

# **The Islamic view on Insurance: Types, Rulings and Models**

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فَمَنْ كَانَ يَرْجُوا لِقَاءَ رَبِّهِ فَلْيَعْمَلْ عَمَلًا صَالِحًا وَلَا يُشْرِكْ بِعِبَادَةِ رَبِّهِ إِنَّهُ

**"So whoever hopes for the Meeting with his Lord,  
let him work righteousness and associate none  
as a partner in the worship of his Lord."**

The Noble Qur.aan - Soorah al-Kahf, Aayah 110

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بِسْمِ اللّٰهِ الرَّحْمٰنِ الرَّحِیْمِ

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*Many people ask about the Islamic ruling for contemporary forms of insurance, as well as related schemes such as product warranties and guarantees. This humble paper has been written to shed some light on this very important topic...*

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In the name of Allah, the Most Merciful, the Bestower of Mercy. All praise is for Allah, the Lord of the Worlds. May peace and blessings be upon our Prophet Muhammad, his family, companions and those who follow his guidance.

Insurance based transactions are increasingly relevant to various spheres of life, with personal, business and property insurance becoming more and more common. Many people ask about the Islamic ruling for contemporary forms of insurance, as well as related schemes such as product warranties and guarantees. This humble paper has been written to shed some light on this very important topic, compiled from the Fataawa and research carried out by the scholars of Islam.

## An Introduction to Insurance

The primary objective of insurance is to financially compensate for any form of unexpected loss or harm - financial or otherwise.

The concept of insurance is based upon a pooling of funds from many entities to compensate a loss which may be suffered by a smaller number of entities i.e. a large number of people pay into a central fund to compensate the loss of a small number of people. Because the pool of funding is taken from a large number of entities, it is enough to cover financial losses, assuming that only a fraction of those people require compensation. Due to the sheer amount of funds collected, the insurance company can compensate a loss much greater than the amount an individual has paid in.

Based on the above, the parties involved in insurance transactions are:

1. The insurer: a person, company or organisation which collects funds and in exchange promises to underwrite (i.e. compensate) the loss.
2. The insured: Often referred to as the 'policy holder' i.e. the person or company who pay a specified amount with the understanding that any loss will be compensated for.
3. The policy: This is the actual contract between the policy holder and insurer, wherein the payment and amount of compensation are agreed. There may be other different levels of compensation stipulated by the policy, as well as applicable scenarios.

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## Types of Insurance

The scholars of Islam have categorised insurance into two primary types:

1. At-Ta'meen At-Tijaaree: This is commercial insurance whereby there is profit and loss for the insurer, therefore it is a contract of trade and transaction.
2. At-Ta'meen At-Ta'aawunee: This is cooperative insurance, this model is based upon charitable cooperation, there is no profit or loss and therefore it is not considered as trade.

### **First Type: At-Ta'meen At-Tijaaree (Commercial Insurance)**

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#### Definition

This is a contract which obligates the insured party (i.e. policy holder) to pay a set fee to the insurer, with the agreement that any loss will be financially compensated to a level. The policy holder is seen as a client or customer who is buying a contract, and it is a commercial transaction because the insurer is trying to make a profit.

#### Types & Schemes

Commercial insurance schemes are available to insure almost anything, including:

- Life: In the event of a death, family members will be compensated so funeral costs can be covered.
- Health: In the event of disabilities, the policy holder will be compensated as he may need to leave work.
- Body parts: For people who have a heavy reliance on a particular part of the body such as sports stars or celebrities, they will receive compensation if that body part is injured.
- Residual debt insurance: Known as payment protection or credit insurance, wherein a debt will be covered by the insurer in the case of death.

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- Cars, houses, phones etc: If one's property is damaged due to his own fault and/or other people's fault, some form of compensation will be afforded to the owner(s) of the item.
- Employees and Public: If an employee or a member of public is injured due to the policy holder's business, compensation will be paid.
- Pets and animals: Veterinary costs will be compensated for if one's pet becomes diseased.

In all the above schemes, the policy will detail when, how much and for what the compensation will be given as well as exemptions to

## Islamic Ruling

All forms of commercial insurance are Haraam (Prohibited) in the Sharee'ah; if a policy has been agreed it would be annulled by an Islamic court.

Note: In many countries, some form of car or medical insurance is a legal requirement, in which a person does not have any other option. In such cases, it is permitted for a person to take out the minimum level of insurance which he is legally bound to do so.

