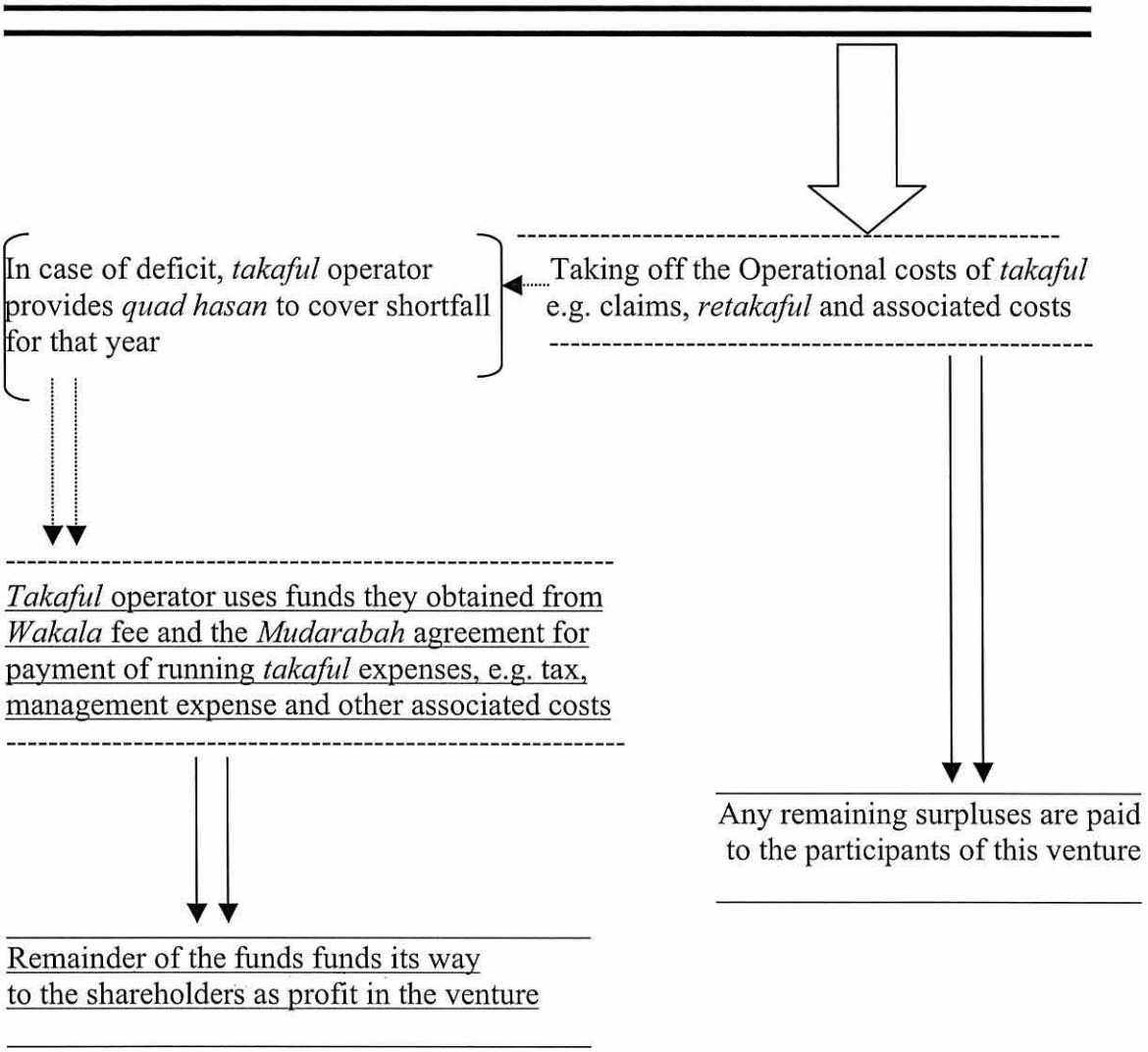

[MUDARABAH]
Takaful operator takes % of remaining surplus funds, which go to the shareholders as profit in the venture under Mudarabah arrangement
Participants takes remaining % of the surplus of this venture under agreed Mudarabah arrangement

Diagram 6.6: Existing Hybrid of *Waqf*, *Wakala* and *Mudarabah* based model illustration:




Taking off the Operational costs of takaful e.g. claims, retakaful and associated costs
In case of deficit, takaful operator provides quad hasan to cover shortfall for that year
Takaful operator uses funds they obtained from Wakala fee and the Mudarabah agreement for payment of running takaful expenses, e.g. tax, management expense and other associated costs
Any remaining surpluses are paid to the participants of this venture
Remainder of the funds funds its way to the shareholders as profit in the venture

Part III

The basics of Islamic Insurance

Chapter 7: Different types of relevant Islamic financial instruments

1. Introduction:

It is necessary, at this stage of the project, that a separate chapter to be dedicated to highlight a number of *Sharia* approved finance vehicles in operation. The reason for this is not just to give an understanding of the working ethics of the *halal* vehicles and setting some background understanding for what is out there, but also the thesis later deals with an independent proposed *takaful* model. Unlike Western jurisdictions, Islamic law lacks the full extent of the contract relationship due to the various restrictions such as *riba*, *gharar*, and *maisir,* since these elements prevent contracts from being *Sharia* compliant. However, this does not mean that freedom of contract between the parties is compromised; rather, a contract will be considered *halal* so long as it is within the ambits of Islamic law. In fact, this chapter aims to consider under Islamic law a number of different contracts that are considered valid and are relevant to the proposed *takaful* model, which is discussed below. It would be noticed that, save for the different Arabic headings, one would notice that the effects of these *Sharia* compliant contracts are the same as witnessed in the Western business community.

2. *Ijarah:*

2.1. Background:

Ijarah is an Islamic term that loosely means providing something in return for payment. The origin of the word *ijarah* comes from the Arabic letters of the alphabet *Alif*, *Jim* and

Ra that mean reward or compensation.[444] Under Islamic jurisdictions, the concept of *ijarah* covers two scenarios. One concept aims to cover circumstances where an asset is actually leased by the lessor for a period of time, so that the lessee may enjoy the usufruct of the asset and its properties and, in return, pays a fee for leasing, which is counted as the rent. As always with Islamic analogies, the lessor is called the "*Mujir*" and the lessee is called the "*mustajir*", while the fee paid in consideration as rent is called *"ujrah"*.[445]

In a separate circumstance, the concept of *ijarah* also refers to situations of service activities such as employment contracts, where individuals with specific skills are hired. This would include circumstances where there is an employer and employee relationship in employment, or even contractor situations where individuals such as doctors, lawyers or even labourers, who are hired to do a specific task, for which the consideration is given by money. In these circumstances, the person giving the task, i.e. employer or instructing party, is called the "*mustajir*" and the person who is using his skill, i.e. employee or the contractor, is called the "*ajir*" and the remuneration paid in consideration is called the *"ujrah"*.[446]

In relation to this thesis, as it would be clear in the later chapters, the concept that is more relevant is the second type of *ijarah* mentioned above. However, the first type has significance as well, when the proposals are viewed from an alternative perspective, hence the need to talk about both concepts. However, before embarking on a consideration of the different types of *ijarah,* it is necessary to consider the common relevant points of *ijarah* as mentioned by scholars,[447] which are as follows:

i. In any *ijarah* contract, the principal aim is for the separation of some sort of benefit, which is certain and specific.

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[444] Justice (r) Dr. Munir Ahmad Mughal, 'What is Ijarah' pp. – 1 - 7 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 29 August 2013

[445] Justice Mufti Muhammad Taqi Usmani, *An introduction to Islamic Finance* (1st edn, Maktaba Ma'ariful Quran 2007) p. - 158

[446] Justice Mufti Muhammad Taqi Usmani, supra at p. - 157

[447] Justice (r) Dr. Munir Ahmad Mughal, supra at pp. - 9 - 16 and 32 – 35 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 22 August 2013

ii. The benefit is a *Sharia* compliant contract, as such *halal* gains that are derived under the *ijarah* contract.[448]

iii. The amount of payment must be specifically mentioned in the *ijarah* contract.

iv. The length of the contractual relationship must be mentioned in the *ijarah* contract.

v. In the *ijarah* contract, the relationship between the giving party and the receiving party is that of belief. The latter is considered to be in a position of trust for the former, as such could be liable for claims of negligence if it fails to exercise an adequate duty of care.

vi. An *ijarah* contract cannot be broken unless there has been misrepresentation, fraud or mutual consent.[449]

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[448] As under Islamic law, there are different activities that are considered to be *haram*, such as if there are any connections to do with alcohol, gambling, pornography, swine. In those cases, the contract would immediately consider as *haram*. As it has been mentioned very clearly on the Holy Quran in *Surah Al-Araf* (Chapter 7), Verse 33 that:

- "*Say, "My Lord has only forbidden immoralities - what is apparent of them and what is concealed - and sin, and oppression without right, and that you associate with Allah that for which He has not sent down authority, and that you say about Allah that which you do not know.'*"

Holy *Quran*, (quran.com) <http://quran.com/7> accessed 30 August 2013

Additionally, as mentioned in the previous chapters, restrictions on the Holy Quran in *Surah Al – Ma'idah* (Chapter 5), Verses 90 and 91 it is stated that:

- "*O you who have believed, indeed, intoxicants, gambling, [sacrificing on] stone alters [to other than Allah], and divining arrows are but defilement from the work of Satan, so avoid it that you may be successful.*
- *Satan only wants to cause between you animosity and hatred through intoxicants and gambling and to avert you from the remembrance of Allah and from prayer. So will you not desist?*"

Holy *Quran*, (quran.com) <http://quran.com/5> accessed 30 August 2013

[449] Justice (r) Dr. Munir Ahmad Mughal, supra at pp. - 61 - 68 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 30 August 2013

2.2. Leasing related *ijarah*:

2.2.1. The Concept:

This type of *ijarah* is prevalent in the economic industry as it is used for investment purposes in the Islamic sector. As mentioned above, in this type of *ijarah* relationship, the lessor leases the assets to the lessee in return for an agreed amount, as a rent. The Arabic word for this type of *ijarah* is called *Ijaratul-Ashya.*[450] Justice Usmani compares this type of *ijarah* to a sale of goods in that consideration is being provided, save for the fact that, in the former, the title remains with the original owner and only transfers the right of use. However, he further argues that such *ijarah* are not initially aimed to be used as finance models, rather a normal business idea of renting.[451] A number of scholars, including Justice Usmani and Al-Kasani, went on to lay down some of the conditions that are necessary for such lease *ijarah* contracts to be valid, and which are in addition to the general points mentioned above:[452]

i. In a leasing *ijarah* contract, the subject of the lease must be specific, with clarity of the usufruct to be transferred for a specific period and for a specific amount of rent. There can be different rental amounts for different phases, but this must be made specific at the outset.

ii. The subject of the lease has to have valuable use so as to be possible to exercise the usufruct, otherwise a non-existent item usufruct cannot be valued, leading to *gharar*.

iii. The ownership of the subject of the lease must remain with the lessor and only the usufruct can be transferred; as such, anything leased which affects the

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[450] Justice (r) Dr. Munir Ahmad Mughal, supra at p. - 20
<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 30 August 2013
[451] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 158 - 159
[452] Hasanuz Zaman, (1991) in the Textbook: Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp.– 281 – 282 **Also:**
Justice Mufti Muhammad Taqi Usmani, supra at pp. – 159 - 163

ownership, e.g. food, money, which cannot be used without utilisation of ownership, cannot be part of leasing *ijarah*.

In circumstances where the parties enter a contract where ownership is affected, the transfer is no longer a transfer of mere usufruct; rather, it becomes a loan. Any rent charged in that respect is to be considered as *riba* due to the fact that the lessor is making money without actually doing anything.

iv. The lessor remains responsible for all ownership liabilities of the subject of the lease, whilst the lessee becomes liable for responsibilities for use of the subject of the lease.[453]

v. The use of the subject of the lease must adhere to the purpose mentioned in the leased contract, otherwise for normal course of use only. Any other type of use needs the lessor's prior approval.

vi. The lessee must compensate any damage to the subject of the lease by the lessee.

vii. The subject of the lease involving co-ownership should have the rent divided in terms of the co-ownership share and each co-owner can only lease their share of the subject of the lease.

viii. *Ijarah* contract is a binding irrevocable contract; as such, unilateral changes such as concluding or rental amount changes are not permissible and would make the contract void unless agreed between both parties.

[453] This can be witnessed by examples of a rental accommodation where the ownership associated liabilities of the property such as Council tax are the lessor responsibility whilst the lease related liabilities of the property such as gas bill, electricity bill, television licence are the lessee responsibility

ix. Any advance rent payment made would be counted as satisfaction of rental arrears after the due date.

x. The effective commencement date of leasing a *ijarah* contract is when the subject of the lease has been delivered to the lessee, irrespective of the lessee commencing use of it.

xi. In the event, where the subject of the lease is no longer useable, then the leasing *ijarah* contract concludes on that day, save where the loss is caused by negligence of the lessee, who would then be liable for the losses.

In addition to the above, other scholars have raised a few other points that could be of relevance for a *ijarah* leasing contract:[454]

xii. Where the leased item has two or more owners, then the rent raised from the leased item should be distributed to the owners in line with the proportionality of their shareholdings.

xiii. Along the same lines of the above point, the respective owner can own or lease his respective share and does not have automatic authority to lease for the others. It is opined that, due to the fact that the respective owner does not have delegated authority and holding over the other portions, and since he does not own the other portions, he does have the requisite title to pass on to the lessee to use of the usufruct of that portion of that item.

xiv. In the *ijara* contract, the rent payable cannot be of the genre as the leased item.[455] It is believed that the aim is to avoid arguments of *riba* and money is to be used as a medium of finance to assist and avoid any circumstances of inequality in exchange.

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[454] Justice (r) Dr. Munir Ahmad Mughal, supra at p. - 28 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 31 August 2013

[455] The condition is peculiar to the Hanifi school of thought.

A number of scholars have argued that *ijarah* by its nature was not considered to be a mode of finance, like sales; rather, it was supposed to be a straightforward renting, where usufruct of an asset is provided for a specific period in return of specific consideration. There are a number of issues, which are argued by scholars as being the differentiating factor for *ijarah* from being used as modes of finance. There are a number of traits of *ijarah* that are relevant as further requirements for *ijarah* contract, which are as follows:

i. With a leasing *ijarah* contract, it is permissible to have a future date when the contract will be effective, upon delivery of the subject of the lease for a specific rent. As one would note under *Sharia*, as discussed in previous chapters, it is not permissible with a sale transaction to have a forward sale and it should be effective immediately.[456]

ii. In situations where the lessee is asked to make the purchase of the subject of the lease on behalf of the lessor, the lessee initially acts as an agent for the principal and then the leasing relationship starts when the delivery of the subject of lease, is taken by the lessee. In such circumstances, the lessee's obligation commences only on a future date and not instantly, as is the case with a sale transaction under *Sharia*. Also, the subject of the lease remains at the risk of the lessor, being the owner, at all times even though only the usufruct has been transferred. This allows the lessor to charge the lessee, whilst under a *Sharia* sale transaction, this would not be possible as the lessee would have been the only one taking the risk from taking the delivery point onwards.[457]

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[456] *Sharia* doesn't allow forward sale to take place as it falls under the restrictions of *gharar* and *maisir* i.e. uncertainty and speculation. However, this is save a few exceptions such as *salaam* and *istisna*. *Salaam* is considered below, as it is one of the concepts, which is relevant to this thesis in understanding the arguments and proposed model of the researcher.
Justice Mufti Muhammad Taqi Usmani, supra at pp. – 163 - 165

[457] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 165 - 167

iii. Similarly, the lessor remains liable for all ownership-related expenses for the subject of the lease at all times, while the lessee remains liable for any damages caused to the subject of the lease.[458]

iv. Additionally, having in possession for use of the usufruct of the leased item any damage to the item either through exploitation or due to wear & tear, the lessee remains responsible for that up to the point of his control.[459]

v. Fixing of rental for a certain period of time at certain rates is acceptable under *Sharia* and, after the expiry of the period, the parties can negotiate new terms for extending the *ijara* contract period. The rental can be benchmarked against known economic variables such as the rate of inflation or amount of tax rate changes. There appear to be disagreements between scholars whether tying up the rental rates to interest rates such as LIBOR is *Sharia* compliant. Authors such as Justice Usmani mentioned that this contradicts Islamic principles as contracts are made akin to interest-based aspects and rate of interest fluctuation is unknown, leading to *gharar*.[460] However, Hasanuz Zaman argues that simply benchmarking does not make the contract *haram* as long as the basic principles of the *ijarah* contract are *Sharia* compliant, while limiting any fluctuation of rates should avoid situations of *gharar*.[461]

vi. In the event of a late payment of the rent by the lessee, the lessor has the opportunity to penalise the lessee for the delay. However, under *Sharia* the lessor is not allowed to benefit and take the penalty on top of the rent as this would amount to *riba*; therefore, the penalty should be stipulated and paid to a charity instead.[462]

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[458] Justice Mufti Muhammad Taqi Usmani, supra at p. – 167
[459] Ibid.
[460] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 167 - 171
[461] Hasanuz Zaman, supra at pp. – 283 – 284
[462] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 171 - 173

Therefore, in consideration of the above points, it can be safely argued that a *ijarah* leasing contract is not a sale contract, hence the restrictions related to sale transactions should not be applicable to a *ijarah* leasing contract. Own view is that the *ijarah* contract in such a case is different as the movement is temporary, with certainty that the title remains with the original owner at all times and any temporary assignment is not on the title but on the resources, which are to return to the original owner.

2.2.2. Religious laws:

There are a number of *hadiths* that deal with the concept of leasing *ijarah* and on providing of rent in return for the leased item. This has been the practice of sharing and is mentioned in Book 10, Hadith 3729 of Sahih Muslim that:

- "*Abu Huraira (Allah be pleased with him) reported Allah's Messenger (may peace be upon him) as saying: He who has land should cultivate it or lend it to his brother, but if he refuses, he should retain his land.*"[463]

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[463] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=010&translator=2&start=118&number=3725> accessed 31 August 2013

There are other *hadiths* which confirms that the Prophet had restricted Muslims lending of land for rent and this can be witnessed from Book 10, Hadith 3742 of Sahih Muslim that:

> "*Rafi b. Khadij (Allah be pleased with him) reported: We used to give on rent land during the lifetime of Allah's Messenger (may peace be upon him). We rented it on the share of one-third or one-fourth of the (produce) along with a definite quantity of corn. One day a person from among my uncles came to us and said: Allah's Messenger (may peace be upon him) forbade us this act which was a source of benefit to us, but the obedience to Allah and to His Messenger (may peace be upon him) is more beneficial to us. He forbade us that we should rent land with one-third or one-fourth of (the produce) and the corn of a measure, and he commanded the owner of land that he should cultivate it or let it be cultivated by other (persons) but he showed disapproval of renting it or anything besides it.*"

Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=010&translator=2&start=127&number=3734> accessed 31 August 2013

However, it is necessary to note that during those times, the renting, as is evident from the *hadith* the rent payment was in the form of barter transaction as taking portions of produce. Such barter transactions are not allowed in Islam for *ijarah* contracts as can be noted from one of the requirements above. As money was not used a medium hence the reason for the Prophet's objection to that, which supports analogy that otherwise there are concerns of presence of *riba*. However, the Prophet had no objections when money was used as a medium as can be note from from Book 10, Hadith 3748 of Sahih Muslim that:

> "*Hanzala b. Qais al-Ansri reported: I asked Rafi' b. Khadij about the renting of land for gold and silver, whereupon he said: There is no harm in it for the people let out land situated near canals and at the ends of the streamlets or portion of fields. (But it so happened) that at times this was destroyed and*

Additionally, sharing of the outcome of the asset in satisfaction for the return of the asset has been mentioned in the *hadith*, confirming that the arrangements are acceptable in Islam. This is mentioned in Book 10, Hadith 3763 of Sahih Muslim that:

- *"Ibn Umar reported that 'Umar b. al-Khattab (Allah be pleased with him) expelled the Jews and Christians from the land of Hijaz, and that when Allah's Messenger (may peace be upon him) conquered Khaibar he made up his mind to expel the Jews from it (the territory of Khaibar) because, when that land was conquered, it came under the sway of Allah, that of His Messenger (may peace be upon him) and that of the Muslims. The Jews asked Allah's Messenger (may peace be upon him) to let them continue there on the condition that they would work on it, and would get in turn half of the fruit (of the trees), whereupon Allah's Messenger (may peace be upon him) said: We would let you continue there so long as we will desire. So they continued (to cultivate the lands) till 'Umar externed them to Taima' ang Ariha (two villages in Arabia, but out of Hijaz)."*[464]

As is quite apparent from the *hadiths* above, the Islamic laws have no objections with lending and making a return on items, so long as the conditions to distance from *riba*, *gharar* and *maisir* are maintained.

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that was saved. whereas (on other occasions) this portion was saved and the other was destroyed and thus no rent was payable to the people (who let out lands) but for this one (which was saved). It was due to this that he (the Holy Prophet) prohibited it. But if there is something definite and reliable (e. g. money) there is no harm in it."
Search Truth, '*Hadith* online' (searchtruth.com)
<http://www.searchtruth.com/book_display.php?book=010&translator=2&start=136&number=3743>
accessed 31 August 2013

[464] Search Truth, '*Hadith* online' (searchtruth.com)
<http://www.searchtruth.com/book_display.php?book=010&translator=2&start=154&number=3761>
accessed 31 August 2013

2.3. Wage related *ijarah*:

2.3.1. The Concept

As mentioned above, *ijarah* has been divided to cover both the rental of items and hiring of services. The Arabic word for this type of *ijarah* is called *Ijaratul-Ashkhas.*[465] Entering into a *ijarah* contract is not a complicated arrangement. The matter is quite straightforward in that the employer, who is the *mustajir,* hires the individual, *ajir,* for his skill. The *ajir* is to conduct the work assigned by the *mustajir* and, upon completion of the work, as a reward for his services, he is paid his remuneration, the *ujrah.* The principles of such a relationship are embodied in the texts of the religious laws as discussed below.

