

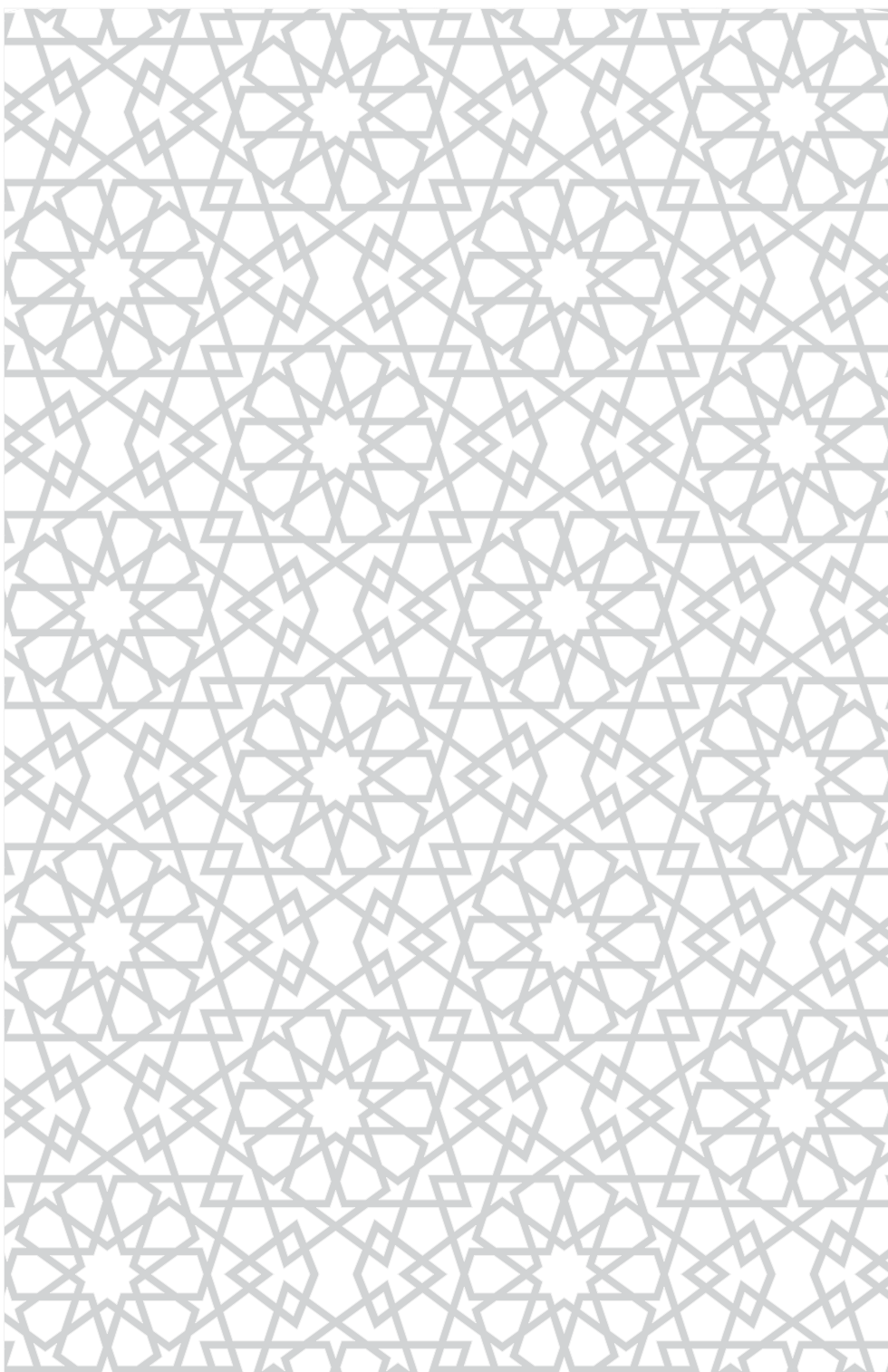
**Shari'ah Standard No. (41)**

# **Islamic Reinsurance**



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***IN THE NAME OF ALLAH, THE ALL-MERCIFUL, THE MOST MERCIFUL***

All praise be to Allah, the Lord of all the worlds, and blessings and peace be upon our master, Muhammad, and his household and all his companions

## **Preface**

This Standard aims to illustrate the rules and principles of Shari'ah that govern Islamic reinsurance and indicate the controls which Islamic insurance and reinsurance companies as well as Islamic financial institutions (Institution/Institutions)<sup>(1)</sup> should observe in dealing with traditional insurance and reinsurance companies. The overall objective of the standard is to facilitate transference of risks and increasing of insurance capacity.

