36955 - Ruling on buying cooperative shares for insurance

the question

What is the ruling on buying shares in the cooperative insurance company that is offering shares on the Saudi stock market?.

Detailed answer

Praise be to Allah.

The shar’i ruling on this matter may be summed up as follows:

1 – The shar’i ruling on insurance

The majority of contemporary scholars are of the view that commercial insurance is haram and cooperative insurance is permissible. This view was adopted by most of the fatwa-issuing councils, such as the Council of Senior Scholars in Saudi, the Standing Committee for Issuing Fatwas, the Islamic Fiqh Council of the Muslim World League in Makkah al-Mukarramah, the International Islamic Fiqh Council of the Organization of the Islamic Conference in Jeddah, and others. That is because commercial insurance involves elements of ambiguity, gambling and consuming wealth unlawfully, unlike cooperative insurance which is based on takaful and tadamun (mutual support and solidarity). The one who looks objectively at the insurance industry nowadays will realize that this is a moderate and fair-minded approach, and will understand the extent to which it is in accordance with the aims of Islamic sharee’ah of achieving the people’s interests and meeting their needs without being unjust or causing them any harm. Studies of the insurance industry bear witness to that. In a commercial insurance organization, huge amounts of wealth are accumulated by the insurance companies in return for some compensation which may be regarded as very little in comparison to the profits that they make. The result is that only a few rich people benefit the most from the advantages of insurance and its services, whilst the vast majority of poor people are

deprived of it because they are unable to afford insurance payments. These companies make people feel that there is no way to spread risk except in this manner. This is something which has been proven false by the experience of cooperative insurance schemes which have been set up in some advanced countries, where it has been more successful in achieving the aims of insurance than the commercial insurance companies.

2 – The difference between commercial insurance and cooperative insurance

In the case of commercial insurance, the administration of the insurance is carried out by a company which has an identity separate from that of those who are insured by it. This company is entitled to all the instalments paid in return for its commitment to pay out insurance money when it is due (i.e., when an accident or whatever happens). What is left of these instalments is not paid back to those who are insured by the company, because it is considered to be a payment in return for the company's commitment to pay the compensation as agreed. If all the instalments collected by the company are not enough to pay all the compensation, then the company has no right to go back to the customers and ask them to pay more. This is the essence of the kind of ambiguous transaction that is forbidden in Islam, and is consuming wealth unlawfully.

In the case of cooperative insurance, a number of people who are exposed to the same type of danger get together and each of them pays a specific contribution. These contributions are for the purpose of paying compensation to anyone who becomes entitled to it as the result of some harm that befell him. If the sum of contributions is greater than the sum paid out in compensation, the members of the scheme are entitled to take back the difference. If there is a shortfall, then the members are asked to make additional contributions to cover the deficit, or else the compensation paid is reduced in accordance with that deficit.

It does not matter if the cooperative insurance scheme is run by some entity that is separate from those who are covered by the scheme, or that entity takes wages or commission in return for running the scheme. It also does not matter if it takes part of the profits earned by investing that money, in return for acting as their investment agent.

Thus it is clear that both types of insurance companies may be a separate entity independent of those who are covered by the insurance. In both cases it may be a profitable company – i.e., one which aims to make a profit. The difference between the two types is clear in two basic matters:

The first difference: in the case of commercial insurance, there is a contractual commitment between the insurance company and those who are covered by it, whereby the company is obliged to pay compensation to the customers, in return for which the company is entitled to all the instalments paid. In the case of cooperative insurance, there is no room for this commitment, because compensation is to be paid from whatever is available of instalments paid. If the instalments are not enough to cover all the compensation, then the members are asked to increase their contributions in order to make up the difference, otherwise compensation will be paid in part, depending on what funds are available.

The second difference: the cooperative insurance company does not aim to make a profit from the difference between the instalments paid by its customers and the compensation for harm that is paid to them by the company. Rather if the sum of instalments is greater than the sum paid out in compensation for damages, the extra amount is returned to the customers. In contrast, any extra funds in the case of commercial insurance belong entirely to the insurance company in return for its commitment to compensate its customers.