2.3.2. Requirements:

As with any *Sharia* compliant vehicle, there are a number of conditions that have to be met as a bare minimum. As will be noticed while perusing this thesis, whenever there are discussions about *Sharia* requirements, there is a silent but powerful message calling out for equality of all the parties in the contract. This really should not come as a surprise, as *Sharia* rules are set according to God's principles and the Prophet strived very hard to set the message clear. As mentioned above, the religious law stands firm on the payment of the *ajir's* wages and, in time, the requirements are as follows~~,~~ which, once more, ~~are~~ to be considered in addition to the common points mentioned earlier:

i. The job that the worker is to conduct must be specifically well-defined.[466]

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[465] Justice (r) Dr. Munir Ahmad Mughal, supra at pp. – 20 - 21
<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 30 August 2013
[466] Justice (r) Dr. Munir Ahmad Mughal, supra at p. – 29
<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 3 August 2013

ii. The work to which the *ajir* is contracted must not be something that is prohibited in *Sharia* and, as such, *haram* e.g. magic tricks, alcohol promotions.[467]

iii. The service for which the *ajir* is being instructed to do is not something that is already mandatory under the *Sharia* rules, e.g. attempting to pay someone to do the daily prayers of someone else, or do the *Hajj* (pilgrimage) for someone else, which are obligations that a person must do himself/herself.[468]

iv. The payment of remuneration to the *ajir* should be unconnected to external aspects, as from the return produced of the manufactured item or from the income generated from renting that item, if such are included.[469]

v. It is important to note that such *ijarah* contracts are bilateral contracts and cannot be terminated unilaterally.[470]

vi. Where the *ajir* is being trusted to do the work by the *mustaijir*, any goods provided to the *ajir* by the latter are held to remain in trust in the custody of the former and should there be any damage caused to the said goods, the *ajir* will be held responsible for that irrespective of how the damage took place.[471]

Whilst the requirements mentioned above are certainly the basics for a wage-related *ijarah* contract, it is necessary to note that, if the *mustajir* states the remuneration to be paid to the *ajir* for the work to be done, or even if the *ajir* proposes an amount which is agreed by the *mustajir*, both are acceptable under the *Sharia*.[472] However, the

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[467] Ibid
[468] Justice (r) Dr. Munir Ahmad Mughal, supra at pp. – 30 - 31 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 30 August 2013
[469] Ibid
[470] Justice (r) Dr. Munir Ahmad Mughal, supra at p. – 34 <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 30 August 2013
[471] Justice (r) Dr. Munir Ahmad Mughal, supra at p. – 35 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 30 August 2013
[472] Justice (r) Dr. Munir Ahmad Mughal, supra at pp. – 46 - 50 http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2017140> accessed 31 August 2013

remuneration and the work details, such as description, length of service, etc., are factors that must be made clear on the outset for a valid wages-related *ijarah* contract.

2.3.3. Religious laws:

It is relevant to justify the Islamic backing of the applicability of a *ijarah* contract for Muslims. The use of *ijarah* contracts is supported by both the Holy Quran and the *hadith*. There are strict rulings in *Sharia* about the payment for services of a person and his wages. In the Holy Quran in *Surah Al-Qasas* (Chapter 28), Verses 25 and 26 deal with the narrative of Prophet Moses, where the payment from the work was to be set-off against the outstanding marriage dowry and it is mentioned that:

- "*Then one of the two women came to him walking with shyness. She said, 'Indeed, my father invites you that he may reward you for having watered for us.' So when he came to him and related to him the story, he said, 'Fear not. You have escaped from the wrongdoing people.*"

- "*One of the women said, 'O my father, hire him. Indeed, the best one you can hire is the strong and the trustworthy.*"[473]

Also, in the *hadith* the whole of Book 23 named Wages (Kitab Al-Ijarah) of Sunan Abu-Dawud is considered wholly on the concept of payment of wages. One of the relevant sections is in Book 23, Hadiths 3501 and 3502 of Sunan Abu-Dawud as narrated by Aisha, Ummul Mu'minin that:

- "*The Apostle of Allah (peace_be_upon_him) said: Profit follows responsibility.*"[474]

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[473] Holy *Quran*, (quran.com) <http://quran.com/28> accessed 31 August 2013
[474] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=23&translator=3&start=37&number=3499>; accessed 30 August 2013

- "*Makhlad ibn Khufaf al-Ghifari said: I and some people were partners in a slave. I employed him on some work in the absence of one of the partners. He got earnings for me. He disputed me and the case of his claim to his share in the earnings to a judge, who ordered me to return the earnings (i.e. his share) to him. I then came to Urwah ibn az-Zubayr, and related the matter to him. Urwah then came to him and narrated to him a tradition from the Apostle of Allah (peace_be_upon_him) on the authority of Aisha: Profit follows responsibility.*"[475]

A simpler way of looking at this is that the *ajir* took responsibility of the work that he has been instructed to conduct and thus he is entitled to the profits as promised, i.e. the wages. In other *hadiths,* which have been considered by *Sharia* scholars as being authentic, it is narrated by Abdullaah ibn Umar that the Prophet said: *"Pay the laborer his wages before his sweat dries."*[476] Also, it has been narrated by Abu Sa'eed Al-Khudri that, the Prophet, said: *"Whoever employs someone to work for him, he must specify for him his wage in advance."* [*Musannaf 'Abdur-Razzaaq*][477]

Additionally, it is narrated by Abu Huraira in Book 34, Hadith 430 of Sahih Bukhari that:

- *"The Prophet said, "Allah says, 'I will be against three persons on the Day of Resurrection: 1. One who makes a covenant in My Name, but he proves treacherous. 2. One who sells a free person (as a slave) and eats the price. 3. And one who employs a laborer and gets the full work done by him but does not pay him his wages."'"*[478]

The circumstances of the payment of one's wages in *Sharia* are more stringent when the wages have, for some reason, been missed. Not only is the *mustajir* under a duty to make the payment to the *ajir* promptly, but the *mustajir* is to act as a trustee of the

[475] Ibid
[476] Masjidma, 'Pay the Laborer his Wages Before his Sweat Dries' (2012 masjidma.com) <http://masjidma.com/2012/09/03/the-employer-employee-relationship/> accessed 30 August 2013
[477] Ibid
[478] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=wage&translator=1&search=1&book=&start=0&records_display=10&search_word=all> accessed 29 August 2013

remuneration, and all consequential proceeds from that belongs to the *ajir*. This has been mentioned nicely in the *hadith,* which relates to a narrative mentioned by the Prophet of three men stuck in a cave and were asking for God's mercy to get them out. In this, one of the narratives related to a man who failed to pay the wages of the *ajir*. It is mentioned in Book 36, Hadith 472 of Sahih Bukhari, narrated by Abdullah bin 'Umar that:

- *"...The Prophet added, "Then the third man said, 'O Allah! I employed few laborers and I paid them their wages with the exception of one man who did not take his wages and went away. I invested his wages and I got much property thereby. (Then after some time) he came and said to me: O Allah's slave! Pay me my wages. I said to him: All the camels, cows, sheep and slaves you see, are yours. He said: O Allah's slave! Don't mock at me. I said: I am not mocking at you. So, he took all the herd and drove them away and left nothing...."*[479]

Finally, it is a strong *Sunnah* for Islamic finance vehicles to consider that the payments of remuneration are strict where they have been contracted between the parties. It is mentioned in Book 36, Hadith 478 to 480 of Sahih Bukhari, narrated by Ibn 'Abbas that:

- *"When the Prophet was cupped, he paid the man who cupped him his wages."*[480]

- *"When the Prophet was cupped, he paid the man who cupped him his wages. If it had been undesirable he would not have paid him."*[481]

- *"Narrated Anas: The Prophet used to get cupped and would never withhold the wages of any person."*[482]

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[479] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=wage&translator=1&search=1&book=&start=0&records_display=10&search_word=all> accessed 30 August 2013

[480] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=wage&book=&translator=1&search=1&search_word=all&start=10&records_display=10> accessed 30 August 2013
Cupping was a medical procedure that was prevalent in the earlier times when the affected area of the human body would have a cup placed to get the bad blood out of there. This is still used in modern times although not so common.

[481] Ibid

3. *Bai Salaam:*

3.1. The Concept:

Bai Salaam originated from the Arabic words "*Bai'un*" ("purchase and sale") and "*Salamun*" ("advance").[483] *Salaam* is considered to be a special type of exceptional sale transaction that is allowed in the *Sharia* where, unlike other sale transactions, the sale object need not be present at the time of sale. It is a forward selling transaction, where the buyer makes the payment for the goods in advance at the time of the contract and the seller has the advantage of being able to provide the goods at a future date. In such circumstances, payment and delivery are not concurrent and, as mentioned, are exceptions that have been allowed, as generally *gharar* and *maisir* restrictions (explained in previous chapters) confine the trading of future dealings. However, under the Islamic law, a number of strict requirements have been set for a *Salaam* contract to come into existence, which are discussed below.

Generally, in a *Salaam* contract, the buyer is known as "*rabb-us-salam*", the seller is called "*muslam ilaih*", the purchase price is called "*ra's-ul-mal*" and the subject matter of the sale is called "*muslam fih*".[484] Of course, this kind of transaction has its advantages as the seller receives his remuneration immediately, whilst the buyer remains in a strong bargaining position to be able to negotiate a lower price, as opposed to a spot rate price.

3.2. Religious laws:

As mentioned earlier, *Salaam* is a special type of sale contract that falls under the exception of the type of sales that are allowed in Islam. The history recalls the time when Prophet Mohammed (pbuh) migrated from Makkah to Medina in Saudi Arabia and came

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[482] Ibid
[483] Islami Bank Bangladesh, '*Bai Salaam*' (islamibankbd.com) <http://www.islamibankbd.com/prodServices/prodServBaiSalam.php> accessed 25 June 2014
[484] Justice Mufti Muhammad Taqi Usmani, supra at p. – 186

across a tradition followed by the inhabitants there, where they paid in advance for fruits that would be delivered to them in the next one to three years. The Prophet Mohammed (pbuh) allowed these types of sales to continue but with requirements that the items' attributes and delivery date were to be defined. This can be expressed nicely in the *hadiths* of the Prophet, mainly under Book 35 of Sahih Bukhari entitled "Sales in which a Price is paid for Goods to be Delivered Later (As-Salam)". The relevant *hadiths,* as in Book 35, Hadith 443 of Sahih Bukhari as narrated Ibn Abbas state that:

- "*The Prophet came to Medina and the people used to pay in advance the price of dates to be delivered within two or three years. He said (to them), "Whoever pays in advance the price of a thing to be delivered later should pay it for a specified measure at specified weight for a specified period.*"[485]

Similarly, in Book 35, Hadith 446 of Sahih Bukhari as narrated Shu'ba that:

- "*Muhammad or 'Abdullah bin Abu Al-Mujalid said, "Abdullah bin Shaddad and Abu Burda differed regarding As-Salam, so they sent me to Ibn Abi Aufa and I asked him about it. He replied, 'In the life-time of Allah's Apostle, Abu Bakr and 'Umar, we used to pay in advance the prices of wheat, barley, dried grapes and dates to be delivered later. I also asked Ibn Abza and he, too, replied as above.'"*[486]

Also, this has been nicely set out in Book 23, Hadith 3459 of Sunan Abudawud, where it has been narrated by Abdullah ibn AbuAwfa ibn AbuAwfa al-Aslami that:

- "*...We made a journey to Syria on an expedition along with the Apostle of Allah (peace_be_upon_him). The Nabateans of Syria came to us and we paid in*

[485] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=35&translator=1> accessed 31 August 2013
[486] Ibid

advance to them (in a salam contract) in wheat and olive oil at a specified rate and for a specified time..."[487]

Some authors such as Hasanuz Zaman have viewed this as a necessary type of exceptional sale to assist the farmers and orchid owners to continue businesses. Following the Prophet's quest of spreading Islam, traditional loans that had *riba* in them were no longer allowed and the farmers needed funds in the meantime to enable them to grow crops and feed their families until the harvest. Hence, this was an exception that has been allowed.[488] This thesis agrees with other scholars in this respect, as it assists the seller with his capital investment by having a liquid capital, which is needed to enable the project to lift off in the first instance.

3.3. Requirements:

In any given sale, the *Sharia* is strict in regards to the transaction, such as the item for sale must be in the seller's possession, be it physical possession or constructive possession, and mere ownership is inadequate. Also, the subject matter must be present at the time of sale and not something non-existent, irrespective of the time limit when this will come into existence. Additionally, the seller must have the ownership of the subject matter of the sale, as he needs to have the required authority to pass this on to the buyer. This can be seen as analogous to the English sale contract where, without ownership, the seller does not have the requisite to pass on the item to the buyer and, for the buyer to acquire it, there must be a good title on the sale item otherwise this would lead to a nullified sale. However, a *Salaam* contract is an exception. One can state a number of basic rigid conditions that have to been set, which are as follows:

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[487] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=23&translator=3&start=19&number=3451> accessed 28 August 2013

[488] Hasanuz Zaman, supra at pp. - 443 – 444;
Muhammad Ayub, supra at pp. – 241 – 242;
Justice Mufti Muhammad Taqi Usmani, supra at p. – 186

i. At the time of the transaction, the purchaser is obliged to pay the full amount to the seller. It is a condition precedent of the *Salaam* contract, as otherwise deferral of the payment would amount to dealing with debts against debt, from both the buyer and the seller, which would lead to a different type of complication as there are significant issues about debt with debt payments due to the presence of *riba* and *gharar.* Also, the main idea behind a *Salaam* contract is that the seller receives the payment in advance of delivery, otherwise the vehicle wouldn't make sense.[489]

ii. Whilst entering into a *Salaam* contract, the agreement must be on specific goods on which quality and quantity can be precisely ascertained. Where quality and quantity cannot be determined, then there cannot be a *Salaam* contract.[490] It is felt that the rationale behind this is to avoid as much uncertainty in the contractual obligations as possible. Already, the purchaser is taking a risk to an extent by departing with his money in advance; additional risk factors of vagueness of the items would add no benefit to the contractual obligations.

iii. When entering into a *Salaam* contract, the seller cannot be obliged to provide the item of sale from a specific origin, such as a specific field or farm. This is because, whether the specified origin would provide the outcome is outside the control of the seller. The condition may appear archaic but, as mentioned above, one needs to bear in mind the era when these provisions were made. The idea behind this restriction is that the seller is unable to confirm with certainty the harvest or outcome from the specific field or farm to meet the purchaser's demands.[491] It is opined that the seller agreeing to such conditions would, undoubtedly, be acting outside his scope; but also, setting the obligations of the parties is an uncertainty as he himself simply doesn't know of the responsibilities he is promising.

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[489] Justice Mufti Muhammad Taqi Usmani, supra at p. – 187
[490] Ibid
[491] Justice Mufti Muhammad Taqi Usmani, supra at p. – 188

iv. It is necessary as part of the *Salaam* contract that the quality of the item of sale be disclosed to the purchaser in full without any vagueness.[492] Once more, the concept is to avoid uncertainty. A different way of looking at it is that a *Salaam* contract requires full and frank disclosure on the item, with a high threshold of disclosure built into the *Salaam* contract.

v. Additionally, in a *Salaam* contract, the quantity of the sale item must be clearly expressed, may it be in terms of weight or in volumes, as may be the case with the sale practice of that item.[493]

vi. The specific delivery date and place of delivery must be clearly mentioned in the *Salaam* contract.[494] This is similar to English marine law contracts such as CIF contracts, where it is a requirement for the party delivering to ensure that the date and place are specific to their contract.

vii. A S*alaam* contract is inapplicable where spot exchange/delivery is an essence to the contract. Along the same lines, a *Salaam* contract cannot be used for barter transaction as instant delivery of items becomes crucial to the contract.[495]

viii. A *Salaam* contract is inapplicable for use on the sale of items, the value of which changes on subjective assessment.[496]

Provided that the following conditions are met, a *Salaam* contract can be used as a method of financing. The parties are free to negotiate the price of sale, but the buyer would be in a strong bargaining position due to the availability of funds in advance. In the *Salaam* contract, as goods are to be provided at a later date by the seller, the buyer has

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[492] Ibid
[493] Ibid
[494] Ibid
[495] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 188 - 189
[496] Hasanuz Zaman, supra at pp. - 255 – 256

the advantage of asking the seller to furnish him with some sort of security on the value. This security can be either a guarantee or mortgage, or providing a pledge of an asset similar to secured debt. The aim is to win the buyer's confidence so that, in case of default by the seller, the buyer would still have avenues for reimbursement.

Justice Usmani gave his view that this becomes a hassle for the financial organisations to deal with different commodities from different clients as security. Also, the financial organisations are unable to sell these securities until they have been delivered, as otherwise it would end up being a sale of debt, which has severe limitations under *Sharia.* However, he goes on to state that it is necessary for Islamic finance models to consider commodities in their diagrams, as making money out of money without doing anything, such as advancing loans, is not allowed in Islam.[497] This thesis agrees with the views of Justice Usmani in that simply dealing with commodities should not be a major factor hindering the integration to modern commercial advancements. Commodities in *Salaam* contracts are valuable assets that have been used as security to replenish risks. Making money out of money without doing anything is not only *haram* but also has its limits.

3.4. Securitisation in a *Salaam* contract

As in a *Salaam* contract, the buyer is parting with his funds before he is in receipt of the goods, therefore it is of no surprise that he should ask for some type of security. This is more relevant if the proposed sale is the first transaction between the parties. In such circumstances, it is allowed in the *Sharia* that the seller furnishes the buyer with some kind of collateral as a sign of assurance to the buyer that he would be willing to keep his obligations. This is expressed nicely in the *hadiths* of the Prophet in Book 35 Hadith 453 of Sahih Bukhari, which deals with security in a *Salaam* contract that:

[497] Justice Mufti Muhammad Taqi Usmani, supra at p. – 192

- *"Narrated 'Aisha: Allah's Apostle bought some foodstuff (barley) from a Jew on credit and mortgaged his iron armor to him (the armor stands for a guarantor)."*[498]

- *"Narrated Al-A'mash: We argued at Ibrahim's dwelling place about mortgaging in Salam. He said, "Aisha said, 'The Prophet bought some foodstuff from a Jew on credit and the payment was to be made by a definite period, and he mortgaged his iron armor to him.'"*[499]

Here, the Prophet himself had provided pledges for circumstances where he had taken funds on credit, as is the case with *Bai Salaam* contracts. In *Salaam* contracts, it is accepted that the seller provides a security, surety or pledge to the buyer as a safety measure of his responsibility. In the event of default, the buyer is entitled to recompense from the security, surety or pledge. This may involve accessing the safety measure funds or going after the surety or pledge to quantify for the loss sustained due to the actions of the seller.

3.5. Minor disagreements between schools on conditions of *Salaam* contract

It is not the intention of this thesis to go into detail regarding the various schools of thought as this may defeat the purpose of this thesis. However, it is necessary at this stage to point out some of the salient points that the different schools of thought have included as additional conditions for the utilisation of the *Salaam* contract.

The Hanafi school of thought opines that the item of *Salaam* contract be available at the time of contract until the time of delivery. It is not good enough if the item simply becomes available at the time of delivery only. However, the more popularly acceptable view, which is approved by the other three schools of thought, i.e. Shafi, Maliki and

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[498] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=35&translator=1&start=10&number=450> accessed 31 August 2013

[499] Ibid

Hanbali, does not state that it is necessary for the item to be available at the time of contract as it is not a condition precedent of the *Salaam* contract, so long the item is available at the time of delivery.[500]

Another aspect that has been a point of disagreement is the Hanafi and Hanbali schools of thought, that there must be a minimum of one month from the date of contract to the delivery date. They justified this with the idea that a *Salaam* contract is for poor farmers and they would need time to fulfil their obligations. Also, due to the price differences between a *Salaam* contract and spot rate, they ask for a month's difference. The Maliki school of thought argues that the time difference should be 15 days instead due to the rate change in markets.

