

**Resolution of OIC Fiqh Academy  
(Related to Islamic Economics and Finance)**

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

**Resolution No. 200 (6/21)**

**Bases of Cooperative Insurance  
In the light of Shari‘ah Rulings and Controls**

The Council of the International Islamic Fiqh Academy (IIFA), of the Organization of Islamic Cooperation (OIC), in its 21<sup>st</sup> session, held in Riyadh (Kingdom of Saudi Arabia), during the period *15-19 Muharram, 1435H* (November 18-22, 2013),

**Having reviewed the recommendations of the Seminar** on “*Bases of Islamic Cooperative Insurance in the Light of Shari‘ah Rulings and Controls*”, organized in Jeddah (KSA) by IIFA, during the period *20-22 Jumada-II, 1434H* (April 30 - May 1, 2013), in response to IIFA Resolution No.187 (2/20), issued by its 20<sup>th</sup> Session, held in Oran (People’s Democratic Republic of Algeria), during the period *26 Shawwal-2 Dhul Qi‘dah, 1433H* (September 13-18, 2012),

And based on the discussions of the subject,

**Resolved the following:**

Cooperative insurance is a new contract based on the principle of cooperation, which, in its turn, is governed by controls derived from guidance of the holy *Quran* and *Sunnah* (Prophetic Tradition).

Insurance, in general, is divisible into two types:

- (1) Commercial insurance, which aims to achieve gain to insurance seeker through compensation for risks, while from the standpoint of the managing company, it aims to achieve profit.

- (2) Non-commercial insurance that does not aim to achieve profit, but to serve interest of its participants through mutual contribution to bearing of injury.

The second type of insurance has several denotations, including cooperative insurance, solidarity insurance, reciprocal insurance and Islamic insurance.

There are essential differences between cooperative insurance and commercial insurance of which most important are the following:

- 1) Islamic cooperative insurance is a form of cooperation between members of a group or a number of groups in the society through mutual contribution to risk bearing without seeking profit. Therefore, it does not constitute a *mu'awadah* (compensation) contract, and the degree of *gharar* (uncertainty) it involves is forgivable. Contrarily, commercial insurance is a *mu'awadah* (compensation) contract, which aims to generate profit through compensation for shifting of risks from insurance client to insurance company. Therefore, commercial insurance is subject to the rulings on compensatory financial dealings that are affected by *gharar*.
- 2) The parties of the relationship in cooperative insurance are: the total number of participants in the cooperative insurance fund and the managing party, while in commercial insurance they are the company and the policyholders.
- 3) In cooperative insurance, there is a fund containing assets that comprise contributions of policyholders, profits generated from investment of contributions, and reserves, whereas there is no such fund in commercial insurance.
- 4) In cooperative insurance, the Management Company assumes the tasks of managing the coverage and insurance business, besides investment of insurance funds, whereas in commercial insurance the insurance company is the insurer who owns the insurance premiums as well as insurance profits and surplus.
- 5) Policyholder and insurer in cooperative insurance are, in fact, the same person with two different legal considerations, contrary to the case in commercial insurance, where they are completely different, since the participant is the insurance client and the insurer is the insurance company.
- 6) Management in cooperative insurance, whether an elected body from the participants, a specialized company or public institution, is an agent that assumes contracting on behalf of participants' (policyholders) fund, and

has the right of receiving a pay for that, while in commercial insurance, management is a principal party who performs contracting on its own.

- 7) Management Company in cooperative insurance does not own the insurance premiums (contributions), because premiums are owned by participants' (policyholders) fund, but in commercial insurance, the company owns the insurance premiums against its commitment to provide compensation in case of injury.
- 8) In cooperative insurance, the remaining amount of premium and its returns – after deduction of expenses and compensations – remains owned by and in the accounts of the fund. It constitutes the surplus, which regulations of the fund indicate the way of disposing of it. This can never happen in commercial insurance, where the company owns the premiums contractually and in terms of actual possession. That is to say, in commercial insurance, premiums represent revenue and profit for the insurance company.
- 9) In cooperative insurance, returns on investment of premiums – after deduction of management costs, which go to Management Company – remain in the policyholders' fund, while such returns belong to the insurance company in commercial insurance.
- 10) On liquidation of cooperative insurance fund, its assets are either spent on charitable purposes or distributed among participants instantly (as indicated in detail in clause 13 hereafter), where such assets go to shareholders in commercial insurance.
- 11) In cooperative insurance, the company is bound to observe relevant rules of Islamic Sharī'ah and *fatwas* (Sharī'ah Opinions) of its Sharī'ah Board, a situation, which is irrelevant to commercial insurance.