3 – Ruling on joining cooperative insurance schemes

From studying the financial statements of the National Cooperative Insurance Company (al-Sharikah al-Wataniyyah li'l-Ta'meen al-Ta'awuni) over the past five years, it is clear that it is not permissible to join this company for the following reasons:

Firstly: The insurance contract with this company is for commercial insurance, not cooperative. Even though the company was established by separating the fund for instalments paid by shareholders from the financial activities of the insurance company (which has to do administering the funds paid by members of the insurance scheme) – as is the case with cooperative insurance – the system of insurance practised by this company is nothing more or less than commercial

insurance, contrary to what its name may indicate. This is clear from the following points:

(a)The basic system of the company states that if there is any surplus money which represents the difference between instalments paid in and money paid out in compensation, 10% of it is to paid out to those who are covered by the insurance, and the remainder, which is 90% of the net surplus, is to be paid out to the shareholders, because they have taken a risk by investing in this insurance. (Article 43 of the constitution of the company; article 70 of the executive regulations of the watchdog committee on cooperative insurance companies). This means that the insurance system in this company is based on a contractual commitment, whereby the shareholders are entitled to the instalments in return for their commitment to pay compensation. This is the true nature of commercial insurance. Giving back a part of the surplus to the customers is no more than an attempt to give an air of shar'i legitimacy to the contract. But in cooperative insurance, the entire surplus must be given to the customers, either being paid out to them or placed in a contingency fund.

(b)As a result of this rule, the company had surplus funds from its insurance activities, which in 2003 was 178,914,000 riyals, of which 18,000,000 was returned to its customers, i.e., 10% of the surplus. The remaining amount, after taking out some for the contingency fund, was added to the accumulated funds of the company that it has acquired from its insurance activities, the total of which is 548,452,000 riyals. According to the rules of the company, this surplus is regarded as belonging to the shareholders.

(c)This company has contracts for reinsurance with companies that offer this service, which are usually foreign companies that deal on the basis of commercial insurance. It may be noted that reinsurance represents more than half of the insurance payments collected, as is reflected in the following table:

Year	1999	2000	2001	2002	2003
Reinsurance (in thousands)	424.671	498.845	735.523	663.152	716.584
Insurance (in thousands)	628.742	716.983	1.023.206	1.081.173	1.545.797

From this table, it is clear that more than half of the insurance payments are sent outside the Kingdom (Saudi Arabia). This is the nature of commercial insurance.

Secondly: The company invests in some haram activities.

The company has invested the money paid by its customers in haram stocks and bonds, the value of which in 2003 was 430,525,000 riyals, which is equivalent to 24% of the total insurance activities.

The company also invested the shareholders' money in haram stocks and bonds, the value of which in 2003 reached 34,981,000 riyals, or 8% of the total of the shareholders' rights. In addition to that, the company owns 50% of one of the commercial insurance companies.

Suggestions for a cooperative insurance scheme that is in accordance with shar'i guidelines and achieves the aims of insurance:

(a)The administration of the cooperative insurance should be done by a shared-based company, where the shareholders' financial affairs are truly independent of the insurance operation.

(b)The share-based company should be allowed to deduct all the administrative and running costs from the total amount of insurance payments collected, and charge fees in return for running the insurance operation as a paid agent. It should also be allowed to invest the money collected from its customers for insurance in permissible investments, for which it will be entitled to a percentage of the profits from those investments because it is acting as an investment partner.

(c)The company should avoid entering into haram investments such as stocks and bonds, etc., whether that is investing solely for the shareholders or investments that have to do with the insurance operation.

(d)The company's obligation to pay compensation is of two types: permissible and impermissible. The permissible type means that the company is committed to running its business in an honest and professional manner; if it falls short in that, it should bear responsibility for the consequences and offer compensation for that. As for the type that is impermissible, that means giving an

absolute commitment to offer compensation whether the harm is done by the company or by someone else. This goes against the basic principle of cooperative insurance. Instead of that, the company should set up a contingency fund with the money that it has accumulated from insurance payments, and this contingency fund should not be recorded as belonging to the shareholders, rather it belongs exclusively to the insurance operation.

(e)The company may make insurance contracts conditional upon spreading risk, subject to the condition that these contracts are of the cooperative insurance type.

In conclusion, we ask Allah, may He be blessed and exalted, to enable those who are in charge of this company to do all that is good, and to guide us and them, and all the Muslims, to that which He loves and which pleases Him. May Allah send blessings and peace upon our Prophet Muhammad.

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