However, other Hanbali jurists and the Shafi school of thought do not agree with that and the popularly acceptable view is that the Prophet did not set any time limit on delivery. The main aspect is that the date must be certain so as to avoid *gharar*, otherwise it is open to the parties to negotiate what they feel is appropriate, as per the circumstances of their contract and obligations. This approach has been accepted for modern transactions as well, as mentioned by Ashraf Ali Thanawi in Imdad-ul-Fatawa v.3.[501]

3.6. Parallel *Salaam* contract:

It would be worth mentioning a few of the advantages of a *Salaam* contract as a finance vehicle, as it would assist in understanding the anticipated model of *takaful* as proposed later on.

i. Whilst there are restrictions on selling goods without having receipt of the delivery under Islamic law, it is allowed and has been utilised by Islamic financial organisations in a *Salaam* contract to make use of a parallel *Salaam*

[500] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 189 - 190
[501] Justice Mufti Muhammad Taqi Usmani, supra at pp. – 190 - 191

to make up their mark profit, immediately on receipt of the items from the original *Salaam* contract.[502]

ii. Similarly, due to *Sharia* restrictions of selling goods which have not yet been received, the buyer of the original *Salaam* contract is allowed to enter a promissory agreement with a different party which, although unilateral and no monies have been paid, would assist the original buyer in managing his economic circumstances as the prices and customer would have been organised.[503]

There are strict *Sharia* rulings against selling an item to someone before being in receipt of it. The aim under Islamic law is, most likely, not just to have a clear conscience about the situation, but also to avoid disputes. There is a *hadith* which deals with an exact situation of a disagreement as narrated by Abdullah ibn Umar in Book 23, Hadith 3460 of Sunan Abu-Dawud that:

- "*A man paid in advance for a palm-tree. It did not bear fruit that year. They brought their case for decision to the Prophet (peace_be_upon_him). He said: for which do you make his property lawful? He then said: Do not pay in advance for a palm-tree till they (the fruits) were clearly in good condition.*"[504]

Additionally, in a more explicit *hadith* it has been narrated by AbuSa'id al-Khudri in Book 23, Hadith 3461 of Sunan Abu-Dawud that:

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[502] Justice Mufti Muhammad Taqi Usmani, supra at p. – 193
[503] Ibid
[504] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=23&translator=3&start=19&number=3451> accessed 30 August 2013

- "*The Prophet (peace_be_upon_him) said: If anyone pays in advance he must not transfer it to someone else before he receives it.*"[505]

As can be witnessed, the Prophet had made it absolutely clear not to conduct such transactions where parties are in the dark about whether they can fulfil the agreement they are making. Given that the reliance is on someone else to fulfil their part of the obligation, one can quite rightly understand the analogy behind the strict provisions of being certain of the item before entering into a further contract. Perhaps a better *hadith* in this respect with a clear warning is narrated by Hakim ibn Hizam in Book 23, Hadith 3496 of Sunan Abu-Dawud that:

- "*Hakim asked (the Prophet): Apostle of Allah, a man comes to me and wants me to sell him something which is not in my possession. Should I buy it for him from the market? He replied: Do not sell what you do not possess.*"[506]

iii. A third point, although not a viable option but necessary to be mentioned for a better understanding, is that, on the delivery date, the item of *Salaam* contract should be sold back to the seller, perhaps at a higher price to make up the mark. This option falls foul of *Sharia* regulations in two aspects: the first being that it is never allowed for an item to be sold before taking delivery of the same; second, being sold at a higher price amounts to *riba* as the increase of funds is not as a result of either party. Even if the following is done, after the delivery, the sale back cannot be prearranged with the original *Salaam* contract.[507]

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[505] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=23&translator=3&start=19&number=3451> accessed 31 August 2013

[506] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=23&translator=3&start=28&number=3472> accessed 31 August 2013

[507] Ibid

This is most likely because, if it is prearranged at the beginning, then there is no actual *Salaam* sale and it is simply *riba* occasioning under a veil. Additionally, there is a strong *hadith* from the Prophet, which prohibits two sales taking place in one sale. This has been mentioned in Book 31, Hadith 31.33.72 and Hadith 31.33.74 of Malik's Muwatta that:

- *"Yahya related to me from Malik that he had heard that the Messenger of Allah, may Allah bless him and grant him peace, forbade two sales in one sale."*[508]

- *"Yahya related to me from Malik that he had heard that al-Qasim ibn Muhammad was asked about a man who bought goods for 10 dinars cash or fifteen dinars on credit. He disapproved of that and forbade it. Malik said that if a man bought goods from a man for either 10 dinars or 15 dinars on credit, that one of the two prices was obliged on the buyer. It was not to be done because if he postponed paying the ten, it would be 15 on credit, and if he paid the ten, he would buy with it what was worth fifteen dinars on credit. Malik said that it was disapproved of for a man to buy goods from someone for either a dinar cash or for a described sheep on credit and that one of the two prices was obliged on him. It was not to be done because the Messenger of Allah, may Allah bless him and grant him peace, forbade two sales in one sale. This was part of two sales in the one sale. Malik spoke about a man saying to another, "'I will either buy these fifteen sa of ajwa dates from you, or these ten sa of sayhani dates or I will buy these fifteen sa of inferior wheat or these ten sa of Syrian wheat for a dinar, and one of them is obliged to me.' Malik said that it was disapproved of and was not halal. That was because he obliged him ten sa of sayhani, and left them and took fifteen sa of ajwa, or he was obliged fifteen sa of inferior wheat and left them and took ten sa of Syrian wheat. This was also disapproved of, and was not halal. It resembled*

[508] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/searchHadith.php?keyword=two+sales+in+one+sale&translator=4&search=1&book=&start=0&records_display=10&search_word=all> accessed 31 August 2013

what was prohibited in the way of two sales in one sale. It was also included under the prohibition against buying two for one of the same sort of food."[509]

As is quite clear from the *hadith* above, the Prophet has been strict about including two transactions in one sale. It is contended that it is not only to have transparency in the contract, so as to have conditions such as utmost good faith and full and frank disclosure to be practised adequately, but also to avoid situations of iniquitous tactics for one party to practice on another. It is necessary to note that parallel *Salaam* contracts have some obligations to comply when utilised. This does not mean that the requirements of a *Salaam* contract are inapplicable to the parallel *Salaam* contract, but the parallel *Salaam* carries these additional requirements due to the concurrent nature of it.

i. Each of the contracts, i.e. the original *Salaam* contract and the parallel *Salaam* contract, are distinct and cannot be correlated with each other. The obligations and responsibilities that the seller has towards the buyer in the original *Salaam* contract are unconnected to the obligations and responsibilities that the seller has towards the buyer in the parallel *Salaam* contract.[510] Obviously, in the parallel *Salaam* contract, the buyer in the original *Salaam* contract is the seller. Therefore, even if the seller fails to meet his obligations in the original *Salaam* contract, the buyer in the parallel *Salaam* contract can still have a good cause of action against the seller of the parallel *Salaam* contract, irrespective of the fact that the seller (who was the buyer in the original *Salaam* contract) was unable to fulfil his obligations due to a defect of someone else.

This is not very different from how the marine trade works under English law, as the seller remains under an obligation to the buyer when marine contracts are entered. In an analogous situation, it terms of liability apportionment, it is no different to how English insurance law works. For instance, under **section 148 Road Traffic Act 1988**, the motor

[509] Ibid
[510] Justice Mufti Muhammad Taqi Usmani, supra at p. – 194

insurers are strictly liable to indemnify for torts, irrespective of any indemnity issues they may raise in relation to the motor policy. They are still required to indemnify for the torts and later they have the option to raise a separate claim against the policyholders for their own allegations of avoidance of policy.[511] The same goes for Employers Liability insurance. Employers are under a strict duty of care regarding the torts suffered by the employees in the course of their employment and any argument for setting that duty aside is irrelevant.

It is felt that *Salaam* agreements would work if implemented in English law, as the characteristics are similar to the age-old English concepts. Questions may arise as to the practicality of how the litigation might work between the parties in the original *Salaam* contract and the parties in the parallel *Salaam* contract. However, it is argued that it is actually straightforward, as the buyer in the parallel *Salaam* contract can commence litigation for recovery from the seller of the parallel *Salaam* and the seller of the parallel *Salaam* can, no doubt, bring in the seller from the original *Salaam* contract, as an additional or Part 20 Defendant (as under Civil Procedure Rules Part 20), in the same litigation.[512] This would undoubtedly save both time and costs when dealing with both the claims effectively in one court.

ii. The buyer of the parallel *Salaam* contract must be someone other than the seller of the original *Salaam* contract.[513] It rationale behind such condition is quite apparent, otherwise it will defeat the whole purpose of having a *Salaam* contract in the first place and would be an iniquitous way of buying back the items sold. It is arguable that, if the buyer of the parallel *Salaam* contract is a different legal entity, e.g. company, but is wholly owned by the seller of the original *Salaam* contract, it would still be a restriction on the parallel *Salaam* sale.

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[511] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/1988/52/section/148> accessed 8 March 2014
[512] Justice, 'English Civil Procedure Rules online' (justice.gove.uk) <http://www.justice.gov.uk/courts/procedure-rules/civil/rules/part20> accessed 28 August 2013
[513] Justice Mufti Muhammad Taqi Usmani, supra at p. – 195

It is crucial to understand that these provisions are not man-made in order to circumvent legal aspects and human authorities. These are rules set by God and, irrespective of what tactics humans may impose to show on paper that there are different legal entities, the beneficiary remains the same; as such, the parties would still be conducting *haram*, as it diverts from the main theme, which is to abide by God's laws and please Him. Ultimately, as believed by every Muslim, a person is answerable to God on his worldly affairs. This has been mentioned in the Holy *Quran* in *Surah An – Najm* (Chapter 53), Verse 42:

- *"And that to your Lord is the finality"*[514]

Additionally, in the Holy Quran, on the Day of Judgment when everyone has to answer to God on his earthly affairs, in *Surah Al-Zalzalah* (Chapter 99), Verses 6 to 8:

- *"That Day, the people will depart separated [into categories] to be shown [the result of] their deeds."*[515]

- *"So whoever does an atom's weight of good will see it."*[516]

- *"And whoever does an atom's weight of evil will see it."*[517]

Additionally, in the Holy Quran in *Surah* Al-Muddaththir (Chapter 74), Verse 38:

- *"Every soul, for what it has earned, will be retained."*[518]

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[514] Holy *Quran*, '*Surah An – Naj*' Chapter 53 Verse 42 (quran.com) <http://quran.com/53> accessed 28 August 2013
[515] Holy *Quran*, '*Surah Al – Zalzalah*' Chapter 99 Verse 6-8 (quran.com) <http://quran.com/99> accessed 28 August 2013
[516] Ibid
[517] Ibid
[518] Holy *Quran*, '*Surah* Al-Muddaththir' Chapter 74 Verse 38 (quran.com) <http://quran.com/74> accessed 28 August 2013

As is quite apparent from the verses of the Holy *Quran*, it is clear that the affairs must be *halal* and the dealing on such matters is with God directly who shall judge them on the steps taken.

4. *Bai Mujjal:*

4.1. The Concept:

Bai Mujjal in simple terms means sales on credit. The words *Bai Mujjal* are a combination of the Arabic words "*Bai'un*" which means "purchase and sale" and "*Ajalun*" which means "a fixed time or a fixed period". This type of *halal* contract has the same effect as a sale of goods, where ownership of the goods transfers on consideration of payment, which is paid later on. The term as such refers to a situation where the sale has taken place and the seller has given a time limit for the buyer to make the payment.[519]

The items sold in such manner are passed from the seller to the buyer immediately upon *majlis al aqad,* i.e. in the same transaction session or contract place, but the buyer is allowed under *Sharia*, in such transaction, to make payment for these sold goods later. Another name for such contracts, and more popularly used in Malaysia, is *Bai Bithaman Ajil.*[520] Of course, it is crucial that both the parties are well aware by this point of the deferred payment settlement date and the price being fixed, so as to avoid any uncertainties. In respect of this thesis, the payment settlement period must be a known agreed time and should not be dependent on a certain occurrence or event, as it would call upon the concepts of *gharar* and would result in having the same issue as present day *takaful*, as mentioned above. Such a deferred payment contract is also referred to as *Bai Al-nasiah, Bai Al-Taqsit* and *Bai Al-Ajil.*

[519] Islami Bank Bangladesh, '*Bai Mujjal'* (islamibankbd.com) <http://www.islamibankbd.com/prodServices/prodServBaimuajjal.php> accessed 28 May 2014
[520] Brian B. Kettell, *Islamic finance in a nutshell* (1st edn, John Wiley & Sons 2010) pp.- 44 – 45

4.2. Religious laws:

The *fuquha* has confirmed that such credit transactions are *halal* and the reference is drawn from the *hadith* of the Prophet Mohammed (pbuh). It is narrated by Aisha, in paragraph 282 and by Qatada in paragraph 283 that, on one occasion, Prophet Mohammed (pbuh) had to provide his iron armour as security to a Jew, so that he could buy food on credit for his family and had agreed to pay later.[521]

In relation to the sale of the goods on a deferred basis, it is crucial that the price does not fluctuate later, when payment is due, otherwise it will end up appearing as a *riba* transaction, as nothing has been done by the seller to justify the extra payment other than time having passed. The price could be any price the parties bargain and agree on, although it appears there is some disagreement between scholars on the price figure.

Holger Timm in his paper mentions that the price to be paid is the cost and the profit made by the seller.[522] It is necessary to note that, in Islamic law, the parties are always free to negotiate on the terms, as long as any sharp practices are avoided and, in such cases, the parties are open to negotiate the credit period. In fact, as would have been noticed from perusing the thesis so far, the various restrictions set in Islam have been set so as to avoid circumstances of sharp practices in trade.

5. Conclusion:

In summary, the Islamic finance vehicles discussed above are similar to the traditional finance tools that are utilised in the normal day-to-day transactions. It is asserted that, keeping aside the difficult Arabic names, given that the origins of these vehicles are from the Islamic rulings and texts, which were originally set in Arabic, the ultimate operational ideas are very much the same, as can be witnessed in the traditional Western society.

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[521] Search Truth, '*Hadith* online' Paragraphs 282 and 283 Chapter 34: Sales and Trade, Sahih Bukhari <http://www.searchtruth.com/book_display.php?book=34&translator=1&start=19&number=281> accessed 8 May 2013

[522] Holger Timm, *The cultural and the demographic aspects of the Islamic financial system and the potential of the Islamic financial products in the German market* (GRIN Verlag 2004)

There is, no doubt, the restrictive pillars of *riba*, *gharar* and *maisir* in the various Islamic vehicles, which project an impression of being a hindrance to the advancement of *halal* vehicles. However, it is considered that the obstructions are necessary restrictions, the ultimate aim of which is to provide an equal bargaining platform for the parties so as to avoid an imbalance. The traditional Western society also has various gates in place, which appear under different names such as disclosure, utmost good faith, materiality;[523] these aspects had been introduced by human beings as society developed, whereas under the *Sharia* law the above concepts had already been ordained by God and must be strictly followed. As mentioned, these limitations are necessary safeguards that have been put in place, perhaps for a better democratic society; but in any event, irrespective of whether they are sent by God or man-made, the restraints are considered the consequential effects of the same.

The instruments of *Ijara*, *Bai Salaam* and *Bai Mujjal* are only a few of the Islamic finance vehicles that are in operation at present. There are a number of other *halal* finance mechanisms available, but it is outside the scope of this thesis to discuss those, as they are not directly connected to the ultimate proposed *takaful* model. As discussed earlier, this part of the thesis is to establish the various Islamic finance instruments that are in existence and are of direct relevance to the thesis. The idea of this thesis is not to analyse the various *halal* financial models used at present in Islamic institutions, as that would defeat the purpose of the thesis and would be unfocused and unambitious. Rather, the aim is to analyse the underlying principles of these instruments so as to witness their workability and practicality to be used as tools. The ultimate aim, as would be witnessed in later chapters, is to discuss how the various instruments mentioned above can actually fit into the marine insurance concept. This will lead to the creation of a model, which would be a *halal* marine insurance, minus the flaws that exist with the *takaful* models that are in operation at present.

[523] The comparative analogies of these terms between Islamic concepts and western terminologies have been discussed in previous chapter. See chapter 1 above.

The idea is to connect the concepts of premium, risks, excess and compensation into a *takaful* system so that a new innovative model can be introduced, which would have the skeleton of a traditional marine insurance but in *halal* form. Following up the lead from previous chapters on the proposed *takaful* model, the concept of a premium payment can be organised to sit under the Islamic instrument of *ijarah,* which is similar to a rental contract, whether it be the leasing of items or hiring someone for his/her skill. The concept of risk fluctuates during the course of insurance, depending on whether it turns adverse or not. If it turns adverse then, in traditional marine insurance, a claim is made, which means that compensation has to be paid out. The instrument of *Bai Salaam,* which relates to a contract of future sale but for which the payment is received at the present time, can be utilised in this aspect. *Bai Salaam* is considered as an exceptional type of sale that has been allowed in the *Sharia* and, in such contracts, the payer is entitled to ask for securitisation of the funds he is paying in advance. Securitisation relates to compensation and, in the proposed *takaful* model, both can be cosmetically related to comply with the concept of compensation.

Finally, the concept of excess payment can be configured with the assistance of the *Bai Mujjal* instrument in this respect. *Bai Mujjal* is essentially the reverse of a *Bai Salaam* contract, where the payer can pay later for the goods that he receives. It is a deferred payment arrangement between the parties. An excess payment is a payment that is paid later on, depending on the changing nature of the risk. Therefore, should the *Bai Mujjal* instrument be configured to work in a *takaful* model in such a manner that the excess payment is contemplated and completed, depending on the fluctuation of the risk, then this could envisage the introduction of a new type of *takaful* model. With this mind, the next chapter is introduced, where the proposed *takaful* model is unleased, considering all the discussions considered up til now in this thesis. The various traditional insurance concepts of premium, risks, excess and compensation, which are paired up with the Islamic instruments of *Ijarah*, *Bai Salaam* and *Bai Mujjal*, come into operation in their working function ability in the configuration of the proposed *takaful* model.

Part IV

A fresh new perspective towards *halal* marine insurance

Chapter 8: Proposed *takaful* model - "*X3-I.M.S. fusion*" *takaful* model[524]

The Big Picture

1. Introduction

This chapter explains in detail the proposed recommendations and model, which has been discovered during the course of the research, to fulfil the aims and objectives of this thesis. The principal idea is to examine whether it is possible to create a working model that maintains the strict *Sharia* rules, but which can amalgamate the principles of English marine insurance rules, without damaging or hampering the working mechanism of any or the other.

It has become a common consensus amongst scholars that Islamic finance had attempted to play catch-up with traditional Western markets. This had resulted in the creation of a structure that, on the face of it, was portrayed as *halal* but ended up as something that was simply a replica of Western instruments under the heading of *halal*. This affected the credibility of Islamic products as *Sharia* principles were being surrendered for economic achievement, which is contrary to Islamic laws.[525] With respect, it is felt that the same has taken place in this case, with *takaful* as well. *Takaful* attempted to operate in the same way as insurance; however, ~~however,~~ whilst the outer shell may appear to be fine, the internal instruments are in total disarray. This has resulted in an outcome that is not only unfavourable, but it became extremely questionable as to whether those models themselves are *halal*.

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[524] Please consider paragraph 3 of the Introduction below in this page, which details the reason behind the name of the researcher's proposed *takaful* model as "*X3-I.M.S. fusion*" *takaful* model

[525] Oliver Agha, 'Tabarru in Takaful: Helpful innovation or unnecessary complication?' 9 UCLA J. Islamic & Near E. L. 69 2009-2010, pp. – 69 - 70

A structure has been created of the proposed *takaful* model, which is set out below at the end of this chapter. During the course of the discussion of the proposed model, the different segments of the model will be broken down. The whole aim of this research has been to determine whether there is any possibility that an acceptable *Sharia* compliant marine insurance model can be established, which would work well within the boundaries of English marine insurance law. For easy reference, the proposed model will be named "*X3-I.M.S. fusion*" *takaful* model.[526] During further consideration of the proposed model below, the relevance of the title of the proposed working model will be understood better. However, to assist in our understanding, it should be noted the proposed model is not a hybrid, as is generally the case with other *takaful* models; rather, it is a fused mechanism of three different distillations or phases. Though both words appear synonymous at first glance, "Hybrid" is defined as "*A thing made by combining two different elements*"[527] and "Fusion" is defined as "*The process or result of joining two or more things together to form a single entity*"[528]. In the proposed model, three different and distinct instruments are wielded and set out in a single platform to create the complete mechanism, which is the proposed *takaful* model. The remainder of the name for the proposed *takaful* model is based on the fact that there are three distinct contracts in place and the letters represent the initials of each of the Islamic finance instruments in place.

Without repeating the issues of *takaful* as raised in the previous chapters, the existing models are extremely cumbersome and it is unlikely that they will have anything other than a short life span in English marine insurance market, even if they were to enter or able to enter the market.[529] It is not a secret that *takaful* has attempted to enter the English

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[526] Please consider the Annex below which has the whole proposed model drawn together, however, for the sake of ease, each of the phases and segments are broken down in this chapter. Without repeating the references mentioned previously, this chapter is kept concise on references to avoid repetition.

[527] Oxford Dictionaries, 'Hybrid meaning' (oxforddictionaries.com) <http://www.oxforddictionaries.com/definition/english/hybrid?q=hybrid> accessed on 14 May 2014

[528] Oxford Dictionaries, 'Fusion meaning' (oxforddictionaries.com) <http://www.oxforddictionaries.com/definition/english/fusion?q=fusion> accessed on 14 May 2014

[529] The researcher does raise a concern of *takaful* capability to enter English marine insurance market as the licensing and regulatory bodies such as the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) have very strict criteria for entering insurance services (which is not within the

insurance market during the last few years, only to fail dramatically. In July 2008, a *takaful* product was commenced in the English market called *Salaam halal* insurance, but the relevant company stopped trading a year later because of solvency issues. Although blame had been apportioned on the lack of inability to raise enough capital, this raises issues regarding the credibility of a *takaful* business for failing to convince prospective investors.[530] It would make more sense for investors to back a project that was well-organised and had a strong potential, especially following a recession when investors had lost funds in Western stocks and property markets. However, this really raises the difficult and major concerns, namely whether existing *takaful* models are really capable of trading in the Western insurance sector. It is believed that the answer lies in remodelling a *takaful* that will be viable and practicable in order to work within this niche market, being the English marine insurance market.

To give a concise comparative snapshot, the initial step is when the insured approaches the potential insurer for a marine insurance quote to find out whether the insurer would cover the specific voyage. As with marine insurance, it could be possible that the prospective insurer might cover 100% of the risk or perhaps a portion of the risk, in which case the insured would approach another marine insurer until all of his risks are covered. Once the insured finds full cover, then he/she is quoted a premium which, if accepted, they are then considered to have a valid insurance contract. In the event of an event occurring from defined marine perils, the insurer would cover the insured for the losses. In *takaful*, keeping aside the various differences, the working principle is the same, with cover provided in return for a specific amount for defined perils to the participants. In circumstances of losses from defined perils, the participants can make a claim from the *takaful*. It is not disputed that the comprehension of both insurance and *takaful* appears the same, at least from the outside.

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ambit of this thesis) and the existent models of *takaful* does raise grave concerns on the safeguard of consumers when in case of deficits, the end users i.e. insureds are personally liable.

[530] Dunkley J, 'Islamic insurance company Salaam Halal closes to new business' (2009) The Telegraph <http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/6600525/Islamic-insurance-company-Salaam-Halal-closes-to-new-business.html> accessed 9 February 2014

The important part of this proposed model is that the portrayed operational layer of the way traditional insurance works remains unaffected; rather, it is the internal mechanics of the functional aspects that are adjusted to ensure they are *Sharia* compliant. Internally, as the potential insured gets the marine insurance quote, he/she now has the opportunity to either accept or reject the quote. If they decide to accept the quote, in traditional insurance this quote is the premium that the insured would now have to pay to get the cover. However, in the proposed model, due to restrictions of *riba*, *gharar* and *maisir*, the insurer would be prevented from charging a premium.[531]

Some scholars have, rather regrettably, taken a much narrower approach on the functioning of traditional insurance.[532] It is stated that traditional insurance involves a bilateral service contract of risk protection selling that is not present in *takaful*, arguing that the latter works on a community basis discouraging wealth maximisation rather than for sole individual purposes.[533] Unlike commercial contracts, buying and selling forms the basis of the business relationship and, without that, there is no commercial venture to get involved in. Insurance business, like any other commercial businesses, is a trade that is there to assist individuals, but the insurer is there to make profits as well. If we take buying and selling out of it, we are left with a charitable organisation and we are back to square one, where existing *takaful* models are at present, which is a cumbersome, unfavourable, unappreciated, borderline *Sharia* authoritative appliance. It is no use hiding the fact that insurance is a profit-generating industry, with transactions based on risk administration, for which Muslims need to accept and devise *takaful* models that would fit the criteria, without damaging *Sharia* laws. It is believed that this is exactly what the proposed model of *takaful* is endeavouring to achieve.

Further, scholarly arguments involve that *gharar* and *maisir* clinging with traditional insurance because of the lack of certainty on "*future contingency will ever come to pass*

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[531] The restrictions of *riba*, *gharar* and *maisir* have been discussed in details in the introductory chapters, namely chapters 3 and 4 above.