Cooperative and commercial insurance are similar, in consideration of the basic principles of insurance, including:

- 1) Principle of Insurance Interest: which is the legal right of insurance that stems from a legally recognized financial relationship between the insurance client and the subject matter of insurance.
- 2) Principle of Good Faith: which means the positive and voluntary duty of strict and perfect disclosure of all essential facts relating to the risk insured against, whether such facts are requested or not.
- 3) Principle of Close Direct Cause: which refers to that effective cause which is sufficient to set in force a series of incidents constituting the cause of the

result that originate from them, without the invention of any other factor stemming from an independent new source and breaking the series.

- 4) Principle of compensation.
- 5) Principle of Participation.
- 6) Principle of Substitution and Rights.

Cooperative insurance has also its own distinguishing principles, which include:

- 1) Abidance by rules and principles of Sharī'ah in all dealings and contracts.
- 2) No insurance is provided under this system to Sharī'ah taboos.
- 3) Avoidance of any transaction that involve receipt or payment of *ribā* (usury).

Fundamental Bases and Principles of Cooperative Insurance

**Clause (1): Definition:**

Cooperative insurance is the process in which a group of people, who face certain risk(s), agree that each of them contribute a specific amount, based on cooperation, to a non-profit fund that is to be used for compensating anyone of them for the harms he would encounter when the risk in question materializes, as per signed contracts and adopted regulatory legislations.

**Clause (2): Forms of Cooperative Insurance Management:**

Cooperative insurance is managed by an independent licensed body that works in compliance with the rules of Islamic Sharī'ah, and may take one of several forms of which most notable are the following:

- a) A selected panel of policyholders.
- b) A specialized insurance management company.
- c) A public institution established by and report to a state or number of states.

**Clause (3): Relationship between Insurance Fund and Management:**

The relationship between insurance fund and managing party is as follows:

- a) Regarding management of insurance business: the relationship is according to agency contract, with or without pay.
- b) In case of investment: the relationship is governed by either an agency or a *muḍārabah* contract. When agency contract is used, agency can be against pay or not. When using *muḍārabah*, the managing party is entitled to a share in the profit as per agreement, whereas any loss is borne by owners of capital, except in case of negligence or default, or breach of conditions or regulations.

**Clause (4): Pay for Management:**

Pay for management takes one of two forms:

- a) When cooperative insurance business is managed according to rulings of agency contract, pay for managing party can be a lump sum amount, or a given percentage of contributions.
- b) When management of investment assets of participants' fund is arranged through *muḍārabah*, managing party (*muḍārib*) is entitled to a given percentage of the profit, whereas if investment is according to agency contract, the remuneration could be a lump sum amount, or a given percentage of invested amounts.

**Clause (5) Ownership of Contributions and Returns on their Investment.**

Contributions and net returns on their investment are considered as rights of cooperative insurance fund, whereas rights of policyholders in the fund are determined according to the insurance system and conditions of entitlement regarding compensation and insurance surplus.

**Clause (6): Remuneration of Insurance Business Managing Party**

Remuneration or pay for insurance business management is estimated, subject to fair criteria set by an independent body, such as an institution of insurance supervision or through negotiation between the representatives of the fund or any party chosen by participants to oversee their interests, and the managing party.

**Clause (7): Responsibility of the Fund:**

The cooperative insurance fund bears any losses whether in investment or in insurance activities, except when such losses originate from negligence, default or

breach of conditions or regulations by the managing party, who should bear them in such case.

**Clause (8): Insurance Surplus:**

Insurance surplus is the financial balance that remains from collected contributions in addition to its investment returns and any other revenues, after payment of compensations and deduction of necessary allocations and reserve balances, as well as all due expenses and outstanding commitments of the fund.

The entire insurance surplus can be retained in the fund or distributed, totally or partially, among policyholders in a way that achieves justice, and conforms to regulations of the fund.

**Clause (9): Cooperative Insurance Fund Deficit (How it can be dealt with):**

In case of failure of cooperative insurance fund to pay its due commitments, the managing company may resort, without commitment, to one or more of the following actions:

- a) Borrowing from a third party.
- b) Provision of *qard hasan* (benevolent loan) from the managing party.
- c) Increasing the amount of contributions after the consent of participants.
- d) Agreement with compensations' beneficiaries to reduce the amounts of compensations or pay them in installments.

The managing company may also resort to any other arrangements it deems suitable, after clearance by the fund's Sharī'ah Board.