## Evidences

Amongst the factors for which the Sharee'ah prohibits a transaction, is the presence of:

1. Jahaalah: An ambiguity whereby the price, merchandise or service is very ambiguous.
2. Gharar: A large extent of uncertainty in receiving the merchandise or the price required.
3. Dharar: Harm to any of the parties due to the transaction.

The first two factors render a transaction speculative, which can then easily lead to fraud and cheating. Islamically, when a transaction is conducted, both the price and the merchandise being purchased must be specific and quantified.

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In commercial insurance, both Jahaalah (ambiguity) and Gharar (uncertainty) are present, in fact they are very much intrinsic to insurance. This is because insurance is dependent upon unforeseen loss and risk. An accident is only a probability, it is speculative and even the nature and financial cost of an accident is speculative. The customer pays a set fee however he may never suffer any loss and therefore not require compensation; or he may receive compensation much greater than what he has paid; conversely, he may receive compensation much less than what he has paid; this results in Dharar (harm and loss). Even if he agreed to the above possibilities, the transaction remains Haraam.

The ambiguous and speculative nature of insurance leads to many instances of fraud and exploitation, sometimes from the insurer who will refuse or delay payment or from the policy holder who will make fraudulent claims. All the above has been forbidden in Islam,

The Prophet (sal Allaahu alayhi wa sallam) specifically “forbade any speculative transaction.”<sup>1</sup>

Also Allah, the Wise, said:

**{O you who have believed, do not consume one another's wealth unjustly but only [in lawful] business by mutual consent}**<sup>2</sup>

Many commercial insurance companies make large profits, dictating market prices to ensure they maintain such profits; the public are forced to accept this as they have no other choice. In addition to the above, insurance companies may invest policy holders' money to further their own profits and/or place the money in interest-paying bank accounts. This then becomes a clear case of Riba (Usury and interest). The policy holder may well be compensated from the interest alone, and the rest is profit for the insurance companies.

In reality the above only reiterates the fact that the existence of insurance is a mechanism of pure capitalistic gain and often preys on the misery of the public.

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<sup>1</sup> Narrated by Abu Hurayrah; Collected by Muslim

<sup>2</sup> The Noble Qur'aan 004:029

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Much worse than the financial uncertainty, ambiguity and loss that people suffer is the effect it can have upon their Imaan (faith). In cases of life insurance, a person places his dependence upon the insurer as opposed to having Tawakkul (Reliance) upon Allah and accepting His wisdom in what He decrees.

## **Second Type: At-Ta'meen At-Ta'aawunee (Cooperative Insurance)**

This is an agreement in the spirit of cooperation and collective responsibility in which a group of people agree to contribute a set amount to a central fund, which will be used to alleviate any loss or facilitate an emergency of any one of the contributing members. The funds are collected by a committee of people or trustees and placed into a holdings account.

Crucially, no party makes a profit or a loss, there is no transaction of purchase; there is only a mutual agreement to contribute to a fund to help each other. Each person is a shareholder of the central fund, and there is no customer.

Note: Any such scheme would require a committee which manages the fund, and it is permitted for the management committee to take a fee for their role in management. However, this fee is defined and is not taken from the central fund; the fee does not increase or decrease as profits and investments do, rather it is a set administrative fee.

### Types & Schemes

Although cooperative insurance schemes are almost non-existent on a national or governmental scale, they can often be found on a local community level between friends and families, and sometimes under the auspices of a Masjid.

Common examples include:

- **Funeral Committees:** The heads of a household agree to pay a contribution to a central fund which will be used to cover the expenses of a funeral for the contributor and his dependants from his household.

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*Crucially, no party makes a profit or a loss, there is no transaction of purchase; there is only a mutual agreement to contribute to a fund to help each other. Each person is a shareholder of the central fund, and there is no customer.*

”



- Student Health: The parents of a school agree to pay an annual contribution to a central fund which will cover any medical care expenses of a student from that school. Sometimes this is done in partnership with the school, local government or the Ministry of Health.
- Medical Insurance: A government run scheme wherein members of the public can contribute towards a non-profit central fund, which covers them for future medical costs.
- Pension funds: The government gives an option to the public to contribute towards a central fund to fund pensions when the donors retire from work.