[532] Haemala Thanasegaran, 'Making an entrance – Can Australia contribute to *takaful* (Islamic insurance) law reform?' (2013) 24 Insurance Law Journal, pp. – 107 -109

[533] Haemala Thanasegaran, Growth of Islamic Insurance (Takaful) in Malaysia: A model for the region?' (2008) 143 Sing. J. Legal Stud., p. - 145

and disputes about whether the contingency has occurred or pre-existed the contract have bred enormous litigation".[534] This view is disagreed and it is opined that traditional insurance functioning is to be appreciated more liberally. Disregarding traditional insurance simply because of the uncertainty of future events is unlikely to be an accurate reflection of the principles of *gharar* and *maisir*. After all, uncertainty exists in every aspect of life and commerce, even insurance litigation, which is conducted in the UK and USA is mostly funded on a contingency fee arrangement, i.e. whether the lawyer's remuneration is dependent on the contingent outcome to the matter. Such lawyer arrangement with a client would be validly upheld under Islamic law under the concept of labour-based *ijarah*,[535] despite the uncertainty. The analogy here is not to validate that the traditional insurance is *halal,* rather the aspect is that there are alternative instruments that offer flexibility, even under Islamic law, rather than holding a rigid view. It is asserted that the proposed model aims to look at flexible instruments, which would minimise the need to resort to litigation, thus saving time and costs.

It is crucial to note that, with any insurance relationship, there are two principles at work consecutively, namely contract and tort. It is felt that, with *takaful*, too much emphasis had been placed on the contractual relationship and not enough on the tortious aspect. All the existing *takaful* models, appear to have prompted mainly to introduce various ways for the *takaful* operator to maximise their income from underwriting. However, at the point of compensation, the models fall through, as they do not appear to cope with the amount of claims received. It is necessary to note that, under English marine insurance law, the tort law is followed very strictly and, until all the components of tort are satisfied, the payment of a claim is very unlikely. This thesis has not been designed to look at contractual or tortious issues under English law, but it might assist during perusal to note the following:

Contractual relationship = Agreement (offer and acceptance) + Consideration from both sides

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[534] Hania Masud, '*Takaful*: An innovative approach to insurance and Islamic finance' (2010-2011) 32 U. Pa. J. Int'l L. 1133, pp. – 1141 - 1142

[535] See Chapter 7 above for details of Labour based *ijarah*

Tortious relationship = Duty of care + Breach of that duty of care + Causation + Foreseeability of that tort

Diagram 8.1 (see annex) gives a rough breakdown of the working operation of traditional marine insurance and the steps followed when a claim is made. As would be noted, insurers have an enormous arsenal in their possession when a claim is made and, unfortunately, it appears that the whole concept had been glossed over when the *takaful* models were generated. Ultimately, due to the rather poor structures of *takaful* models, the participants become responsible for liabilities of a *takaful* operation, along with various components of the *takaful* model clashing with each other, both under jurisdictional law and, sadly, under *Sharia* law as well. With traditional marine insurance contracts vis-à-vis *takaful* contracts, each aspect of the insurance relationship needs to be handled individually and then joined back together to have a completely viable model. In fact, this is one of the principal objectives that the proposed *takaful* model aims to achieve, by breaking down the basic structures and then building them back up, brick by brick, so as to have a sustainable model without compromising on either principle.

2. Part I of the proposed model: "The Contractual stage":

2.1. The *Ijarah* component:[536] Wage-related analogy:

The initial part of any insurance contract and the part of the proposed model starts with the prospective insured making the premium payment to the insurer. This is, of course, following the latter's quote to insure the specified marine insurance voyage risk on defined goods. Generally, in English marine insurance law, the insurer at this stage would ask for a specified premium from the insured so as to cover defined voyage marine risks.

[536] *Ijarah* is explained in details in chapter 7 above, which is of 2 types, both of which variety can be used in this the proposed model. The first one, wage related *ijarah* relates to remuneration related arrangement where wages is paid in return for labour. The second one, lease based *ijarah* relates to rent related arrangement where payment is paid in return for use of usufruct of leased asset.

In *takaful* contracts under the various existent models,[537] the premium is camouflaged as *tabarru,* i.e. donation/contribution, so as to appear that the participants are giving away the funds without any intention of return. The idea is to sidestep the restrictions of *riba*, *gharar* and *maisir* in *Sharia* law by veiling the same as a charity. Obviously, as would have been noted from previous chapters, such an approach is not correct at all, as the *takaful* operator takes the funds to make yields with the *niya,* i.e. the intentions of the participants are nothing other than to be in a commercial venture for their own safeguards. The purposes of both parties are anything but from any charitable ideology.[538] It is intended to break down the proposed "*X3-I.M.S. fusion*" *takaful* model in each compartment during perusal to give a better understanding, with diagram 8.2 dealing with the *Ijarah* part initially.

In the proposed model, there is no need to smokescreen the monies paid as a premium as something else, and the premium should be allowed to enter as it is really intended to be, i.e. as a premium, where the insured would be paying the insurer the quoted premium. The ideology is set under the concept of a *ijarah* paradigm, which allows charging in return. As has been noted, the *ijarah* concept comprises two parts: one is for service charging and the other is lease charging.[539] It is asserted that the first part of the proposed insurance model can be explained from both prerogatives. However, commencing with the simpler analogy service-based *ijarah*, the insurer would be providing their specialist

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[537] Readers would have noted from chapter 6 above that examines the various *takaful* models that are existent at present and all of which clocking the premium payment as charity payment so that the payment does not look like that it is given to return more money i.e. compensation.

[538] See chapters 5 and 6 above where discussion has been done in details. In the event, readers wants to have a quick snapshot, the payment given by the insureds called as participants, are considered as *tabarru* i.e. donation rather than being considered as premium. Worse part is the donation goes on to become capital from which business is conducted. The researcher strongly disagrees with this approach in *takaful* of consideration the payment as *tabarru* as under Islamic principles, if the payment is actually be a *tabarru* then the doner i.e. participants really cannot be asked to pay specific amount as quoted by *takaful* operator since doner of a donation is at liberty to pay whatever donation they want to pay. The donee may set a guide but doner's is under no obligation to pay sum suggested by donee as it is a donation for charitable cause, provided voluntarily. Of course, by now, the readers would have noticed from reading the thesis, that the participants' needing the cover knows well that it is not a donation but a payment to cover them with insurance. The *takaful* operator knows well that it is here to maximise the funds to make business for *takaful* shareholders. Both parties know well that their respective intentions are for their own sake and not for the sake of others, yet they put on the pretence that this is for the common good. Their respective *niya*s are muddled from the original *niya* required for respective instruments to work under Islamic principles. Therefore, such aspects discredit and invalidate the whole of the pretence models at its initial point.

[539] See Chapter 7

service of marine risk handling, for which they are entitled to charge a fee. This fee can be benchmarked against the premium that would generally be charged in such marine insurance. Generally, benchmarking is allowed in Islam and this has been mentioned by a number of academics, including making reference to a verse in the Holy *Quran*. Benchmark is defined by Robert Delimio (1995) "*as an improvement process used to discover and incorporate best practice into business operation. Benchmarking is the preferred process used to identify and understand the elements (causes) of a superior or world class performance in a particular work process*".[540] It is mentioned in the Holy *Quran* in *Surah Al – Ahzab* (Chapter 33), Verse 21 that:

- *"There has certainly been for you in the Messenger of Allah an excellent pattern for anyone whose hope is in Allah and the Last Day and [who] remembers Allah often."*[541]

As can be noted from the above verse, God has pointed out that Prophet Mohammed (pbuh) has the best of the skills, which he practised as a human being and asked mankind to follow the prophet ways of life to attain God's reward. In effect, this is the reason why the *hadith* of the Prophet Mohammed (pbuh) is considered as a primary source of information for *Sharia* law after the Holy *Quran*. Benchmarking, in essence, is following the steps of another as a barometer. Justice Usmani considered the issue of benchmarking of the traditional LIBOR interest rate for *murabahah* transactions.[542] Although he expressed reluctance for such a practice, he confirmed that there is nothing in Islam that contradicts with benchmarking against the non-Islamic components. He rationalised that, as long as the elements of Islamic finance instruments are satisfied, simply using an aspect of non-Islamic nature for determining revenue, it does not make the transaction

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[540] Bashir Uj Jaman, 'Benchmarking in Islamic finance' (2011) Benchmarking in Islamic Finance and Banking, Markfield institute of higher education, University of Gloucestershire, p. – 2 <http://www.scribd.com/doc/59086711/Benchmarking-in-Islamic-Finance-and-Banking> accessed on 12 March 2014

[541] Holy Quran, '*Surah Al – Ahzab*' Chapter 33 Verse 21 (quran.com) <http://quran.com/33> accessed on 12 March 2014

[542] *Murabahah* sales refers to mark-up transactions where the seller informs the buyer the actual cost of the former to purchase the goods and the goods are then being sold to the buyer with an added mark-up to make profit. *Murabahah* is not the same as *Mudarabah* sales where the latter is an investor and entrepreneur relationship, as is utilised by existent *takaful* models.

haram, as the Islamic sale remains free from *haram* and is simply an indicator.[543] Also, Islamic finance scholar, Sheikh Yusuf De Lorenzo (2009), stated that *"A benchmark is no more than a number, and therefore non-objectionable from a sharia perspective..."*[544]

Accordingly, to keep in line with examples provided in the previous chapters, the fee payment made by the insured to the Claims Entity of the insurer would be referred to as £X, as illustrated in the diagram above. There are two crucial points about the *ijarah* relationship between the parties in the proposed model that need to be explained.

Firstly, it is vital to note that, in the proposed model, it is the insurer who is getting a fee, i.e. the premium, for offering to provide their specialist service of risk handling and not taking over the risk of the marine voyage of the insured goods. Although this aspect may relate to risk passing, in essence it is more closely connected to contract formation as this is phase 1 of the proposed *takaful* model. It is intended to make this aspect unambiguous, as may have been mentioned by authors including recent scholars,[545] that, on offering an insurance contract, it is argued that risk does not shift from the insured to the insurer. The risk stays with the insured at all times and the risk cannot be transferred simply by means of an insurance contract. Insurance is just a contractual relationship between the insurer and insured for indemnifying the latter by the former for defined losses, but not to get involved with latter's relationship with others. Should the insurer aim to get involved in the relationship of the insured and a third party, then the insurer and the insured would have to agree on separate contracts, such as that of subrogating the right of the insured to the insurer to deal with the matter independently by the insurer. Nonetheless, English law requires that three basic elements be present for formulation of any insurance contract,

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[543] Justice Mufti Muhammad Taqi Usmani, *An introduction to Islamic Finance* (1st edn, Maktaba Ma'ariful Quran 2007) pp. – 118 - 120
Justice Usmani continued with a nice example of two brothers, one dealing with alcohol, which is *haram* and the other with soft drinks, which is *halal*. To keep the latter's business profitable he used the profit rates of the former to his customers, so as to set his business scales on the *haram* business. On consideration, profits derived by the latter are not *haram* at all as he conducted a *halal* business and simply using the *haram* business as a scale, which did not affect his *halal* business. Hence, Justice Usmani justifies that using of benchmarking even to a *haram* business does not make a *halal* business *haram*.

[544] Bashir Uj Jaman, supra at p. - 4

[545] Tahani Coolen-Maturi, 'Islamic insurance (*takaful*): demand and supply in the UK' (2013) Vol. 6, No. 2, International Journal of Islamic and Middle Eastern Finance and Management, ISSN: 1753-8394, p. - 89

which are as follows: the premium amount, risk type incorporating subject that is being covered, and length of the cover.[546] In this proposed *takaful* model, all of these requirements are well satisfied for the formulation of a valid insurance service contract. Professor Bennett corroborates that an English marine insurance contract follows the same rules as basic contract law rules in terms of formation of contract.[547]

As such, the ideology behind the above argument is that, in English contract law, the risk follows the property of the goods. This has been set down both in common law and in statute under English law and so, whoever has the property of the goods, has the risk of it. In statute it has been mentioned in **s. 20(1) of the Sale of Goods Act 1979** that:

- "*Unless otherwise agreed, the goods remain at the seller's risk until the property in them is transferred to the buyer, but when the property in them is transferred to the buyer the goods are at the buyer's risk whether delivery has been made or not.*"[548]

Chitty critiqued that the automatic presumption is that risk and property goes hand in hand and whosoever maintains the ownership maintains the property and, as such, the risks.[549] This has been documented in various English law precedents such as *Healy v Howlett & Sons,*[550] *Pignataro v Gilroy,*[551] *Underwood Ltd v Burgh Castle Brick and Cement Syndicate,*[552] *Wardars (Export and Import) Co Ltd v W Norwood & Sons Ltd,*[553] *Stora Enso Oyj v Port of Dundee.*[554] In international trade, depending on the type of contract between buyer and seller, e.g. CIF (costs, insurance and freight) or FOB (free on board), risk and property may pass at different times. However, the aim of this thesis is

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[546] John Birds, *Birds' Modern Insurance Law* (7th edn, Sweet & Maxwell 2007) pp. – 82 - 83
[547] Howard Bennett, *The Law of Marine Insurance* (2nd edn, Oxford University Press 2006) pp.– 29 - 30
[548] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/1979/54> accessed on 14 March 2014
[549] H.G.Beale (ed), *Chitty on Contracts: Volume II: Specific Contracts* (31st edn, Sweet & Maxwell: Thomson Reuters 2012) paragraphs – 43-222 – 43-226
[550] Healy v Howlett & Sons [1917] 1 K.B. 337; Ibid
[551] Pignataro v Gilroy [1919] 1 K.B. 459; Ibid
[552] Underwood Ltd v Burgh Castle Brick and Cement Syndicate [1922] 1 K.B. 343; Ibid
[553] Wardars (Export and Import) Co Ltd v W Norwood & Sons Ltd [1968] 2 Q.B. 663; Ibid
[554] Stora Enso Oyj v Port of Dundee [2006] 1 C.L.C. 453; Ibid

not to explore international trading between parties, but rather *takaful* models with the aim of advancement from a marine insurance perspective.[555]

Also, as a simple illustration, this can be witnessed from the titles of various precedents as well. Irrespective of whosoever the insurers are indemnifying for defined insured catastrophes, the claims are lodged and/or defended in the name of the insureds, which is particularly true for liability insurance claims. For instances, in various cases where there has been personal involvement as a litigator during the researcher's career, on behalf of the Claimants, this is very much evident.[556] For example, in an Employer's Liability matter involving harassment and bullying, the employer, the Defendant's insurers, were an international insurance group; but as the Defendant was liable as the insured employer, the claim commenced under the insured's name. Also, in a Public Liability case involving food poisoning, the insurers were a well-known overseas insurance group, but since the latter was the liable party, the claim commenced under the insured's name. Similarly, in a Road Traffic accident case, although the tort-doer insurers were a major English insurance group, as the tort-doer the claim commenced under the Defendant's name, who was the insured.

In light of the cases mentioned above, the pleading headlines emphasise that the risk has remained with the insured, thus making the insured liable for the consequences of the respective tortious acts. However, there are precedences where claims had been filed by the insured against their own insurer for losses sustained, which, no doubt, have been reflected in the title such as *Britton v Royal Insurance Co*[557] involving an own insurance claim for arson loss under a fire policy, and *Beresford v Royal Insurance Co*[558] involving a claim under own insurance for loss of life under a life policy. The crucial concept to note is that the distinction lies on the principal basis of the claim. Litigation commenced under own policy against own insurer involves claims buttressing under the contractual obligation of the underlying insurance contract, whereas litigation commenced or

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[555] Ibid

[556] The case name could not be mentioned at all to avoid any disclosure of the parties' name, in line with the SRA provisions and guidelines

[557] Britton v Royal Insurance Co (1866) 4 F. & F. 905; John Birds, supra at p. - 220

[558] Beresford v Royal Insurance Co [1938] A.C. 586; Ibid

defended under the insured name is reinforcing the tortious obligation of the underlying insurance contract. Risk that circulates when an insured takes a policy with the insurer is for the controlling of tortious liability and any proceedings against own insurer relate to the satisfaction of the contractual promise of the insurer to indemnity. Risk of an asset relates to tortious aspects of it and will not leave the sight of the owner and insurance; it simply provides a promise that the insurer would step in to assist in case of consequences from the defined calamity.

Therefore, in line with the above analogy, it is safe to suggest that the risk remains at all times with the insured and the insurer is simply entering into an insurance contract for insured indemnification. The indemnification contract would, undoubtedly, be subjected to scrutiny and be set limits, hence losses from defined perils are only covered as, otherwise, this would take the matter outside the remit of the contractual relationship agreed between the parties. Even in respect of subrogation, the risks are always retained with the insured and it is only at a later contract between the parties, with the insurer seeking to limit insured losses (which the former has to satisfy under contractual obligation), that the insured has to give over his rights to the insurer.

Secondly, it is important to note that, in the proposed model, it is the Claims Entity of the insurer which is making the contract. Generally, it is considered that the insurer is the entity that makes the insurance contract and is the same entity that indemnifies the claims. However, in reality, insurers have a number of entities dealing with specific activities separately, e.g. underwriting, claims, investments and such others. They might have same parent organisation, but each have their own corporate legal entity. Examples include Hiscox insurance, whose insurance arm is registered as "Hiscox Insurance Company Limited" under company number 00070234[559] among others, whereas Hiscox underwriting arm is registered as "Hiscox Underwriting Limited" under company number

[559] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 12 March 2014

02372789[560] among others and their investment arm is registered as "Hiscox Investment Holdings Limited" under company number 03585353[561] among others.

The same scenario exists with Aviva insurance, whose insurance arm is registered as "Aviva Insurance UK Limited" under company number 00099122[562] among others, whereas their investment arm is registered as "Aviva Investors UK Funds Limited" under company number 02503054[563] among others.[564] Similarly with Zurich insurance, whose insurance is registered as "Zurich Insurance Company (U.K.) Limited" under company number 00376989[565] among others, whereas their investment arm is registered as "Zurich Pensions Management Limited" under company number 04150045[566] among others.

Therefore, the proposed model attempts to keep in line with the aspects of this separate entity as the objective is to produce a *Sharia* compliant model which, if required, would sit well with existing marine insurance doctrines and practices. Note should be taken that, for the consideration of this proposed model, the two entities that would play a role are the Claims Entity of the insurer (CE hereafter) and General Entity of the insurer (GE hereafter).

With this mind, the first part of the proposed model starts with the CE quoting a premium, where the risk management is to be handled on behalf of the owners of the insured goods which, at this preliminary point, is with the prospective insured.[567]

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[560] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 12 March 2014

[561] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 12 March 2014

[562] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 12 March 2014

[563] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 11 March 2014

[564] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://www.aviva.co.uk/legal/post-office/list-of-aviva-companies.html> accessed on 11 March 2014

[565] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 11 March 2014

[566] Companies House, 'England & Wales Companies House' (wck2.companieshouse.gov.uk) <http://wck2.companieshouse.gov.uk//compdetails> accessed 11 March 2014

[567] It is vital to note that the insurance agreement under the proposed model is for the goods on the specified marine voyage and not on the insured. This is in line with present marine insurance practice as in international trade depending on type of contract agreed between buyer and seller e.g. CIF or FOB the title

Therefore, considering the proposed model under the principles of a wage-based *ijarah* contract, the insured can be considered as *mustajir* who is paying the insurer as the *ajir*, a fee for the *ajir*'s specialist risk management service, which can be considered as the *ujrah*.[568] The job that the insurer has to do is defined along with the length of time, such as how long the risk management service is needed, which is determined by how long the cover is needed for. A risk management service is not prohibited in Islam, to be conducted as work for someone else, by an insurer's expertise.[569] It is important to note that the risk management service wages are unconnected to any external factors and the relationship is a bilateral contract between the parties. There is nothing incorrect with payment in advance to the labourer, in line with the *hadith* of Prophet Mohammad (pbuh) *"Pay the laborer his wages before his sweat dries"*.[570] Therefore, so far the first part of the proposed model fits well with the traditional marine insurance practice in English law, where the premium is paid to the insurer; it also fits well with Islamic law as the payment is under the *ijarah* wages contract, which is allowed in Islam.

2.2. The *Ijarah* component - Alternative lease-related analogy:

As has been mentioned earlier, it is believed that the *ijarah* concept, in both its categories, can be used for the proposed model. The wage-based *ijarah* concept, which is straightforward, has been examined above. Alternatively, it is necessary to analyse the applicability of the lease-based *ijarah* in the proposed model, which could assist not only understanding the model from a different angle, but also might assist in further studies in this area.

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of the goods will change hands, which basically means that risks also changes from the person who took the policy. That basically states that the designation of insured will shift along the way in international trade depending whosoever holds the title to the insured goods at the time of defined insured peril(s) to make the requisite claim. This is unlike traditional insurance contracts e.g. of road traffic where the insurance is on the individual. However, to avoid side tracking on this thesis, this project is confined to consideration of proposing a *halal* marine insurance model, which would set well with English marine insurance law.

[568] See Chapter 7 above for details of Labour based *ijarah* where the various terms are described in details along with their relationship and Islamic law notions

[569] The readers would have noted from the previous chapters particularly from Chapter 5 that there is nothing in Islam, which prohibits against taking steps to avoid risks and insurance as an ideology is not a concern against Muslims rather the operational concept, which is an issue.

[570] See chapter 7 footnote 33

Without repeating the points mentioned above, the prospective insured always bears the risk irrespective of taking an insurance cover as, at the time of taking the policy, the goods belongs to them. Therefore, the insured would have the authority to provide a lease of the goods for which he/she holds the title. Just like the approach on the proposed model above, the prospective insured would be aiming to enter an insurance contract with the CE. Diagram 8.3 explains this matter further.