**Clause (10): Reinsurance**

- (1) It is permissible for the cooperative insurance company to conclude reinsurance contracts, taking into consideration that the reinsurance transactions it takes part in, by virtue of such contracts, conform to rulings of Islamic Sharī'ah and basic principles of cooperative insurance as decided by its Sharī'ah Supervisory Board.

- (2) Cooperative insurance companies are committed to do all their reinsurance arrangements with Islamic reinsurance companies. When it is impossible, for reasonable justifications, to observe such commitments, they may conclude reinsurance contracts with traditional reinsurance companies to the extent of their real needs and in conformity with the controls set by Shari‘ah boards and any other controls they deem suitable, including the following:
- a) Cooperative insurance companies should keep the ratio of traditional reinsurance coverage at the minimum level.
  - b) The managing party should not direct reinsurance premiums paid to cooperative insurance company to any type of investment that does not comply with rules and principles of Islamic Shari‘ah. Conversely, the managing party should neither claim a share in the returns on investments of traditional reinsurance companies nor should it accept to bear any portion in the losses incurred by investments of these companies.
  - c) Cooperative insurance companies should not pay or receive any interest relating to their reinsurance arrangements with traditional reinsurance companies. Additionally, reinsurance funds should be kept with cooperative insurance companies rather than with traditional reinsurance companies.
  - d) Agreement with traditional reinsurance companies should be for the minimum possible period.

**Clause (11): Shari‘ah Compliance**

Cooperative insurance management should comply with rules of Islamic Shari‘ah in all insurance operations, activities and investments.

**Clause (12): Shari‘ah Supervision:**

A cooperative insurance enterprise should appoint a Shari‘ah supervisory board and a Shari‘ah audit body as has been stated in IIFA’s Resolution No. 177 (3/19) on “Role of Shari‘ah Supervision in Controlling Islamic Banking Business (Significance, Conditions and *Modus Oprandi*)”. Appointment and operation of this Shari‘ah board should be subject to approval of central Shari‘ah supervisory body, if any.

### **Clause (13): Fund Liquidation:**

When a cooperative insurance fund is liquidated, its assets can be channeled into charitable purposes or distributed among participants, according to fair bases after meeting its technical and legal commitments, subject to regulation of the fund and under supervision of the public authority of Sharī'ah supervision. Fund manager, in this case, is not entitled to any share of the assets.

### **Clause (14): Conflict Resolution:**

Conflicts that arise between cooperative insurance company and policyholders should be dealt with, according to prevailing regulations and laws, starting from reconciliation, then arbitration and finally resort to competent judiciary body.

### **Clause (15): Relationship between Participants of the Cooperative Insurance Fund**

The relationship between participants of the fund is a form of cooperation in which a group of people agree to contribute specific amounts so that the proceeds of their contributions be used in compensation for harm or realization of interest to anyone of them when need arises. Such cooperation is based on forgiveness, equality and permissibility of benefiting from the rights of each other, rather than on reciprocal compensation, stinginess and drive for profit. Therefore, a lot of *gharar* can be excusable under this type of arrangement, which also has nothing to do with *ribā*. Several instances to substantiate this fact can be quoted from Sharī'ah, such as:

**Firstly:** The divine order to cooperate in the cause of righteousness and piety. In this regard, Allah the Almighty says: ***“Help ye one another in righteousness and piety, but help not ye one another in sin and rancor”***[*Al-Ma'idah:2*].

**Secondly:** The *Ash'aris hadith* (Prophetic tradition about the *Ash'ari* people) narrated by Abu Musa Al-Ash'ari (may Allah be pleased with him) who told that the Prophet (pbuh) said: ***“When the Ash'aris encounter food shortage during invasion, or have insufficient food stocks for their families in Madinah, they used to collect and pile up all the food they have on a piece of cloth and divide it equally among themselves. (Therefore) Ash'aris are my people and I am one of them”*** [agreed upon].

Commenting on this *hadith*, Al-Nawawi said: *(In this hadith, there is the virtue of the Ash‘aris, the virtue of altruism and consolation, and the virtue of sharing food supplies during travel as well as in urban communities when there is food shortage. The hadith does not refer to “Division” as it is known in Fiqh writings with all its conditions, its prohibition in ribāwiyat “ribā-liable commodities”, equality requirement and the like. What the hadith seems to refer to, is permissibility among the Ash‘aris (to get equal shares) and their consolation to each other with what they had) [Al-Nawawi’s Elaboration in Sahih Muslim: 16/62].*

**Thirdly: *Nihd, Nahd or Munahadah*** (Sharing): Imam Al-Bukhari indicated the concept of *Nahd* in the form of a long title as follows: [*Chapter on Sharikah (Partnership), Sharikah in Food, Nahd and Urood (articles) and how a commodity that should be measured in terms of weight or volume is divided by rough estimate or handful measurement, when Muslims saw no harm that each of them got the same share of their footstock, and also using rough estimate in division of gold and silver, or two different varieties of dates when pooled together*]. What is meant here, is contribution of a group of travelers to all travelling expenses and dividing such expenses among them.