This model of cooperative insurance could work to cover almost any loss or risk – at least on a conceptual level - assuming the relevant standard of procedures, transparency and governance.

#### Islamic Ruling

This type of insurance is Halal (Permitted) according to the Sharee'ah, because it is free of any prohibiting factors and secondly it is not a commercial transaction in which there is profit and loss, rather it is based upon collective responsibility and cooperation. Such forms of community initiatives are encouraged in Islam, as Allah said:

**{And cooperate in righteousness and piety, but do not cooperate in sin and aggression} <sup>3</sup>**

Such initiatives are also encouraged in Islam because they foster ties of brotherhood and contribute to the prosperity of a single Ummah in which there is mutual compassion and care for each other.

In this regard, the Prophet (sal Allaahu alayhi wa sallam) said, "The parable of the believers in their affection, mercy, and compassion for each other is that of a single body. When any limb aches, the whole body reacts with sleeplessness and fever."<sup>4</sup>

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<sup>3</sup> The Noble Qur'aan 005:002

<sup>4</sup> Narrated by Nu'man Ibn Basheer; Collected by Al-Bukhaaree & Muslim

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*Such initiatives are also encouraged in Islam because they foster ties of brotherhood and contribute to the prosperity of a single Ummah in which there is mutual compassion and care for each other.*

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He also said, "Whoever relieves a believer's distress of the distressful aspects of this world, Allah will rescue him from a difficulty of the difficulties of the Hereafter... Allah is helping the servant as long as the servant is helping his brother."<sup>5</sup>

## Differences between Commercial Insurance & Cooperative Insurance

There are several important differences between the two models due to which one is Islamically permitted whilst the other one is prohibited.

Amongst the differences are:

1. Cooperative insurance contracts are cooperative and charitable in nature, whereas commercial insurance contracts are commercial and there is an intent of profit.
2. In cooperative insurance schemes, if the central fund is not sufficient to cover a loss, the donors are requested to increase their contributions to cover the difference. If this does not take place, compensation will not be offered as there is no legal requirement to compensate. In commercial insurance schemes, the insurer is legally required to compensate for the loss, and the other clients are under no obligation to contribute any further.
3. In commercial insurance, the insurer will become bankrupt when their pay-outs to their policy holders exceed the amount paid in by their clients if the company cannot afford the difference. In cooperative insurance, there is no bankruptcy as such – because it is mere cooperation and non-profit based. The donors must agree to further actions.
4. In commercial insurance, the insurer owns the wealth and is free to invest or profit from the total fees collected from their clients, and there is no regard given to what is Halal or Haraam. In cooperative insurance, there is no ownership of the central fund, there is only management of the funds based on trust. The funds cannot be exploited for the mutual profit of any one shareholder, unlike commercial insurance.

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<sup>5</sup> Narrated by Abu Hurayrah; Collected by Muslim

5. In cooperative insurance, the insurers are also the policy holders, they compensate each other from the donations they have given. In Commercial Insurance, the insurer must compensate, and the policy holder is an external element to the company.
6. In cooperative insurance, the main aim is for the members' contribution to merely cover any compensation and administrative expenses. In commercial insurance, the sole objective is for the insurer to obtain profits.
7. In cooperative insurance, if there is a large surplus after compensation of any losses, some or all the money can be returned in equal amounts to the members. In commercial insurance, any surplus is profit for the insurer or dividends for the owners.

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## Fataawa from the Scholars Regarding Insurance

The above categorisation of insurance to commercial and cooperative has been proposed by a number of senior scholars and recognised authorities in Islamic jurisprudence. Amongst the Fataawa are:

1. اللجنة الدائمة للبحوث العلمية والإفتاء

Excerpt: "Previously, the Committee of Major Scholars published their decision that commercial insurance in all its types is prohibited due to the harm and dangers it contains, as well as the incorrect consumption of people's wealth. These are matters which the pure Share'ah forbids and severely prohibits.