Under the lease-related *ijarah* contract, as mentioned previously,[571] the owner party leases the asset to the other party, for the latter to use the usufruct without receiving the ownership. In the proposed model, it is set out that the insurer and insured agree a rent for leasing the goods to the insurer, which the insured wants covered by a marine insurance. This rent is benchmarked against the premium in such circumstances, which is acceptable in Islam, as stated above. The rent will be referred to as £X in line with examples in the previous chapters. The insured would deliver the goods to whichever warehouse is requested by the CE entity of the insurer. It is necessary to note that, under lease-based *ijarah*, the rent that is charged is determined by the usufruct that the lessee can enjoy from the lessor's asset. After all, it is safe to say that, where the usufruct of the leased asset is minor, the rent charged would also be minor and vice versa.[572] Usufruct has been

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[571] See chapter 7 above

[572] A practical example can be considered in which at present the Islamic Bank of Britain (IBB) in UK provides mortgage alternative to customers. IBB offers Home Purchase Plan (HPP) instead of traditional mortgage as offered by normal banks. HPP is based on two Islamic finance vehicles working together, Diminishing *musaharaka* and Lease based *ijarah*. (<http://www.islamic-bank.com/home-finance/home-purchase-plan/> (accessed 12 March 2014) *Musaharaka* stands for partnership with Diminishing *musaharaka* relating to reducing partnership. When any customers wants to purchase a property, he / she puts in the deposit (generally 20%) and IBB puts in the rest and purchases the property in partnership. The next step is that IBB leases this asset out to the customer under lease based *ijarah* for which customer pays rent to live. So, every month the customer pays a certain sum of money of which a portion covers the rent under the lease-based *ijarah* and the remainder portion is used to buy off shares of IBB hold in the property. As time goes along the shares of IBB keeps on diminishing and so is the rent amount until IBB would have nothing left eventually. Just like traditional mortgage, the outcome rest is the same - a full ownership at the end of scheduled period without any more liabilities.
The relevant aspect that the researcher wanted to point out is that where a property is purchased by the customer, would affect the amount he / she has to borrow and as such the rent he / she will have to pay to IBB e.g. a 3 bedroom property in Wales would require a significant smaller amount compared to a 3 bedroom property in Central London, as such the more the usufruct has on the leased property that customer will be using from IBB, the more the rent will the customer will have to pay. A property in Wales

defined by Her Majesty's Revenue and Customs as "*the right to the use and enjoyment of another's property*".[573] Zamir Iqbal and Abbas Mirakhor defined such leased-based *ijarah* as "*a sale of the usufruct (the right to use the object) for a specified period of time*",[574] an analysis also agreed by Muhammad Ayub.[575] Therefore, another way of looking at the matter is as follows:

Rent charged under lease-based ijarah ∝ Usufruct, i.e. Enjoyment of leased asset

Considering the above method, it is clear that, in lease-based *ijarah,* the rent payable is directly proportional to the enjoyment of the leased asset. So, where the lessee uses the asset for positive enjoyment, e.g. in property renting, the more this positive enjoyment increases, naturally the rent increases. Conversely, it is safe to mention that the less the positive enjoyment, the rent deceases. Therefore, the rent charged by the lessor to the lessee would reflect the level of positive enjoyment that the lessee can appreciate from that leased asset.

However, in the case of the proposed model, the insured would be leasing the requisite goods to the CE of the insurer. The aim is for the CE to take those goods on lease from the insured for utilisation of the enjoyment of those assets, but the insured would limit the enjoyment to risk consideration only. The enjoyment of the leased asset to the lessee is defined and, therefore, in line with Islamic law, which mentions that the asset leased has to be defined in their use. Since, the asset belongs to the lessor i.e. insured, at all times and therefore he/she as the owner, has the authority on how they want to deal with their respective asset. This gives more certainty into the contract between the parties and can be argued that restrictions and *gharar* and *maisir* are minimised, if not avoided.

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will have a lot less usufruct then a property in Central London, possibly due to factors such as location, facilities etc.

[573] HMRC Trusts and Estates Newsletter, (April 2013) <http://www.hmrc.gov.uk/cto/newsletter-apr13.pdf> accessed 12 March 2014

[574] Zamir Iqbal and Abbas Mirakhor, *An Introduction to Islamic Finance: Theory and Practice* (2nd edn, John Wiley & Sons Asia Pte. 2011) pp. – 80 - 81

[575] Muhammad Ayub, *Understanding Islamic Finance* (John Wiley & Sons 2007) pp. – 279 - 281

It is opined that, in any asset, there are two main characteristics or *halos* (as may be stated) that are always in existence, i.e. benefit and liability that are always with the owner of that asset. The asset may be leased to someone, but ultimately the ownership stays with the owner of the asset, i.e. the lessor. The lessee simply enjoys, for a defined period, the extracts of those benefits from the positive enjoyment when leased, in most cases. However, in theory, there should not be anything that restricts the lease to be defined only to negative enjoyment of that asset. As an example, a property can be rented to a tenant, but it can be agreed between the parties that the tenant could not use it for residing, i.e. no positive enjoyment, but enjoyment would be restricted to payment of all bills associated the property, i.e. negative enjoyment. Whilst it may appear out of the ordinary, the parties are at liberty to agree terms as they feel appropriate for their circumstances. Perhaps, in the above example, the property has a historical or sentimental value, or the lessee may have obtained a long lease and believes that lease of this property may assist him in some other of his business affairs. It should be noted that these positive values are not positive enjoyment of the mentioned assets, but rather consequential extracts, which are derived even from negative enjoyment of the assets. Either way, it is open to the parties under the freedom of contract to agree what they feel best and such freedom of contract steps are also approved in Islam. It is mentioned in the Holy *Quran* in *Surah* (Chapter 4), Verse 29 that:

- "*O you who have believed, do not consume one another's wealth unjustly but only [in lawful] business by mutual consent...*"[576]

As can be witnessed, it is permitted in Islam for parties to agree their business relationship amicably between themselves, provided it is not in contravention of any *Sharia* provisions.[577]

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[576] Holy Quran, '*Surah An-Nisa'* Chapter 4 Verse 29 (quran.com) <http://quran.com/4> accessed 11 March 2014

[577] Dr. Mohammad Hashim Kamali mentions about the adaptation of various Arab jurisdictions of introduction of their legislative laws, which are in compliance with this aspect of Allah (SWT) law of freedom of contract. Mohammad Hashim Kamali, *Islamic Commercial Law: An Analysis of Futures and Options* (Islamic Texts Society 2010) pp. – 137 - 138

In the proposed model, risk by its nature is an interpretation of responsibility and so the insurer would be faced with enjoyment of the asset, albeit not positive in nature. The insurer will still have the right of enjoyment since, as the lessee, they will decide the level of risk consideration of those assets they want to enjoy. As the insurer is faced with a consideration of risks of the goods, it can be stated that the insurer is having negative enjoyment of the leased asset. Reference is made to the above analogy, in that the rent is proportional to enjoyment; in the proposed model, the insurer is faced with risk consideration enjoyment, which is negative in nature, and the rent should also change its confinements. Therefore, instead of an orthodox lease where the leasee pays the leasor the rent, in this case the insurer, as the lease, would be paid by the insured, as the leasor for negative enjoyment of the risk of the goods, in light of the boundary crossover of enjoyment and rent. This rent that would be paid, as mentioned above, can be benchmarked against the requisite premium, as may arise in such a marine insurance voyage. Benchmarking is acceptable under Islamic law, as stated earlier.

In such an approach of a lease-based *ijarah*, the period would be determined by how long the insured needs the marine insurance cover, the amount of rent (which would be paid by the insured to the insurer, as discussed above) would be certain as benchmarked against premium, which is paid in advance, and the goods title remains at all times with the insured. It is agreed that it might appear, at first glance, slightly far-fetched, but considering the lease-based *ijarah* contract and insurance contract, this relationship between the insurer and insured is nothing inappropriate. This is because, under such approach, the contractual relationship between the parties fits well within the orthodox marine insurance principles, as well as from a *Sharia* perspective.

On could question the use of the lease-based *ijarah* terminology for phase 1 of the proposed *takaful* model. It would be argued that, firstly, the lease-based *ijarah* analogy is an alternative way of considering phase 1 instead of labour-based *ijarah*. It is an alternative way of considering and looking at phase 1 as, for some reason, labour-based *ijarah* could not be applied in a given case. It provides the flexibility for the insurer to implement a different method to the phase, as the need may arise for the insurer business.

Secondly, as the proposed *takaful* model is set for marine insurance, at times there could be circumstances where the insurer might want to closely monitor the risks, i.e. liabilities, of the goods on the marine voyage in question. After all, the whole idea of taking marine insurance cover is for the insurer to cover the liabilities of defined losses, thus the insurer can use this method for phase 1 to weed out a questionable insured with whom they might have doubts about entering into a legal relationship. This could be as a result of the insured's past history on claims, or due to the insured's personal circumstances, e.g. bankruptcy or dishonesty charges, or perhaps due to the nature of the goods that require marine cover. This lease-based *ijarah* method would provide the insurer with the ability to meticulously consider the subject requiring marine insurance cover, when circumstantial aspects raise doubts in the insurer's mind as to whether to provide cover for a specific proposal.

The above point would calrify queries about restricting insurers to only negative enjoyment of the goods, which requires marine insurance cover. The negative enjoyment of the leased goods is simply to contain the issue of dealing with phase 1, in an alternative manner. The negative enjoyment of the goods for the insurer would be to take on the risk appertaining to the goods only and not any positive enjoyment. As would have been noticed above, it is by no means a way of giving away the ownership of the goods in phase 1 of the proposed *takaful* model. The idea is to assist justification of the premium payment under Islamic law and, at the same time, provide the insurer with the flexibility of adaptation of a different method, as the insurer business requires, without damaging the structural architecture of the proposed *takaful* model. Moreover, it goes well in hand with the principle of insurance in that it is a contract of indemnification and, as such, relates to risk and liability indemnifying. Hence, the negative enjoyment of the goods gives the insurer an early opportunity at the stage of taking the premium on status and condition of the said goods.

2.3. Viewpoint of concepts of Premium and Risks from a *Sharia* perspective:

The above analogy of using a *ijarah* contract, irrespective of which category is implemented, can be utilised when covering the concepts of Premium and Risks, as this thesis was intended to consider. The reason being, a *ijarah* contract is acceptable in Islam and has been well advocated by the Prophet Mohammed (pbuh) in his *Sunnah*. The premium that is paid is acceptable under Islamic law as, depending on the type of *ijarah* used, it could be portrayed as a fee for the insurer's risk management service for a wage-based *ijarah,* or it could be reflected as a rent fee for the insurer's negative usufruct on renting for a lease-based *ijarah*.

Either way, the important aspect to consider is that there is a way, as demonstrated under Part I of the proposed model, that a premium can be paid and accepted in exchange and, since *ijarah* is a *halal* instrument, it does not contravene the concept of *riba*. Neither are the concepts of *gharar* and *maisir* applicable here, as the insurer and insured are crystal clear on the contract and know exactly what their obligations are, including the limits and outcome. There simply is no room for uncertainty or a game of chances taking place in this part of the proposed model. With this in mind, the thesis moves to the next step of the proposed model. Before leaving, it is worth noting that each of the components of this proposed model is independent and works separately, without depending on the reliance of another. This is a vital point to consider as narrated by Abdullah ibn Amr ibn al-'As, as mentioned in Book 24, Hadith 3597 of Sunan Abu-Dawud that:

- "*The Apostle of Allah (peace_be_upon_him) said: The proviso of a loan combined with a sale is not allowable, nor two conditions relating to one transaction, nor the profit arising from something which is not in one's charge, nor selling what is not in your possession.*"[578]

[578] Search Truth, '*Hadith* online' (searchtruth.com) <http://www.searchtruth.com/book_display.php?book=24&translator=3&start=19&number=3595> accessed 11 March 2014

The important point to note, as Prophet Mohammed (pbuh) has made clear, is that two sales inside one sale or transaction is not permissible, as it is just a pretence procedure to have the same outcome as *riba* but combining two sales into one. Therefore, in the proposed model, each component is independent rather than interdependent and the parts of the proposed model are simply phases that an insurance contract goes through rather than being part of that contract.

3. Part II of the proposed model: "The Preliminary Invigilation stage":

3.1. The *Bai Mujjal* Component:

The next part of the proposed *takaful* model involves the deferred sale of the goods that will go on the marine voyage. It is felt that this step is not only necessary for the proposed model to work, but it is also an important step from an insurer's perspective on costs management. From practical experience, it would be opined that a significant amount of costs is being spent every term by insurers in litigation disputing claims.[579] This step would reduce the litigation costs by the ability to examine the goods in advance, to the extent of ticking off the aspect of the Liability argument from the insurer's checklist when a claim is made. This would also be beneficial to the insured as he/she would have greater certainty and prompt resolution when valid claims are made. Allowing the goods to be sold to the insurer during this pre-voyage stage would allows this and the insurer would have the opportunity to analyse and determine before proceeding further, as explained in more detail below. In any event, this part of the proposed model is quite straightforward and is set under the *Bai Mujjal* transaction, as acceptable in Islam, when discussed in the previous chapter. For a better understanding, see diagram 8.4 provided in the annex.

[579] Whether claims are legitimate or not, that is not the issue. The point being particularly in UK, any claims are subjected to significant scrutiny before resolved and in a lot of cases end up being litigated. From the insurer point of view, they are running the insurance business and wants to pay out as little as possible in claims hence claims get disputed often as the insurer wants to be absolutely certain that aspects such as liability, causation, quantum of that claim actually meets the criteria, requiring them to pay for certain. Otherwise, as far as the insurer views, it is a waste to pay claims when there is a possibility that on a claim payment can be avoided.

The insured (who is also the seller in the international trade) takes the goods that he/she wants to go on the marine voyage and makes a deferred payment sale to the General Entity of the insurer (GE). The GE is involved in the transaction, as there are no claims with the deferred payment sale and thus the CE does not need to be involved in this transaction. To reiterate, although the GE and CE may have same parent organisation, namely the principal insurer, each of these entities has their own individual legal personality. Therefore, in this phase of the insurance relationship, the GE purchases the goods from the insured for a specific amount and may ask for it to be delivered to a certain place. Although, during phase 1 of the *ijarah* transaction, the goods may have already been sent to the insurer's designated place, it would suffice for the goods to remain in that place.

For ease of understanding during perusal, the deferred price that the GE would pay the insured will be referred as £C. As stated, this is a *halal* deferred sale that is agreed between the parties and, for the sake of completeness, the number of days that the insurer has to make the payment to the insured would be referred to as Q days. The parties agree at this stage that, should payment not be made by the insurer in Q days, then the payment would be waived by the insured as *sadaqah,* i.e. charity. It is important to note that there should be no confusion between phase 2 *Bai Mujjal* contract and the distinct contract that the insured, as the seller, would have with a buyer overseas. The phase 2 *Bai Mujjal* contract relates to the insurance policy that involves the relationship between insurer and insured in regards to the marine insurance cover. The trading relationship between the insured as the seller and the overseas buyer is an international trade contract, in which the phase 2 *Bai Mujjal* contract is not connected. Although the issue is that of the same goods, it is these goods that require marine insurance cover, as the phase 2 *Bai Mujjal* contract is a different way of obtaining *Sharia*-compliant marine insurance cover. One can rest assured that, before the goods set sail to reach their point of destination, as agreed in the international trade, the ownership of the goods returns to the insured, i.e. seller in international trade, in the final phase 3 *Bai Salaam* contract, which is discussed below.

3.2. Viewpoint of concepts of Risks from a *Sharia* perspective:

From an Islamic perspective, the above transaction of *Bai Mujjal* contains nothing that is derogatory and neither does the deferred transaction in terms of English marine insurance law. The goods that will be transported on the marine voyage belong to the insured and, being the owner, he/she has the authority to do whatever they want and to sell whatever way they want. The parties have the freedom of contract and it is a mutual agreement between the parties, i.e. the insured and the insurer, how they want to manage the relationship, etc. If the insured wants to walk away at this stage, there is no harm; however, that would mean that the phase of the insurance is not completed and so cover cannot continue. Conversely, upon acceptance of the goods, the insurer now has the opportunity to examine the goods for which marine insurance is required. Upon inspection, the insurer can determine whether sufficient disclosure and utmost good faith has been practised by the insured. The insurer has the opportunity to walk away, should they fell that there is lack of the same. This is a significant preventative step that would save a considerable amount of time and costs in litigation, rather than attempting to solve the deficiency later on. It goes well in line with the English maxim of "Prevention is better than cure". Similarly, the insured will have the surety that the insurer will not be arguing Liability arguments under this prerogative and will not be able to plead in their defence. This would likely save sufficient time and costs in line with the preamble of Civil Procedure Rules and Jackson reforms that are currently encircling civil litigation in England and Wales.

It is noteworthy that, upon a deferred sale under phase 2, the risk shifts to the insurer, as being the owner of the goods, so any loss occurred starting at this point is the responsibility of the insurer. This gives the insured an added protection under the proposed model, which even conventional marine insurance would not do, and is a necessary part. As will be noted during perusal of the final phase of the proposed model below, goods are returned to the insured at a later date when they reach their final destination. This is the cover that the insured has been looking for, and this deferred sale forms the basis for the final phase to click in. The shipment of the goods via the marine

voyage is the responsibility of the insured, which he/she had agreed separately in a distinct contract with the overseas buyer; these phases do not affect the separate overseas buyer contract, either before the point of departure or until the goods finds their way to the insured.

It is necessary to point out that the deferred sale is an independent contract and not a contract within another contract. There is no *riba* as payment has been agreed at the payment of contract and no increase will take place due to passage of time. In fact, the insured has agreed to waive off the payment, if it is not paid within a certain time. This is a much nobler step from a *Sharia* point of view, as mentioned in the Holy Quran in *Surah Al-Baqarah* (Chapter 2), Verse 280, that:

- "*And if someone is in hardship, then [let there be] postponement until [a time of] ease. But if you give [from your right as] charity, then it is better for you, if you only knew.*"[580]

As can be noticed from the holy verse, God has encouraged even giving up something due as a charity as higher dignified approach. Therefore, in this respect, the second phase of the proposed model is in compliance with the Islamic principles and introduces an aspect which is approved by God Almighty. On a similar note, as a deferred sale can be considered to be a debt that is to be agreed to be paid later after a defined period (although the insured waiving off the debt is another aspect), it has been emphasised to be in writing as in the Holy Quran in *Surah Al-Baqarah* (Chapter 2), Verse 282, that:

- "*O you who have believed, when you contract a debt for a specified term, write it down. And let a scribe write [it] between you in justice. Let no scribe refuse to write as Allah has taught him. So let him write and let the one who has the*

[580] Holy *Quran*, '*Surah Al-Baqarah*' Chapter 2 Verse 280 (quran.com) <http://quran.com/2> accessed 17 February 2014

obligation dictate. And let him fear Allah, his Lord, and not leave anything out of it..."[581]

The verse further continues that:

- "*...And do not be [too] weary to write it, whether it is small or large, for its [specified] term. That is more just in the sight of Allah and stronger as evidence and more likely to prevent doubt between you, except when it is an immediate transaction which you conduct among yourselves...*"[582]

Once more, in this part of the proposed model, the *Bai Mujjal* sale is done in writing with terms and periods explicitly clear, at the time of the contract between the parties. This takes away the issue of *gharar* and *maisir* in its totality as none of the parties can complain that they are uncertain of their obligations in this deferred sale contract. Moreover, the contract is in writing, in line with *Sharia* principles, and it is maintained that this leaves no room for argument from the Islamic perspective, or even from a jurisdictional perspective, to allege any defects in this contract, i.e. the second phase of the proposed model.

4. Part III of the proposed model: "The Tortious stage":

4.1. The *Salaam* Component:

This thesis intends to commence this final phase of the proposed model with the famous quote of renowned playwright, William Shakespeare, "*To be, or not to be, that is the question*".[583] The reason for this is because it refers to the phase where determination needs to be made, whether tortious elements come into play, i.e. whether compensation is payable or not and, if so, how to deal with such entitlement without breaching any of the

[581] Holy *Quran*, *'Surah Al-Baqarah'* Chapter 2 Verse 282 (quran.com) <http://quran.com/2> accessed 17 February 2014
[582] Ibid
[583] William Shakespeare, 'Hamlet' (3/1); <http://www.artofeurope.com/shakespeare/sha8.htm> accessed 16 March 2014

Sharia restrictions, particularly that of *riba*, *gharar* and *maisir*. This, no doubt, has been the centre of a dilemma among *Sharia* society, as can be evidenced from the various models, as discussed in the previous chapters. It is reasoned that it is simple to understand, as how can one structure a financial instrument as insurance *halal,* when the principal aim of insurance is to reimburse uncertainty, yet a *gharar* restriction, in particular, is in play? The answer, it is believed, could lie in the implementation of a *halal* primary instrument as the cog in the insurance machine, which would allow for recoverability in uncertain conditions. In this respect, it is proposed to include a *Salaam* component into the proposed model.

Following the *Bai Mujjal* phase above, the goods that are to go on the marine voyage are, at this stage, owned by the GE of the insurer, which is a separate legal entity. At this final phase of the proposed model, the GE would be entering a *Salaam* contract in the sale of the goods to the insured. However, it must be noted that the *Salaam* contract between the GE and the insured is not a sale back, but a forward payment sale of a different type of goods to the insured. The GE is entering a *Salaam,* i.e. forward selling contract, with the insured, where the GE is selling the insured. For illustration purposes, Y days mature goods in advance, where Y is the number of days it takes for goods to reach the marine port destination. Under the *Salaam* contract, the GE would be known as the *muslam ilaih*, the insured would be known as *rabb-us-salam*, the price that the insured would be paid (referred to as £A) is known as *ra's-ul-mal,* and the goods sold would be called as *muslam fih.* As will have been noted, the *Salaam* contract has been allowed as an exception to the restrictions of *gharar* and *maisir* and it is acceptable in *Sharia* law that the specific goods are delivered later on a fixed date, but payment can be taken upfront. To avoid any confusion, this final phase of the proposed model does not affect the position of the overseas buyer waiting at the point of destination, because the insured has the ownership of the goods at this stage. In the proposed model, there are two aspects to the *Salaam* contract, which need to be clarified in order to understand them better. One is that of time and other is that of payment, both of which are essential in international trading.

Starting with the concept of time, in the proposed model the GE is forward selling, the insured, i.e. Y days matured goods, which the insured will be able to access at a different location, i.e. the destination point of the marine voyage. These Y days have been calculated in line with the number of days it will take for the goods to reach, by marine voyage, the port of destination, keeping in line with the insured's initial intention when he approached the insurer. It might be perplexing that the goods that the GE is transacting under the *Salaam* contract are the same goods that were sold to the GE under the previous phase under the *Bai mujjal* contract. It strongly differs in that viewpoint, as the goods that are sold under the final phase of the proposed model are Y days matured goods that have been sold in advance and paid for in advance. Although the goods may or may not change physically from the outset, depending on the goods the argument remains stable in that the goods sold under the final phase are different configured goods than those sold to the GE previously.

The above argument of the proposed model can be justified in a few ways, of which the obvious instance is when goods, e.g. cheese, are sold. For example, if the GE sells the cheese to the insured for the specific destination point, then, as is the nature of cheese, it matures during the marine voyage; as a result, the cheese that the insured receives at the destination point has been maturing for many days. Undoubtedly, the subject of the sale remains specific as at the time of sale. Using the same analogy, although goods that are sold may not show any apparent change of physical character, it does not mean that they did not mature over the course of that marine voyage; in other words, the change is not visible instantly. Therefore, the *Salaam* sale transaction that takes place between the parties in the third phase is the forward sale, where the insurer obtains funds from the insured in advance, with an obligation to provide the specified matured goods by a specified date.

Additionally, it is essential that the number of days agreed under the *Salaam* contract, i.e. Y days, is less than Q days that is agreed in the second phase of *Bai Mujjal* contract. An alternative way of looking at this is to ensure that the Q days value is larger in number than Y days, as such containing a number of additional days which, for example, would

be additional B days. There are no restrictions in Islam on parties agreeing on the number of days to satisfy separate transactions.