Ibn Hajar Al-Asqalani also indicated that the term *Nihd* or *Nahd* refers to equal sharing of sustenance stuffs while on travel. He, further elaborated that usually sharing comprises a multitude of stuffs among which are food items including *ribā*-liable commodities. Yet, according to Al-Asqalani, *ribā* restrictions on exchange of *ribā*-liable commodities is forgiven in the case of *Nihd*, because proof of *Nihd* permissibility is well established (See Fathul Bari: 5/128).

### **Clause (16): Fund Autonomy**

Cooperative insurance fund should be independent and may comprise other donations besides those of participants. Independence of the fund can be ensured by granting it a legal personality decided by law, or through complete separation of its accounts from those of the managing party. Alternatively, a charitable cash *Waqf* can also be established based on permissibility of such type of *waqf*.

### **Clause (17): Withdrawal from Fund:**

Cooperative insurance policy regulates cases of withdrawal according to regulations, conditions and controls cleared by Sharī‘ah Board, without infliction of harm on others.

**Clause (18): Contribution to Insurance Fund:**

- (1) Contribution is determinable according to actuarial principles based on statistical techniques, with due consideration to whether risk is constant or variable. Determination process would also involve application of principle of proportionality between contribution and risk itself and taking into account type and period of contribution, as well as amount of insurance cover.
- (2) Risk, insured against, must be of probable occurrence, rather than just relating to will of insurance client, and should not relate to a prohibited object.

**Clause (19): Substitution:**

Fund management substitutes the participant it compensates for injury inflicted upon him, in suing harm inflictor in all lawsuits and rights and the proceeds thus collected goes to the fund.

**Clause (20): Bearing:**

It is permissible to stipulate in the insurance policy that insurance client has to bear a lump sum amount or a percentage of compensation amount for harms, which others inflict upon him or those which he inflicts upon others.

**Clause (21): Ownership of Premiums:**

It is permissible for the fund to own contributions and in that case, policyholders will no longer remain owners of their contributions as soon as they pay it. In this case, each policyholder is considered to have assigned his right of owning his contribution to the fund. One of these two options, of owning or relinquishment, of the right in contribution should be explicitly referred to in the insurance policy.

**And Recommends the Following:**

- (1) Communication of these rulings, bases and conditions to concerned parties in Islamic countries, especially those responsible for issuing rules and regulations, cooperative insurance companies and other interested parties.

- (2) Operationalization of what has been stated in IIFA Resolution No. 177 (3/19) concerning call upon Islamic countries to establish central supervisory bodies to oversee the work of supervisory boards of Islamic financial institutions and cooperative insurance companies.
- (3) Call for establishment of an international Sharī'ah board under the supervision of IIFA. The following institutions may contribute to the establishment of the board:
  - Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI).
  - Islamic Development Bank Group (IDBG).
  - Islamic Financial Services Board (IFSB).
  - General Council for Islamic Banks and Financial Institutions (CIBAFI).

Among the basic functions of the proposed board is issuance of Sharī'ah standards that regulate cooperative insurance and Islamic banking activities, getting such standards ratified by IIFA and facilitating their adoption, by supervisory and regulatory bodies, as the laws that govern the work of Islamic financial institutions.

IDBG and IIFA's Secretariat may coordinate for developing the detailed proposal on the working modalities of the board.

- (4) The Secretariat General of IFFA should mobilize more studies on some issues of cooperative insurance including:
  - Presentation of international experiences in the field of cooperative insurance and exploring their abundance by the bases adopted in this resolution.
  - Studying the idea of remunerating the managing party for management of insurance operations through a specific amount or ratio of the insurance surplus without allocating any part of contribution proceeds for payment of management expenses.
  - Studying the idea of remunerating the party that manages insurance operations through a combination of a ratio of contribution proceeds along with a ratio of the insurance surplus, to ensure motivation of management for enhanced performance.
  - Studying the different aspects relating to the *waqf*-related basis of cooperative insurance.