The Committee of Major Scholars also published their edict that cooperative insurance is permitted, as it is based on donations from generous people; its objective is to help the needy and there is no return of profit or capital for the members..."<sup>6</sup>

2. هيئة كبار العلماء

Excerpt: "Those in agreement concluded that commercial insurance is prohibited, and the council also concluded – to the exception of Shaykh Abdullah Ibn Munee' - that cooperative insurance

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<sup>6</sup> The Permanent Committee for Islamic Research and Legal Edicts (Saudi Arabia) Fatwa No. 19406, Vol. 15 P. 266 – 269

is a viable alternative to commercial insurance...”<sup>7</sup>

3. مجمع الفقه الإسلامي

Excerpt: “...After thorough research and an exchange of views, the Council has concluded by majority that: Insurance in all its forms is prohibited whether it is life insurance, merchandise or any other type of property. The Council also concluded by unanimous agreement that it agrees with the decision of the Committee of Major Scholars (Saudi Arabia) that cooperative insurance is permitted...”<sup>8</sup>

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### The Ruling on Warranties and Guarantees

When buying any product, customers want to ensure that it is free from any defects and will function as advertised. Customers also expect the product to work as advertised for a reasonable amount of time. In order to ensure this, companies and manufacturers will often offer guarantees and warranties. Both models come under the term used in Islamic Fiqh: Adh-Dhamaan.

A guarantee is a promise from the manufacturer and/or seller that the product is of the standard as advertised. If the product does not fulfil any aspect of the guarantee, the product is returned either in exchange for another product or the original price. A guarantee can also be an assurance by an external organization that the product matches their quality standards. There is no time limit for the guarantee. In Fiqh terminology, this is called Dhamaan Al-Jawdah.

A warranty is a promise by the manufacture and/or seller that if the product is faulty in any way, it will be repaired or replaced within a specific period of time. The damage and faults which are compensable will be defined as per the contract. In Fiqh terminology, this is called Dhamaan Al-Adaa.

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*A guarantee is a promise from the manufacturer and/or seller that the product is of the standard as advertised. If the product does not fulfil any aspect of the guarantee, the product is returned either in exchange for another product or the original price.*

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<sup>7</sup> The Committee of Major Scholars (Riyadh) in its 10th meeting in Riyadh 4/4/1397h - Edict No.5/10

<sup>8</sup> The Islamic Fiqh Council (Mecca) in its 1st meeting 10/11/1398h

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## Islamic Ruling on Guarantees and Warranties

Both the warranty and guarantee models are Islamically legislated if they are included in the product price, and they ensure the customer is receiving what he has paid for; his wealth is therefore protected from being exploited, as Allah (the High) said,

**{O you who have believed, do not consume one another's wealth unjustly but only [in lawful] business by mutual consent} <sup>9</sup>**

In an Islamically permitted transaction, the amount being paid, and the merchandise being purchased must both be specified and quantified, this includes the merchandise being subject to the quality standards it claims to have.

If the merchandise is defective through no fault of the customer, it is the responsibility of the seller or manufacturer to compensate for the defect by either returning the original price, replacing the defective item or repairing it – according to whatever contract was agreed by both parties.

## Extended Warranties vs. External Warranties

This is an extra option which is given to the customer, for an additional payment the time period of the warranty can be extended. The seller will be liable for any defects which occur during the extended period. This is also permitted as long as the increase in price is included in the overall price of the product and the warrantee is not charged separately to the actual product. It is merely an extension of the seller's promise and guarantee of the quality of the product, and an extra fee for a service in which the defective merchandise will be repaired or replaced.

However, it is not permitted to buy external cover, warranties or guarantees – this then becomes commercial insurance which is not permitted as discussed previously.

Shaykh Ibn Jibreen (may Allah have mercy upon him) was asked about this with the following question: "What is the ruling of increasing the price of a product for an increase in the warrantee period?"

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*However, it is not permitted to buy external cover, warranties or guarantees – this then becomes commercial insurance which is not permitted as discussed previously.*

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9 The Noble Qur'aan 004:029

He replied: *“There is nothing wrong with this as long as both of them accept [the terms], as for buying external warrantees, this is not permissible, and Allah knows best.”*<sup>10</sup>

In this fatwa, the Shaykh differentiates between an extended warrantee from the manufacturer or seller, and between an external warrantee. The former is an extension of his promise and the increase in the price of the product is for an increase in service, whereas the latter is an insurance.

Allah knows best, may peace and blessings be upon His Messenger Muhammad, and upon all his followers.

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*...the Shaykh differentiates between an extended warrantee from the manufacturer or seller, and between an external warrantee.*

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<sup>10</sup> <https://islamqa.info/ar/answers/6249/حكم-رفع-سعر-السلعة-لزيادة-مدة-الضمان>