The other concept is that of payment under the *Salaam* contract between the parties. As it is a forward payment sale contract, the insured has to make the payment to the GE at the time of the contract of *Salaam,* which is illustrated as £A. There are two aspects of this payment under the proposed model of *Salaam* contract. One is that £A is benchmarked against the excess, which the insured would have been required to pay in a traditional marine insurance contract in such cases. The second is that the value of £A is the same as the value of £C, as demonstrated under the second phase of a *Bai Mujjal* contract. Once more, there is nothing restricting benchmarking in Islam and neither is there any restrictions on agreeing a value of a contract, as parties have the freedom of agreement in Islam.

As a *Salaam* contract, unlike a *Bai Mujjal* contract, is a forward selling contract and as would have been noted from the previous chapters, the seller is under an obligation to provide a security to the buyer, in the event that the seller fails to fulfil his/her obligations. In this respect, the proposed model would make reference to the fact that the seller, i.e. the GE, of the *Salaam* contract would provide a security by the CE to the buyer, i.e. the insured, should the GE fail to comply with the delivery of goods within the appointed time under the *Salaam* contract. This could be due to circumstances within the GE's control or defined circumstances outside the GE's control e.g. act of God, leading to loss of goods in the marine voyage. The amount of surety that the CE would be standing for to compensate the insured in the event of loss is determined by the extent of the loss that the insured would face. Another way of looking at this is that the surety provided by the CE would be determined on the compensation cover that the insured intended in the first place. This would provide a certainty to the parties on the amount of obligations and there is no just enrichment, as such *riba*, *gharar* and *maisir* is not applicable in such cases.

4.2. A scientific approach to mature goods under *Salaam* contract:

To add further intrigue, it is felt that scientific reference on the argument of matured goods, as proposed, might suffice. There are various theories in physics that deal with movement of atoms of elements, and it is not the intention of this research to delve into those. However, a couple of theories that are of relevance are the theory of Atom Vibrations and the theory-of Absolute Zero. The theory of Atom Vibrations represents the atoms inside the molecules in every substances and which are in constant vibration and are changing positions and shapes internally, which constitute rhythms.[584] Depending on the substances, the vibrations speed and activity differs, but the vibrations always remain still.[585] Absolute Zero refers to the condition when the atoms no longer vibrate and are brought to a rest and, as such, no more internal changes take place. However, the temperature at which Absolute Zero is recorded is at –273.16° in Celsius.[586] This is equivalent to –459.67K in Fahrenheit scale, which is almost impossible to create except in extreme controlled laboratory conditions.[587] To an extent, it may appear that the above analogy is slightly farfetched, but a closer inspection shows that the instrument of *Salaam* sits well in the proposed model and overall picture. It is not the same goods that are being sold by the GE to the insured under the proposed *takaful* contract, rather it is the forward selling of a specific type of goods that are being sold to the insured.

4.3. Viewpoint of concepts of Excess payment and Compensation from a *Sharia* perspective:

In the eyes of *Sharia* law, a forward sale contract is considered acceptable in Islam. It is considered to be one of the exceptions to the analogies of instant payment, as has been mentioned in the previous chapter. The concept that is of prevalence here is to consider

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[584] D. Lindsay Watson, 'Chemical Music and Its Meaning' (1931) Vol. 19, No. 524, The Science News-Letter, pp. 262-271

[585] Davide Castelvecchi, 'Molecules: With a Closer Look, Chemists Find Molecules Switch Shapes Slowly: Findings May Challenge Theory Explaining Vibrations' (June 2008) Vol. 173, No. 18, Science News, p. - 7

[586] John F. Allen, 'The Approach to the Absolute Zero of Temperature', (1949) Vol. 69, No. 1 The Scientific Monthly, pp. 29-33

[587] Science Daily, 'Absolute zero' (sciencedaily.com) <http://www.sciencedaily.com/articles/a/absolute_zero.htm> accessed 8 March 2014
Also: Planet Save, 'Achieving absolute zero' (planetsave.com) <http://planetsave.com/2013/01/06/temperature-below-absolute-zero-achieved/> accessed 8 March 2014

whether the tactic used is *halal* throughout. In the proposed model of the *Salaam* phase, the payment is made by the insured to the GE for an advance selling contract. In itself that is acceptable and the amount and the time period is a matter of negotiation between the parties, all of which are acceptable in Islam. The situation is definite and every party knows what they are supposed to do and the consequences if they fail to do so. The insured knows that they need to make payment upfront otherwise the contract will fall through and so makes the requisite payment. The GE knows that delivery of certain goods needs to be made at a specified place within the agreed period, otherwise he becomes liable and so the respective actions are conducted. The payment is benchmarked against excess, which is not restricted in Islam; the number of days needed by the GE is a matter of calculation where, in order to keep the business running efficiently, the number of days are fewer in value, in contrast with the number of days that were agreed in the second phase of the *Bai Mujjal*. So far, nothing has occurred which is not acceptable in Islam or contrary from an English common law jurisdictional perspective. There is no place for *riba* as payment is for goods sold, there is no *gharar* as parties are secure on their obligations, or *maisir* as there are no vague, shot-in-the-dark actions. A *Salaam* contract is acceptable in Islam and so any arguments relating to its nature under *gharar* are inapplicable.

Under a *Salaam* contract, collateral is required and is provided by the CE stepping in to stand as the surety. The amount that the CE gives as surety represents the actual value of the goods, in the event that the GE fails to meet his obligations. The price that had been negotiated between the insured and the GE under the *Salaam* contract is a matter of personal choice between the parties under the freedom they have. The CE represents the actual amount of compensation in the case of the GE failing. There is nothing objectionable to this aspect, either under Islamic or relevant English marine jurisdictional law. In fact, even if the *hadith* of the Prophet Mohammed (pbuh) is reflected upon, as mentioned in the previous chapter, where he gave his armour as a guarantee under the *Salaam* contract to get the food on credit, nothing had been said about whether the armour and the food were exact in value. As the *Salaam* contract is considered an exception, any arguments of *riba* in this respect would be inapplicable as there would no

unjust enrichment by one party doing nothing; rather, it is a risk taken by one party if the other party fails to meet his obligations, as he can fall back to be compensated. The compensation is a figure that the parties mutually agree between themselves under the freedom of contract available to them. Therefore, this approach is acceptable under Islamic law, as restrictions of *riba*, *gharar* and *maisir* do not come into play.

5. The Aftermath and the Consequences:

Subsequent to the marine voyage, either of the following two outcomes are applicable: (i) that the goods will reach the destination place as per the *Salaam* agreement between the GE and the insured, or (ii) that the goods do not reach their destination, for some reason or another, and thus be in contravention of the *Salaam* contract. Taking each of the outcomes in turn, in the event that the goods do reach their destination point, as per the third phase of the *Salaam* contract between the parties, the GE retains the funds of £A (the amount which was benchmarked to excess) that the insured had provided. Since the GE has managed to fulfil its contractual obligation under the determined period of Y days, there is no issue of losses and the insured does not have to make a claim for surety to the CE. It is necessary to note, that the second phase of the *Bai Mujjal* contract is still live and which stipulated the payment by the GE to the insured within Q days, where Q days is larger in value than Y days of the third phase. In such case, under the second phase of the proposed *takaful* model and in line with the concept of utmost good faith, as exercised in marine insurance, the GE would be able to make the payment to the insured of £C. It should be noted that the value of £C is the same as the value of £A. Hence, the insured in essence would obtain funds from the deferred sale contract, which had been benchmarked against the excess, as the relationship between the parties worked out well without the need to resort to compensation.

In the alternative situation, under third phase of the *Salaam* contract, the GE fails to keep up its obligations to deliver the goods within the correct time period, i.e. Y days, to the correct destination point, due to calamities taking place on the marine voyage. In such cases, the insured would have the ability to approach the CE, who stood as security to the

GE, and make claim for compensation. The CE, as the payer of the compensation, considers the extent of the losses and determines the compensation to be paid out. As the GE failed to meet its responsibility within Y days under the *Salaam* contract leading to the claim of compensation by the insured, the second phase of the *Bai Mujjal* contract still remains live. The *Bai Mujjal* contract requirement of making the payment of £C by the GE to the insured within Q days, where the value of Q days was greater than Y days, would not be met by the GE and, as per the second phase agreement, the insured would waive off that payment due as charity. It would be reminded that £C is equal to £A that had been benchmarked to excess, hence the net result is a mirror reflection of traditional insurance, whereby the insured made a claim for compensation with payment of requisite excess.

6. Effects on international trade:

It could be strongly argued that, with the implementation of the proposed *takaful* model in marine insurance contracts, there would only be positive effects in international trading. The insurer would get to inspect the goods himself and would manage the voyage aspect as well, thus minimising the need for wasted legal costs and time arguing in court on liability and quantum. Liability arguments, as generally utilised by the insurer, about causation and contractual breaches, should be reduced significantly as, when goods reach the insured, it is the insurer who would be sending the goods on the marine journey. By then, it would have been reasonably expected that the insurers would have been aware of the goods and the voyage. Similarly, this would assist in the payout of compensation to be dealt with promptly and the need for litigation would be significantly curtailed. More importantly, it will be a marine insurance model, which is both *halal* and jurisdictionally acceptable.

The various contracts entered between the insurers and insured under *takaful* have no relationship that the insured, as the seller, had entered with overseas buyer separately for international trade. Various payments for international trading such as carriage charges, freight charges and such others, are dependent on the contract that the insured as the

seller had entered with the overseas buyer, e.g. either CIF or FOB. These have no connection with the phases that the insured and insurer go through for the implementation of the proposed *takaful* model. The phases of the proposed *takaful* model are simply to provide marine insurance cover, as is originally intended both in action and intention,[588] and have nothing to do with the underlying contract that the international trading parties may share. The goods would still be carried by the marine carrier, as was originally agreed between the insured, as the seller with the overseas buyer, and that does not change due to the rhythms that the insurer and insured go through to get *halal* marine insurance cover under the proposed model.

Along those lines of international trading, it is rather a common situation in international trade that goods purchased by the buyer are resold to a second buyer, even when the goods are still on the marine voyage; the goods are then obtained by the consequent owner with the production of necessary documentation, with the payment going through eventually. The same outcome can be achieved with the proposed *halal* marine insurance model as well. The part in which the emphasis is made is the third phase of the proposed *takaful* model in a *Bai Salaam* contract. In general, the *Salaam* contract allows flexibility for the implementation of a parallel *Salaam* contract; as such, the overseas buyer of international trade can enter a promissory agreement with the second overseas buyer for the sale of the defined goods. The only restriction is that, in Islam, goods cannot be sold without receipt, hence no funds are transferred immediately. However, the promissory note acts as an effective tool in any event, as, should the GE under the proposed *takaful* model satisfy its obligations, then the goods can be immediately transferred to a second buyer, with the clearance of the payment going through.

7. Conclusion:

In conclusion, without repeating what is mentioned above, the aim of this thesis had been to find and propose a new *halal* marine insurance model that will work within the ethos

[588] Unlike the other existent *takaful* models where various payments had to be clothed in different purposes only for the payments to go through and even then it does not work well as it keeps on conflicting with other instruments. See Chapter 6 above for the different types of *takaful* models in practice at present

of traditional marine insurance. The proposed *takaful* model was intended to meet that expectation by keeping as close as possible to the orthodox working marine insurance structure, but simultaneously keeping within the remits of *Sharia* principles at all times. The payment of the premium relating to the *Ijarah* contract, the risk/liability and excess arguments relating to the *Bai Mujjal* contract, and compensation payment relating to the *Bai Salaam* contract, are all *halal* financial instruments that could be utilised to achieve the same outcome as traditional insurance, without disappointing one or the other.

From the outset, despite opinions on the structure of the proposed *takaful* model, it is opined to be a small price to pay, so far as Islamic and jurisdictional domains are not compromised. It would be noted that the existing *takaful* models are not basic straightforward structures. Plus, the models are simply becoming complicated along the way, as Islamic society attempts to create hybrid *takaful* models to catch up with the modern world. The conceptual notion of insurance is rather simple, but the implementation of insurance in compliance with Islamic law is not an easy task due to the presence of restrictions of *riba*, *gharar* and *maisir*. Hence, the multifaceted structures are worth paying, as long as the underlying principles are unprejudiced.

The predicaments with existing *takaful* models are that changes have taken place in relation to various concepts, which have long existed in Islamic law. As discussed earlier, the basic concepts had their meanings altered, contrary to the *Sharia* principles, and instead of evolution of Islamic finance, what can be witnessed is nothing other than adverse transmutation. These structures existing with *takaful* models are questionable modernisations, as foundation principles have been compromised along the way. The answer for *takaful* advancement lies in the production of something solid that will be widely acceptable within the Islamic community. It is maintained that this has been achieved with the proposed *takaful* model for marine insurance, which could lead to further advancement in this field, as well as other types of *halal* insurance products.

Diagram 8.1: Diagram of the general steps considered in orthodox insurance when a claim is made:

Traditional marine insurance:

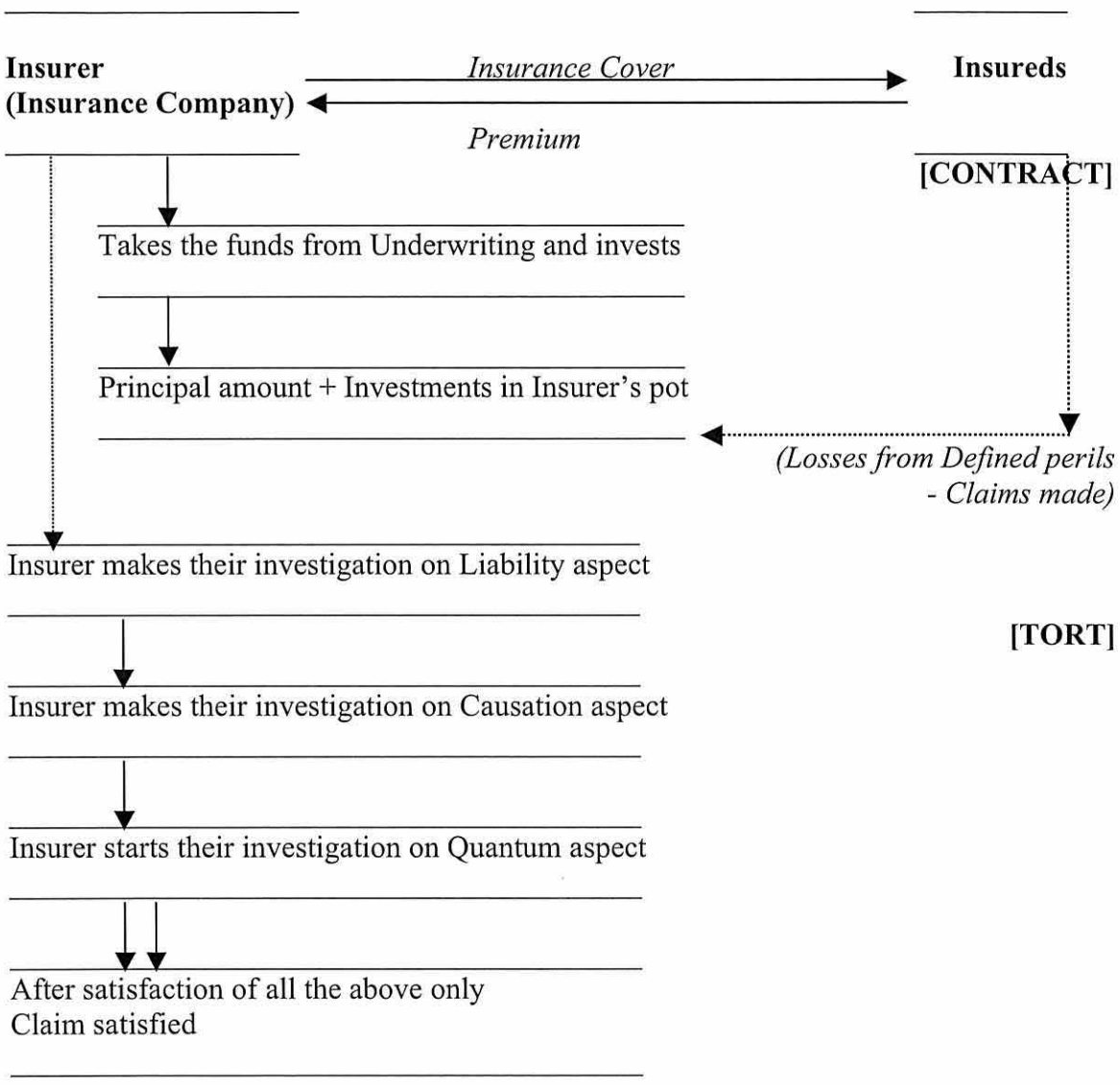
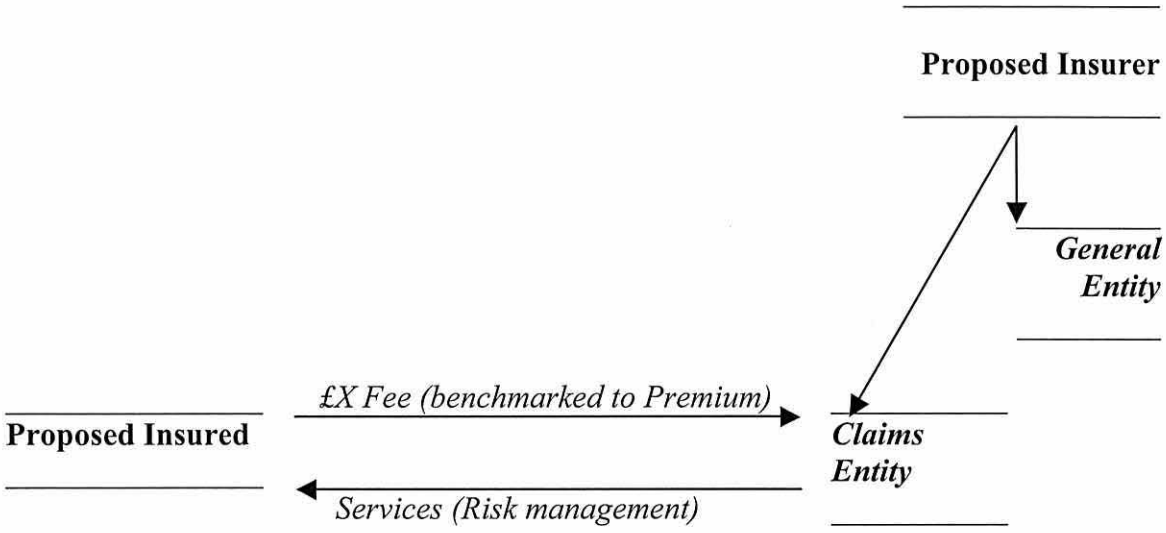
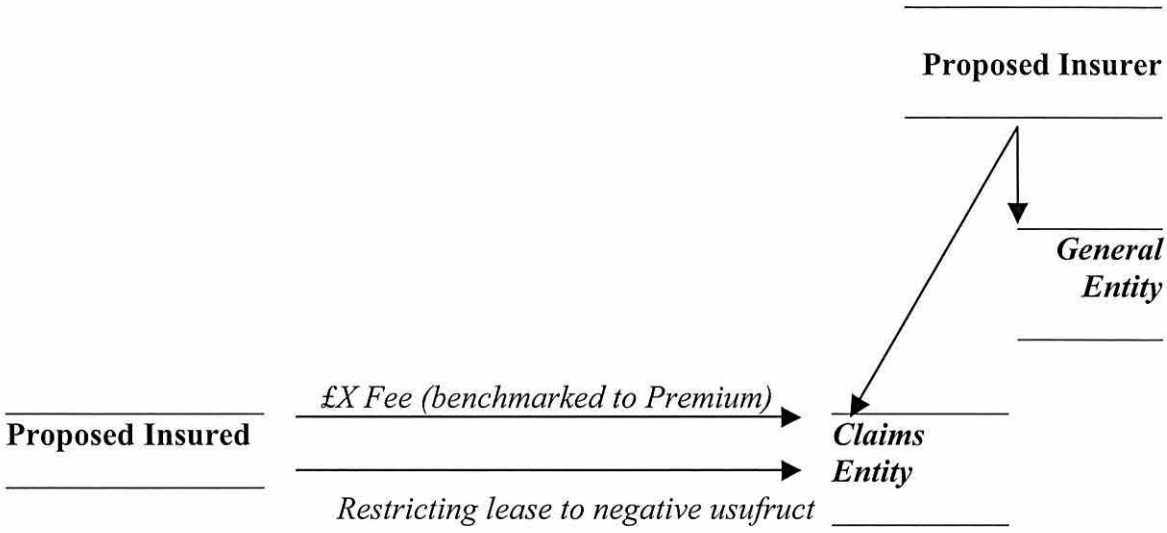


Diagram 8.2: Wages-related *Ijarah* component of proposed model:



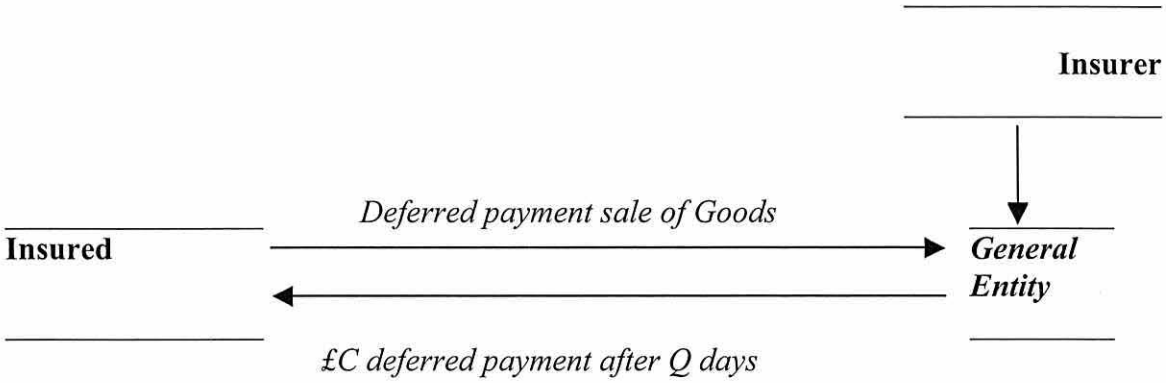
[*IJARAH* – Wages-related Contract]

Diagram 8.3: Lease-related *Ijarah* component of proposed model:



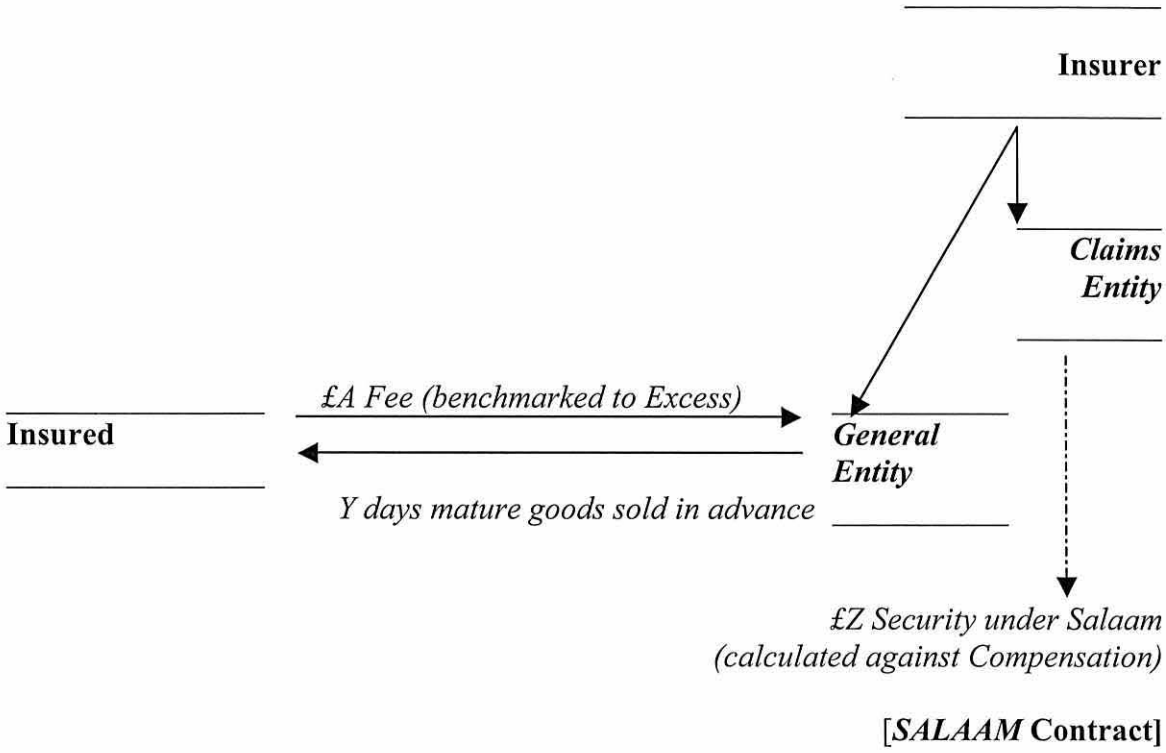
[*IJARAH* – Lease-related Contract]

Diagram 8.4: *Bai Mujjal* component of proposed model:



[*BAI MUJJAL* Contract]

Diagram 8.5: *Salaam* component of proposed model:



Part IV

A fresh new perspective towards *halal* marine insurance

Chapter 9: Conclusion

1. Introduction:

This final chapter in this thesis looks into the viability of the proposed *takaful* model. An overall structure of the whole proposed "*X3-I.M.S. fusion*" *takaful* model is shown as diagram 9.1 in the annex. The proposed model is quite an intricate structure, which had been designed to support the basic contract construction elements of insurance law, namely premium, risks, excess and compensation, but at the same time not to infringe any of the Islamic rules, particularly *riba*, *gharar* and *maisir*. However, the thesis would not be complete without a fair analysis of the adaptability and limitation of the proposed *takaful* model.

2. The adaptability of the proposed *takaful* model:

Firstly, the proposed *takaful* model can offer a number of advantages in terms of the models existing at present. To start with, the proposed model is no doubt an innovative approach to the present chaotic position of the *takaful* model. The model aims to weed out unnecessary factors such as masking the premium payment as a charity donation, to eliminating draconian concerns such as holding the participants responsible for deficits in the *takaful* organisation in any given year. Without repeating the factors that cause concern with present-day *takaful* models, the proposed *takaful* model aims to do exactly what it says on the tin, i.e. it is an insurance device where various concepts will be at play, namely premium, risks, excess and compensation. The proposed *takaful* model will work exactly the same analogy as traditional marine insurance, e.g. insurer pays insured for a valid claim and it is the insurer who is ultimately liable for the insurance business, not the novice insured.

Secondly, the proposed *takaful* model aims to assist in promotion and strict compliance of concepts such as utmost good faith, disclosure and warranties. As buying and selling takes place between the insured and the insurer in the proposed *takaful* model, the insurer obtains the opportunity to ensure that the insured has been "utmost" honest and disclosed everything so as to reflect the risk appropriately. It would not just be a subjective point of view of knowing relevant information, but all facts would be disclosed to the insurer, as the goods travel to the insurer's dominion at certain phases of the proposed *takaful* model. This, as mentioned earlier, would no doubt save a significant amount of litigation time and costs, if and when a claim needs to be made for loss of goods, thus reducing – if not eliminating, to a great extent – certain textbook defences of the insurer in claims.

The role is reversed and assists the insured as well who, although not orthodox, particularly in English marine insurance circumstances, can argue successfully concepts of utmost good faith, if the insurer aims to avoid payment of valid compensation when a claim is made. It is quite prominent in insurance litigation that the insurer aims to file a defence alleging *ab initio* void of insurance contract, arguing full nondisclosure by the insured. This would be severely eliminated under the proposed *takaful* model, as the insurer would know the goods in question very well.

Thirdly, the proposed *takaful* model is aimed to be flexible in order to satisfy the requisite matters of traditional English marine insurance contracts, as set by precedence, including the House of Lords. This includes the premium amount, as set out in *Alliss-Chalmers Co v Fidelity & Deposit Co of Maryland*[589] since, in phase 1 of the proposed *takaful* model, the insurer is already charging a fixed sum, which is even benchmarked against an orthodox premium charged to ensure correspondence. The next point being the nature of the risk, comprising the subject of the insurance as set out in *Beach v Pearl Assurance Co Ltd*,[590] which actually complies well in the proposed *takaful* model as, in phases 1, 2 and 3, the subject matter is not only being declared, but also analysed and scrutinised through

[589] Alliss-Chalmers Co v Fidelity & Deposit Co of Maryland (1916) 114 L.T. 433 at 434
[590] Beach v Pearl Assurance Co Ltd [1938] I.A.C. Rep. 3

the buying and selling processes. The final point being the risk length as set out in *Murfott v Royal Insurance Co.*[591] Here, is satisfied in the proposed *takaful* model, since the risk duration is set out from the outset in phase 1 and the duration time limits are set and are compliant as the process goes through phases 2 and 3.[592]

Fourthly, concerns have been raised by academics that present-day *takaful* are well behind the counterpart insurance in respect of equity returns and international market penetration.[593] It can be envisaged, aside from the fact that *takaful* is a new entrant in the market compared to insurance that the major concern is possibly due to the cumbersome nature of the existing *takaful* models. As will have been noted from the previous chapters, the *takaful* models have components that clash with each other[594] as they attempt to sidestep the general working method of traditional insurance due to the presence of various *Sharia* restrictions.[595] This has resulted in a disproportionate usage of various Islamic paradigms, even when they do not fit well all the time, which has produced unsuitable consequences. With the proposed *takaful* model, it is aimed that it could be utilised in the same manner as traditional marine insurance in normal markets, without the need for a great deal of change. This should assist in meeting more target markets internationally and interest more investors investing, making more equity returns of their investment, as the characteristics of both traditional insurance and *takaful* would be the same.

Fifthly, academics agree that existing *takaful* models currently denote the absence of any Islamic contract present between the parties and basically the whole matter is left to go on by itself, with the expectation that aspects such as good faith would be followed by the insured, as mentioned in Islamic law.[596] The significant problem with such approach is

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[591] Murfott v Royal Insurance Co (1922) 38 T.L.R. 334 at 336

[592] John Birds, *Birds' Modern Insurance Law* (7th edn, Sweet & Maxwell 2007) pp. – 82 - 83

[593] Haemala Thanasegaran, 'Growth of Islamic Insurance (*Takaful*) in Malaysia: A model for the region?', supra at p. - 105

[594] See chapter 5 above for details of the various *takaful* models existent at present and the problems with them

[595] See chapters 2 and 3 above which discusses about the *Sharia* restrictions of *riba*, *gharar* and *maisir*, which restricts traditional insurance to be acceptable in Islam.

[596] Haemala Thanasegaran, 'Growth of Islamic Insurance (*Takaful*) in Malaysia: A model for the region?', supra at p. - 107

that, in the present non-idealist world, without strict enforcement of regulations or consequential threats of failure of the same, it is not possible or practicable for the model to be complied with by every insured. It is submitted that such problems are alleviated in the proposed model as a thread of contractual relationships runs through the whole model, holding the parties to strict obligations. The working relationships are rigid and obligations are strict in the proposed *takaful* model. Unlike present-day *takaful* models, it is not built on anticipation; rather, it will hold parties accountable for their failure to keep up their respective obligations.

3. The limitations of the proposed *takaful* model:

Despite the innovative approach of the proposed *takaful* model, it is not without some limitations. The drawbacks of the proposed *takaful* model might assist in future development in this area, particularly if work is to expand on other types of insurance as well.

One of the limitations of the proposed *takaful* model is that it is devised for marine insurance only, for goods in marine voyage. Whilst that in itself would not be a deal-breaker, for the purpose of using the proposed *takaful* model, the insured, i.e. the seller in international trade, should retain the title to sell the goods to the insurer. In other words, although the seller can enter a contract with the overseas buyer for the title to transfer on receipt of goods at the point of destination, for the *halal* proposed *takaful* model to be used, the seller needs to retain the title of those goods at the time marine insurance is sought using the proposed *takaful* model. This is due to the fact that, during part or all of the phases in the proposed *takaful* model, the goods change ownership between the insured and insurer and, without the insured retaining the title on the goods, the proposed *takaful* model cannot be executed.

Having said that, it is not uncommon in English law to use a concept of retention of title clause. This is supported by both statute under **section 19 Sale of Goods Act 1979** and by common law under "*Romalpa*" clause. **S. 19(1) Sale of Goods Act 1979** states that:

- "*Where there is a contract for the sale of specific goods or where goods are subsequently appropriated to the contract, the seller may, by the terms of the contract or appropriation, reserve the right of disposal of the goods until certain conditions are fulfilled; and in such a case, notwithstanding the delivery of the goods to the buyer, or to a carrier or other bailee or custodier for the purpose of transmission to the buyer, the property in the goods does not pass to the buyer until the conditions imposed by the seller are fulfilled.*"[597]

This section provides the seller with a significant advantage of retaining the title of goods, even after selling to the buyer, provided set conditions are satisfied. Chitty mentions this is generally payment of the sale price,[598] but in this case there is nothing stopping the insured, i.e. seller, to set a condition of obtaining insurance under the proposed *takaful* model before title can pass. Boosting support for this is the "*Romalpa*" clause analogy, which is derived from the case of *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd.*[599] Here, the Court of Appeal held valid the contract clause for title retention and allowed the seller to retain the title of the goods until the clearing of payment by the buyer.[600] However, in the consequent precedent of *Re Bond Worth Ltd,*[601] such title retention clause was holding equitable rather than legal ownership, which required registration as a charge.[602] The effect, which is of relevance here, is that it is possible to retain title of the goods, provided it is agreed between the transacting parties.[603] With specific international trading contracts, e.g. CIF and FOB contracts, the

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[597] Legislation, 'English statute online' (legislation.gov.uk) <http://www.legislation.gov.uk/ukpga/1979/54> accessed 14 June 2014

[598] H.G.Beale (ed), *Chitty on Contracts: Volume II: Specific Contracts* (31st edn, Sweet & Maxwell: Thomson Reuters 2012) paragraphs – 43-206 - 43-208

[599] Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd [1976] 1 W.L.R. 676; noted (1976) 39 M.L.R. 585; [1977] C.L.J. 27; Chitty on Contracts supra at paragraph – 43-209

[600] Ibid

[601] Re Bond Worth Ltd [1980] Ch. 228; Ibid

[602] Ibid

[603] Chitty on Contracts, supra at paragraphs – 43-209 - 43-221

seller is considered to have held his/her right of title retention by holding on to the bill of lading.[604]

However, all is not lost with the proposed *takaful* model, or title retention by the insured, i.e. seller. The seller simply needs to retain the title of the goods during the process of obtaining marine insurance cover, using the proposed *takaful* model, which would be for a quite a short period of time. Although the goods are the seller's, i.e. insured, as they go through the various steps of the proposed *takaful* model the ownership changes hands a number of times. Nonetheless, the insured obtains the title of the goods by the time the goods set sail from the point of departure, as the proposed *takaful* model under phase 3 has the title transferred to the insured, which provides the insured liberty to transfer the title to the overseas buyer, as necessary. To make it safer, the insured (as the seller) has the independence to register his/her charge against the overseas buyer on the goods that are to go on the marine voyage, in the event that it is concluded that legal title of the goods has transferred on the agreement to sell. In that way, at least the insured, i.e. seller, can retain the equitable title and the proposed *takaful* model can still be complied with. Moreover, the "*Romalpa*" clause exists to assist and provide an extra security to the seller, which becomes a mandatory security that the seller must take on when utilising the proposed *takaful* model.

In practice, it could well be the case that the insured, i.e. seller, may have found a buyer for the goods that are to go on the marine voyage. However, before formal agreements are signed, the buyer may insist that the seller obtain all his preparatory work, e.g. finding a vessel, liaising with the bank for the bill of exchange, obtaining marine insurance cover, as otherwise the international trade cannot take place. Therefore, it could well be the case that, whether the title remains with the seller or not, it is practically irrelevant at the stage when marine insurance cover is sought. By the time the marine insurance cover, using the proposed *takaful* model, is obtained, the seller, i.e. insured, already has the title. Hence,

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[604] M G Bridge, *The International sale of goods* (3rd edn, Oxford University Press 2013) paragraphs – 7.07 – 7.10

the effect of using the proposed *takaful* model, with title movement between insurer and insured, should unlikely be adversarial in practice.

Secondly, it is no using masking the fact that the proposed *takaful* model is somewhat complex with a number of phases that are fused together rather than mixed up, unlike present-day *takaful* models. This, at first glance, may make the proposed *takaful* model difficult to appreciate; however, after consideration of the existing conditions, it was a drastic situation that required a drastic model to originate.

Thirdly, another concern that may be raised is that the overseas buyer would want to sell the goods en route to another buyer, as is norm in international trading. The proposed *takaful* model, under phase 3, uses the *Bai Salaam* instrument, i.e. forward sale instrument, which passes the title to the seller, i.e. insured, and the insured then has the flexibility to enter a parallel *Salaam* contract with the buyer overseas. The buyer overseas can have the flexibility of entering a parallel *Salaam* contract with another buyer overseas and so on and so forth. This has been discussed in previous chapters.[605] The query that may arise is that, with a parallel *Salaam,* it is a promissory agreement that is entered into but with the restriction of no payment made until receipt of goods. This may appear to be contrary to international trading at first glance; however, upon a deeper analysis, it could be an achievement to save significant time and costs in litigation when matters go wrong. If goods are received safely at the point of destination by the insured, i.e. seller, then there is nothing wrong or *haram* in him/her receiving payment from the buyer, as there was already a promissory agreement. The same applies for the overseas buyer selling to another overseas buyer, with the use of a promissory agreement as well. In this case, as matters have worked out well, there is no claim to make and the proposed *takaful* model follows its natural cycle, as discussed in this thesis.

On the other hand, should a catastrophe take place during the marine voyage, and the goods at the time of the loss were in the possession of the designated carrier, the insured, i.e. seller, can make a claim against the insurer for the losses under the proposed *takaful*

[605] See chapter 6 above

model. However, the overseas buyer, at best, will have a claim against the insured, i.e. seller, for failing to keep his/her obligation under the promissory agreement. No funds will have been transferred, therefore there is no money claim per se to handle for recovery. The same goes for the overseas buyer selling to another overseas buyer. This would not stop the overseas buyer from denying his right of litigation; but, at the same time, time and costs of litigation would be managed and controlled, mainly in light of the recent Jackson reforms that are storming through English Civil Procedure Rules.[606] Also, such a parallel *Salaam* contract provides the facility of avoiding the Islamic restrictions of *riba*, *gharar* and *maisir*, since no final transaction has taken place; rather, there would be a promissory agreement, which will bear its weight under jurisdictional law but would also be safe under *Sharia* law. Therefore, it is submitted that such a compromise is worth its value in gold when looking at the overall scenario in its fullest.

Fourthly, it can be argued that the proposed *takaful* model restricts the possibility of arguments of invitation to treat, offer and counteroffer. Whilst at the outset it may appear so, it could be argued that such elements presented in English marine insurance law are not compromised at all. Phase 1 of the proposed *takaful* model is dependent on the insurer and insured negotiating on the premium amount and parties are welcome to make offers and counteroffers in response. In fact, in the proposed *takaful* model, there are more security features as the process has three separate contracts, which provide the parties with more room for negotiation, depending on the state of the goods in question. This provides more flexibility as parties inspect the source of risk, i.e. goods, all the way through, with the option for any party to pull out should they conclude that the other party has not practised utmost good faith to its highest level, an aspect which sadly becomes a major issue during litigation.

[606] At present time, the English Civil Procedure Rules are going through changes in litigation to control time and costs of litigation. The Jackson reforms, which came in force from 1st April 2013, made provisions so that budget of litigation is controlled. This is not the aim of this thesis to look into Jackson reforms but it is certainly a point to consider for proposed *takaful* model when insurance mattes includes claims which end up in litigation most times, when disputed. The proposed *takaful* model aims to control litigation and in compliance with the practicality of the changing circumstances.

Fifthly, it may be argued that the proposed *takaful* model is not strictly a *takaful* as it is expected to represent cooperativeness and mutuality as are prevalent in current *takaful* models. It is opined that, whilst looking at the insured and insurer relationship singularly, it may appear that it is just a one-to-one liaison, but insurance is not an individual trait business. The amount of premium charged to the insured would be dependent not just on subjective factors of the individual insured marine voyage circumstance, but also the factor of risk spread by the insurer under the principle of law of large numbers.[607] In that respective, it is safe to suggest that the proposed *takaful* model is a cooperative vehicle, as the premium figure could not be succumbed in the absence of various insured taking over the cover and making the premium payment.

Finally, one of the issues that runs throughout this thesis – and, in fact, has led to the creation of three separate contracts for the proposed *takaful* model – is the hypothesis that two sales in one sale is disallowed in Islam.[608] This is due to the presence of *riba* and *gharar* as a result of unjustified increase and uncertainty. An issue against the proposed *takaful* model is the concept of *Al-Inah*. *Al-Inah* is a somewhat controversial concept since one of the major schools of thought, the *Shafi* School, has allowed validity, but unfortunately this view is not shared by other schools. Concept of *Inah* involves situations where one transaction takes place on a deferred payment basis, followed by another transaction between the same parties on buy back of same item, on lower sum or deferred payment in less time.[609] *Inah* has been defined in an Exposure Draft of Bank Negara Malaysia, Central Bank of Malaysia as:

- *"Bai` `inah refers to an arrangement that involves sale of an asset to the purchaser on a deferred basis and subsequent purchase of the asset at a cash*

[607] See chapter 4 above where arguments for and against about Islamic law restrictions applicability on insurance and theory of LLN is mentioned
[608] See chapter 6 above
[609] Mohammad Hashim Kamali, *Islamic Commercial Law: An Analysis of Futures and Options* (Islamic Texts Society 2010), p. – 132

price lower than the deferred sale price or vice versa, and which complies with the specific requirements of bai` `inah."[610]

Bank Negara Malaysia in their Exposure Draft gave circumstances of an *Inah* transaction, which are nicely exemplified by scholar, Mohammad Hashim Kamali, as follows:

- "*A sells a garment to B for 100 dinars, payable in one month, and then buys from B the same or a similar garment for 120 dinars, payable after two months.*"[611]

- "*A sells the garment to B for 100 dinars, payable in six months and then B, who may or may not take delivery, sells it back immediately to A for a prompt price of 80 dinars.*"[612]

The reluctance of jurists under *Sharia* law regarding the above situations, which is considered to be *Inah,* is because it is seen as an unjustified increase of funds without doing anything and, as such, the issue of *riba* steps in, while other jurists consider *Inah* to be unacceptable under the debt clearance sale; as such, *gharar* becomes relevant due to the uncertainty.[613] However, as mentioned above, the *Shafi* School approves *Inah* and, from the Exposure Draft, it appears that Bank Negara Malaysia recommends it as well. Bank Negara Malaysia quotes a number of Islamic texts in support, including practices of Prophet Mohammed (pbuh) to use money in transactions to avoid *riba,*[614] but does not explain the *hadith* about its relevance with *Inah.*[615]

Nevertheless, irrespective of the controversy regarding the allowance of *Inah* under *Sharia* law, it is asserted that, in the proposed *takaful* model, the *Inah* concept is very

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[610] Bank Negara Malaysia: Central Bank of Malaysia 'Bai``Inah (Shariah Requirements and Optional Practices): Exposure Draft' (2013) paragraph – 7.1 <http://islamicbankers.files.wordpress.com/2013/12/2013-ed-bai-inah.pdf> accessed 14 June 2014

[611] Mohammad Hashim Kamali, supra at p. – 126

[612] Ibid

[613] Sale of debt is quite a controversial area under Islamic law and there is no enough scope in this thesis to discuss about debt sale arguments. Mohammad Hashim Kamali, supra at pp. – 126 - 127

[614] See chapter 5 above footnotes 53 - 55

[615] Bai``Inah (Shariah Requirements and Optional Practices): Exposure Draft, supra at paragraphs – 18.1 – 18.5

unlikely to be applicable, since each of the contracts has been carefully implemented to be distinct and there is no unjustified increase or uncertainty in the transactions. Keeping in line with the variable, which is prevalent in this thesis, when in phase 2 the goods are sold under a deferred sale basis for £C by the insured to the insurer, the parties are clear on their responsibilities and, in fact, the insured is willing to give up his claim of £C if the insurer does not provide the fund in a certain number days as charity, which is strongly encouraged in Islam. In phase 3, a phase shorter in time than phase 2, the forward payment sale is for £A, where £A and £C have the same value. As there is no difference in value there is no issues of unjustified increase. Also, all parties are clear in their obligations in phase 3, so there is no uncertainty or chances. Along the same lines, as the value is the same, the consequent effect is the same as that of *quad hasan,* i.e. gratuitous loan, of the monetary exchange, in that no increase or decrease is taking place. As would have been noted from previous chapters, all existing *takaful* models have an element of *quad hasan* built into them,[616] hence the proposed *takaful* model is closer to the current *takaful* model's analogy in essence. In fact, it would be much better to argue further that the proposed *takaful* model goes the extra mile as, in phase 2, the concept of *sadaqah,* i.e. charity, is included, which allows the waiver of the funds, a hypothesis which is actively encouraged in Islam.

Moreover, although it may appear a farfetched idea, the goods in phase 3 are not the same goods as in phase 2.[617] Phase 3 goods are Y days matured goods, which are different than the goods sold on a deferred basis under phase 2. Therefore, in the proposed *takaful* model, there is no concern over an unjustified increase and there are different goods transacting in phase 2 and phase 3, with no uncertainty. Therefore, it can be safely argued that *Inah* should not be a concern for the proposed *takaful* model.

In conclusion, it is stated that traditional insurance had never been viewed liberally by the Islamic community and, rightly or not, had always been viewed as a contentious hazard. It is not disputed that elements of *riba*, *gharar* and *maisir* are not aspects of concern but

[616] See chapter 5 above
[617] See chapter 7 above

in fact they are very much live contentious issues which needs cautious and appropriate handling. Having said that, the right balance needed to be struck between careful handling of the restrictions whilst keeping intact the functionalism of insurance. The existing models of *takaful* were simply excessively concerned about trying to play hide and seek with the prohibitive blocks of Islamic law; as a result, attention appears to be lost in regards to the principle aim of requiring insurance, which is for the safeguarding of the prospective insured. Without risk of repeating the detailed analysis of what had been discussed earlier,[618] the hand that was supposed to feed gets bitten with the existing *takaful* models, so as to speak. The ultimate risks with the existing *takaful* models are that the insured takes on the risks, not only with regards to himself, but for the whole *takaful* operation. Clearly, this could not be the correct operational ideology of an insurance concept, where the aim is the application of both contract and tort principles for governing their relationship and protection of the insured by controlling risks, and not the other way round.

It is the opinion of this thesis that the balance can be achieved, which requires a different tactic for the satisfaction of both contractual and tortious concepts and, in fact, that is what the proposed *takaful* model in this thesis has tried to achieve. Scholars have expressed the need for a common platform between traditional insurance and *takaful* and have mentioned legal reforms playing an important role.[619] The proposed *takaful* model aims to assist with such advancement and ensuring that elements of insurance, namely premium, risks, excess and compensation, are satisfied.

4. Conclusion:

Following consideration of the above, concerns may be raised about the various stages that the proposed *takaful* model has to go through. After all, as this research had been cornered with the English insurance law in mind, it may be questioned whether there is,

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[618] See chapter 5 above where various existent *takaful* models are discussed with their respective fundamental lacking

[619] Haemala Thanasegaran, 'Making an entrance – Can Australia contribute to *takaful* (Islamic insurance) law reform?' (2013) 24 Insurance Law Journal, p. – 118

in fact, any interest for *takaful* at all in the United Kingdom. The AAOIFI (Accounting, Auditing and Governance standards for Islamic financial institutions) defines that "*Islamic insurance is a system through which the participants donate part or all of their contributions which are used to pay claims for damages suffered by some of the participants. The company's role is restricted to managing the insurance operations and investing the insurance contributions*" (Rabiah Adawiah Engku Ali and Odierno, 2008).[620] Therefore, as long as, in any *takaful* model, the funds donated by the participants are to cover part of the claims and the insurer is involved in the insurance business, along with the fund investment, it would be safe to state that the definition of the Islamic insurance is complied with. It is argued that this has been complied with in the proposed *takaful* model.

In a study conducted by Dar (2005), it was found that only 5% of UK Muslims are actually interested in Islamic finance services, while 83% of UK Muslims do not believe that existing Islamic services are actually *halal*. Although *takaful* had seen significant growth worldwide with 23 functioning *takaful* companies in July 2006, there were only two *takaful* insurers ever to exist in the UK, namely Salaam Halal Insurance and Muslim Insurance Services,[621] but only 13% of UK residents were aware of the existence of these organisations.[622] An empirical study conducted by Tahani Coolen-Maturi and Dar (2005) found that residents of North or Central England are more inclined to buy *takaful* services than in other parts of the country.[623] Authors such as Tahani Coolen-Maturi stated that *takaful* is still in its early stages in the UK and discussed increasing awareness among Muslims as to its existence.[624] However, both of the above-mentioned insurance *takaful* organisations that started back in 2008 have now ceased trading, with Salaam Halal Insurance ending in 2009 and Muslim Insurance Services ending in 2011.

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[620] Tahani Coolen-Maturi, 'Islamic insurance (*takaful*): demand and supply in the UK' (2013) Vol. 6, No. 2, International Journal of Islamic and Middle Eastern Finance and Management, ISSN: 1753-8394, p. - 89
[621] Tahani Coolen-Maturi, supra at pp. – 90 - 91
[622] Tahani Coolen-Maturi, supra at pp. – 100 - 101
[623] Tahani Coolen-Maturi, supra at pp. – 94 - 98
[624] Tahani Coolen-Maturi, supra at p. – 102

This, no doubt, leaves a somewhat mixed message as to whether the community, particularly the Muslim community, has developed a level of appreciation of an alternative to traditional insurance. It is opined that the negativity surrounding the acceptance of traditional insurance among the Muslims is not due to the fact that insurance itself is not allowed in Islam, as has been witnessed previously, despite a number of different scholarly opinions. Rather, the reluctance exists due to the presence of various restrictions in traditional insurance contracts. The desertion of orthodox insurance by Muslims was due to the issues of *riba*, *gharar* and *maisir*. The big concept of *riba,* of inequality of premium and compensation, remains at large and there is no doubt that the restriction of *riba* is taken seriously by Muslims. The verses in the *Quran* and *Hadiths* have already been mentioned regarding the severe consequences of taking *riba*. To exemplify the extreme severity of *riba*, reported by Abu Hurayrah and as stated in the *hadith* of Ibn Majah, the Prophet Mohammed (PBUH) mentioned that:

- "*Riba has seventy segments, the least serious being equivalent to a man committing adultery with his own mother.*"[625]

This in itself makes the situation abruptly clear on how significant the warnings are, that God has sent, to avoid any involvement with anything to do with *riba*. *Riba* has severe alarms ringing around it and Muslims with knowledge of these prohibitions would simply stay away from activities that concern the same. Along the same lines, the concept of *gharar* and *maisir* has also been emphasised in previous chapters. Without repeating further, *gharar* simply has no room to coexist in *halal* transactions, but its presence would be felt as long as the parties' obligations are unclear. Abu Huraira reported that the Prophet Mohammed (pbuh) mentioned:

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[625] Abdulkader Thomas, Stella Cox and Bryan Kraty, *Structuring Islamic finance transactions* (Euromoney Books 2005) p. – 21 <http://books.google.co.uk/books?id=u04Ehd2FusgC&pg=PA21&lpg=PA21&dq=hadith+on+riba+has+seventy+segments&source=bl&ots=5lHfPNDSNV&sig=ffsbgdvrzXWKmrvJCplNh18X7AQ&hl=en&sa=X&ei=RVjiUsWbHuGK7AaUlIHIAg&ved=0CFUQ6AEwBg#v=onepage&q=hadith%20on%20riba%20has%20seventy%20segments&f=false> accessed 24 January 2014

- *"Do not meet the merchant in the way and enter into business with him, and whomever meets him and buys from him, then should the merchant [find a better price] in the market when he arrives, has the option [to rescind the original transaction]."*[626]

As the above *hadith* makes it apparent, the parties are discouraged from entering into transactions where everyone is not crystal clear on the contractual obligations and consequences. Worse still, should such transactions take place, the seller is under liberty to hold the contract as void on his own volition of lucrative circumstances. This could have a highly adverse effect on insurance contracts, particularly marine insurance contracts, where the insured is faced with huge liabilities following loss of casualties. In a well-known verse of the Holy *Quran* in *Surah Al-Kahf* (Chapter 18), relating to incidents about a group who fled and remained in a cave, from their non-Islamic community to avoid worshipping anything other than Allah, there was confusion as to how long they had been there and how many there were in the group. It has been mentioned in *Surah Al-Kahf* (Chapter 18), Verse 19 that:

- *"And similarly, We awakened them that they might question one another. Said a speaker from among them, "How long have you remained [here]?" They said, "We have remained a day or part of a day." They said, "Your Lord is most knowing of how long you remained..."*[627]

The answers regarding the length of time the group spent in the cave are provided in the same *Surah Al-Kahf* (Chapter 18), Verses 25 and 26:

- *"And they remained in their cave for three hundred years and exceeded by nine."*

- *"Say, "Allah is most knowing of how long they remained. He has [knowledge of] the unseen [aspects] of the heavens and the earth. How Seeing is He and how*

[626] Abdulkader Thomas, Stella Cox and Bryan Kraty, supra at p. - 23
[627] Holy Quran, 'Surah Al-Kahf' Chapter 18 Verses 22 (quran.com) <http://quran.com/18> accessed 7 March 2014

Hearing! They have not besides Him any protector, and He shares not His legislation with anyone.""[628]

The above verses highlight the fact that God knows best on everything and has warned human beings not to blindly speculate on matters on which they are unsure. As can be noted, the speculation on the number of years the group spent in the cave was not even close to the correct amount of time spent; it is an admonition for Muslims to avoid such guessing circumstances, but to be sure. Further in the same chapter in *Surah Al-Kahf* (Chapter 18), Verse 22, it is mentioned that:

- *"They will say there were three, the fourth of them being their dog; and they will say there were five, the sixth of them being their dog - guessing at the unseen; and they will say there were seven, and the eighth of them was their dog. Say, [O Muhammad], "My Lord is most knowing of their number. None knows them except a few. So do not argue about them except with an obvious argument and do not inquire about them among [the speculators] from anyone."*"[629]

As can be derived from the above verses, although not relating directly to financial transactions, it is very clear that, under *Sharia* law, guess-working is discouraged without concrete evidence. The same analogy is again repeated, in that speculation should be avoided unless corroborated, and that such instruction is not just relevant to economic aspects, but also to social life. References have been made in the Holy *Quran* to aspects of labour and compensation and it has been stated in *Surah Ali Imran* (Chapter 3), Verse 185 that:

- *"Every soul will taste death, and you will only be given your [full] compensation on the Day of Resurrection. So he who is drawn away from the Fire and admitted*

[628] Ibid
[629] Ibid

to Paradise has attained [his desire]. And what is the life of this world except the enjoyment of delusion."[630]

As can be understood from the above verse, the journey is set during a lifetime in this world and is a voyage that everyone has to go through and, depending on whether good or evil actions are committed during this voyage, everyone will receive their due compensation. Evidently, this is the position with the natural life of human beings, but the aspect to consider is that compensation, i.e. either heaven or hell, is dependent on the performance in this worldly life. Everyone will be judged independently according to his/her actions in this lifetime on the Day of Judgement. Therefore, the analogy of an individual aspect links to an individual risk coverage, as compensation is due on an individual basis on what one does for himself/herself. Hence, whilst in a cooperative scheme, everyone comes into the whole picture as with natural life or insurance, each policy has to be tailored on an individual basis rather than one size fits all under the cooperativeness argument, as is the case with present-day *takaful* models.

It is crucial to consider the whole angle, to perform and lead one's life, including financial transactions, within God's set laws. It has been mentioned time and time again, in both the *Quran* and *hadiths,* the importance of keeping away from the various *Sharia* restrictions. At the end of day, by Muslim beliefs, it is God who will judge human beings, both on their actions and their intentions. The aim of this project has been to suggest a proposed *takaful* model that would work within the ambits of Islamic law and existing jurisdictional law, from a marine insurance perspective. It is mentioned in *Surah Al-Baqarah* (Chapter 2), Verse 256 that:

- *"There shall be no compulsion in [acceptance of] the religion. The right course has become clear from the wrong..."*[631]

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[630] Holy Quran, 'Surah Ali Imran' Chapter 3 Verses 185 (quran.com) <http://quran.com/3> accessed 8 March 2014

[631] Holy Quran, 'Surah *Al-Baqarah'* Chapter 2 Verse 256 (quran.com) <http://quran.com/2> accessed 8 March 2014

The relevant point is that the proposed *halal* model is not on a mission to compel Islamic law onto any jurisdictional law and change the latter's nature. The proposed model aims to sit alongside and work as analogously as possible with jurisdictional law, but maintaining the ethos of Islamic faith at the same time. Rather than swerving with indecisiveness regarding the validity of insurance in Islam, as is presently the situation among *fuqaha*, a set decision needs to be made about insurance legality in Islam. Insurance is either the right course in Islam or not, in line with the above verse, and it is opined that there is nothing in Islam that restricts insurance from being acceptable, both as a concept of assisting individuals by controlling risks and as a commercial venture as profits in return for such specialist service. The concern at heart had been about the creation of a suitable model and it is submitted that the proposed model clearly meets those *Sharia* acceptable paradigms, which are *halal.*

The problem that has occurred with existing models, as has already been discussed, is that various components had been taken and added together to make different models of *takaful*. In some *takaful* models, *tabarru* is mixed with *mudarabah,* or *tabarru* mixed with *wakala,* or *tabarru* mixed with *mudarbah & wakala,* while a recent model is *tabarru* mixed with *waqf, mudarbah & wakala*. The issue that needs to be addressed is that, just because various instruments work well independently in Islam, it does not mean they can be mixed together and the end result will also be *Sharia* acceptable. Each of the instruments has its own nature and scope of action, such as *tabarru* scope in the social field, *wakala* scope in the financial ground. An amalgamation of varieties would not produce the expected outcome and the message is loud and clear from the results that are being witnessed from the present-day *takaful* models. This amalgamation aspect is very important with *Sharia* law, as it is quite a sensitive area with boundaries set by God's laws.

One analogy to digest on could be likening an existing *takaful* model with an alcoholic drink, such as wine. Wine is the product of grapes and water, each of which can be consumed in Islam. However, when these are combined and fermented, the end product is simply *haram* in Islam and no amount of justification can make it acceptable, as wine is

an intoxicant. God has warned, as mentioned in earlier chapters, in the Holy *Quran* in *Surah Al – Ma'idah* (Chapter 5), Verse 90, that:

- *"O you who have believed, indeed, intoxicants, gambling, [sacrificing on] stone alters [to other than Allah], and divining arrows are but defilement from the work of Satan, so avoid it that you may be successful."*[632]

A similar restriction about wine had been mentioned in the Holy *Quran* in *Surah Al – Baqarah* (Chapter 2), Verse 219, where it is stated that:

- *"They ask you about wine and gambling. Say, "In them is great sin and [yet, some] benefit for people. But their sin is greater than their benefit." And they ask you what they should spend. Say, "The excess [beyond needs]." Thus Allah makes clear to you the verses [of revelation] that you might give thought."*[633]

The admonition from God cannot be any clearer about the parameters set for human beings. The current positions of the existing *takaful* models are, rather sadly, such scenarios. However, it is put forward that the proposed *takaful* model does not fall under the same precept, as the structure has been divided into three separate contracts and phases, with each of the cogs set to run independently without being totally interdependent. The result produces the expected outcome and each of the instruments is at liberty to work its own course, without clashing with each other. Each component maintains its own nature and works in parallel rather than mixed together, but simply shares a common platform to work on. Therefore, to use the analogous example, the end product of the proposed model is grape juice rather than wine!

From a different perspective, as mentioned above, one of the restrictions set in Islam is that two contracts cannot be present in one transaction, or that two contracts cannot be interdependent on one another in a single transaction; hence, it is necessary for each of

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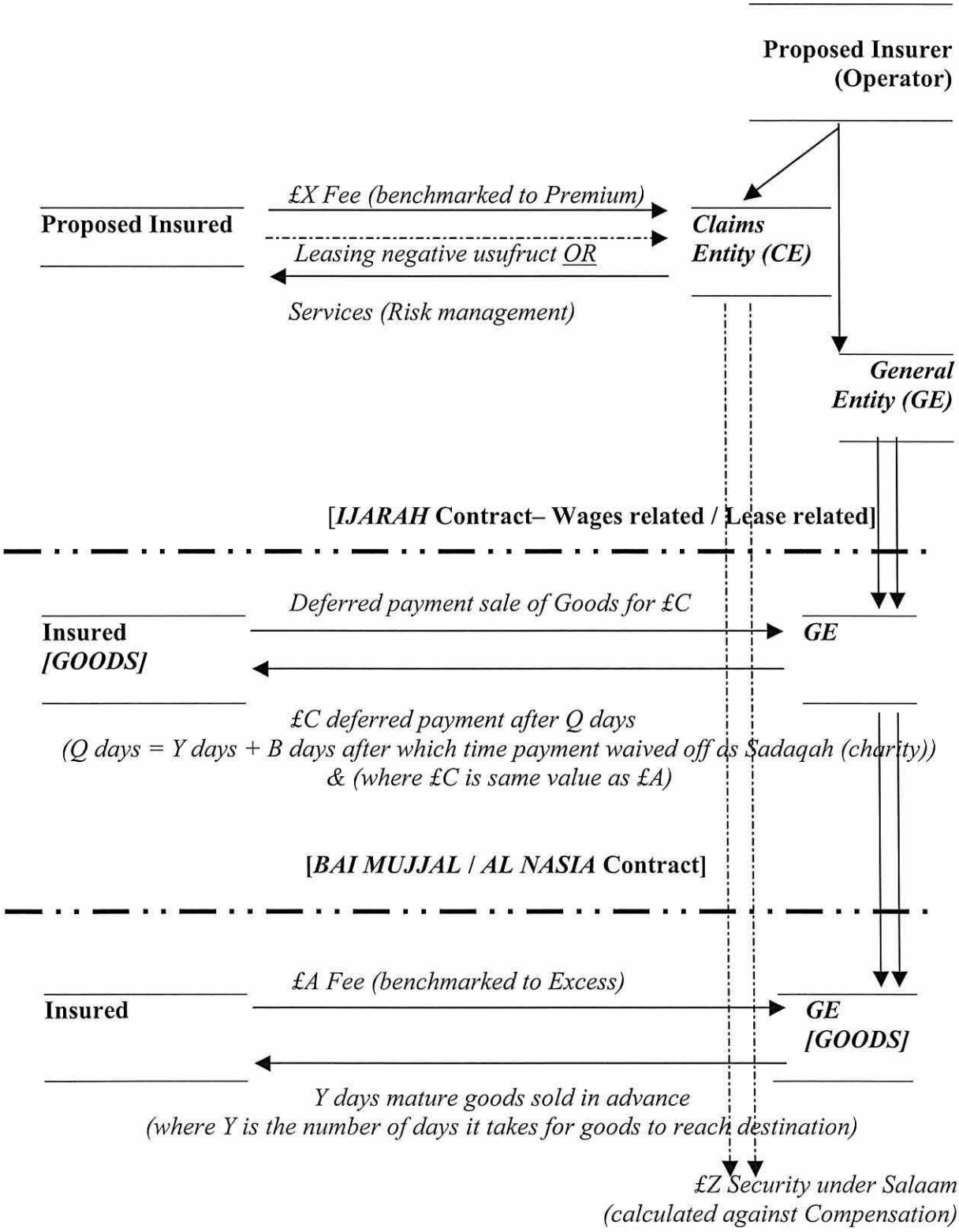
[632] Holy Quran, '*Surah Al – Ma'idah*' Chapter 5 Verses 90 and 91 (quran.com) <http://quran.com/5> accessed 9 March 2014

[633] Holy Quran, '*Surah Al – Baqarah*' Chapter 2 Verse 219 (quran.com) <http://quran.com/2> accessed 9 March 2014

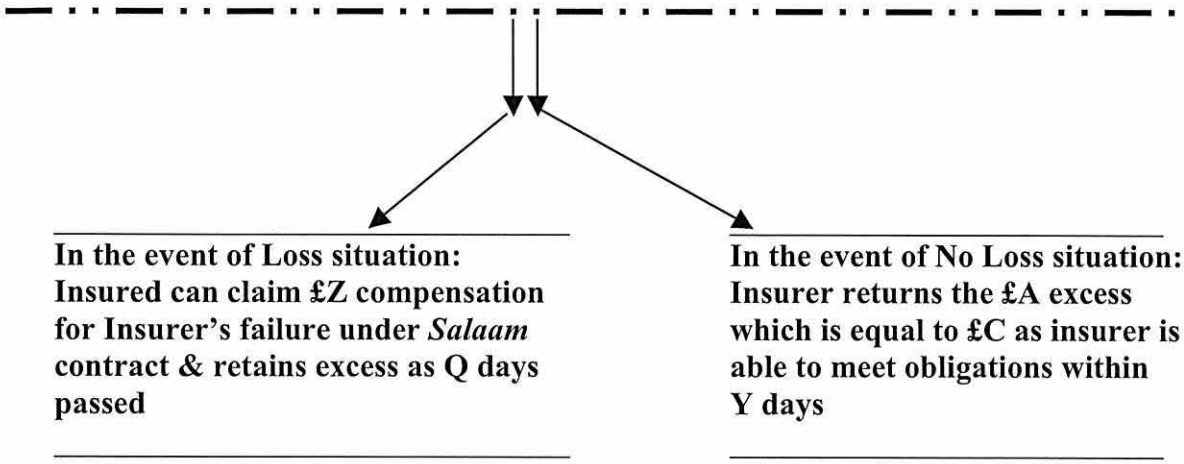
the contracts to work by by itself. This raises the question whether the existing *takaful* has this restrictive characteristic. In existing *takaful* models, there are various concepts that are blended together to produce one transaction and, if either of the concepts are taken off, such as *waqf*, the remainder of the whole of the *takaful* model falls through. Although it had been structured that concepts such as *tabarru* and *waqf* are social instruments, the way they are utilised in the *takaful* models is such that they behave as commercial instruments, so this raises the concern whether the mentioned prohibition is in play in existing *takaful* models.

Conversely, in the proposed *takaful* model, as pointed out earlier, all of the three instruments are working independently without reliance on one another. This allows each of the financial instruments to survive effectively by itself, when the instruments commence and conclude their lives; in the proposed *takaful* model, the *Ijarah* contract is not dependent on the *Bai Mujjal* contract, neither is the *Bai Mujjal* contract dependent on the *Bai Salaam* contract. Each of these three contracts is simply a phase or cog in the overall machine, but all of them work autonomously and automatically by themselves. With this in mind, this thesis concludes by saying that the proposed *takaful* model is compliant with Islamic rules and English marine insurance underlying principles. It is anticipated that this thesis will form the basis for future work on *takaful*, expanding to other areas of insurance for the development of innovative models for the progression of Islamic finance in the modern world.

Diagram 9.1: The proposed "*X3-I.M.S. fusion*" *takaful* model:



[*SALAAM* Contract]



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