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(1) The word (Institution/Institutions) is used here to refer, in short, to Islamic financial institutions including Islamic Banks.

## Statement of the Standard

### 1. Scope of the Standard

This Standard covers Islamic reinsurance and participation with traditional insurance or reinsurance companies. The Standard does not cover Islamic insurance which has already been covered in a separate standard.

### 2. Definition of Reinsurance

2/1 Islamic Reinsurance refers to the agreement among insurance companies, on behalf of the insurance funds under their management, to devise a mechanism for the avoidance of part of the risks which the insurance funds may encounter. On the basis of such agreement a reinsurance fund which has a distinct legal personality and independent financial liability is formed up through making contributions out of the insurance funds paid by the insurance clients on the basis of donation. The reinsurance fund, thus formed, assumes the task of covering part of the risks encountered by the insurance funds.

2/2 Reinsurance, as described above, constitutes the Islamic alternative for the reinsurance provided by traditional reinsurance companies, which is based on exchange of the reinsurance premiums and compensation, rather than on donation commitments.

### 3. Shari'ah Status of Reinsurance

3/1 Shari'ah status of Islamic reinsurance:

3/1/1 It is permissible to reinsure with Islamic reinsurance companies.

3/2 Shari'ah status of reinsurance with traditional reinsurance companies:

It is impermissible for Islamic insurance companies to reinsure with traditional reinsurance companies, except when such reinsurance is sought as a transitional arrangement stemming from public need which amounts to necessity.

#### **4. Key Methods of Reinsurance**

With regard to the scope of commitment of the reinsurer, reinsurance can take place through one of the following two forms:

- 4/1 Selective reinsurance: In this case the insurance company presents the individual risk which constitutes the subject matter of reinsurance to the reinsurer along with a summary of all the information related to it, so that the reinsurer can study the information and decide whether to accept the risk or not. The reinsurance company (insurer) becomes committed to what it accepts.
- 4/2 Comprehensive reinsurance (reinsurance agreement): In this case the reinsurance company assumes the commitment to accept all the risks which fall within the scope of the agreement signed with the insurance company.

#### **5. Key Forms of Reinsurance Requests**

- 5/1 Risk sharing reinsurance: The insurance company in this case seeks reinsurance for a percentage of the insurance policies it issues (50% or 25%), whether such coverage is within or in excess of its own insurance capacity.
- 5/2 Excess risk reinsurance (beyond risk tolerance): The insurance company keeps all the insurance policies which it can easily tolerate their risks and seeks reinsurance for those which involve risks that it cannot tolerate.
- 5/3 Loss reinsurance: According to this type of reinsurance the reinsurance company assumes the responsibility of bearing the losses beyond the specific limit agreed upon. This form of reinsurance is widely used in the insurances which involve big amounts. The insurance company bears, for instance, the first 20 thousand dollars of compensation for the accident, while the reinsurance company bears the rest.

#### **6. Controls on Reinsurance with Traditional Reinsurance Companies**

In reinsuring with traditional reinsurance companies, Islamic insurance companies should observe the following controls:

6/1 Islamic insurance companies should reinsure first with Islamic reinsurance companies, to the largest possible extent.

6/2 Islamic insurance companies should not keep any cash reserves for ongoing risks, that belong to traditional reinsurance companies and on which interest has to be paid. Nevertheless, an agreement can be reached between the Islamic insurance company and the traditional reinsurance company in order to specify a certain portion of the premiums payable to the traditional reinsurance company to be retained by the Islamic insurance company. The Islamic insurance company can invest retained funds through Mudarabah or investment agency, where the Islamic insurance company assumes the role of the Mudarib and the traditional reinsurance company assumes the role of Rab al-Mal. When profit is distributed as per the ratios agreed upon, the share of the traditional reinsurance company is to be added to its account with the Islamic insurance company, whereas the share of the profit earned by the Islamic insurance company for performing the investment as an independent personality is to be added to the account of the participants.

6/3 The periods of the reinsurance agreements sought by Islamic insurance companies from traditional reinsurance companies should be commensurate to the actual need.

6/4 Before signing agreements with traditional reinsurance companies, Islamic insurance companies should seek the approval of their Shari'ah Supervisory Boards.

6/5 Islamic insurance companies should stick to the minimum size of reinsurance with traditional reinsurance companies, and Shari'ah Boards should undertake follow-up in this connection.

#### **7. Shari'ah Status of Compensations and Commissions Presented to Islamic Insurance Companies by Traditional Reinsurance Companies**

7/1 It is permissible for Islamic insurance companies to receive the amounts of the insurance coverage from traditional reinsurance companies.



7/2 It is impermissible for an Islamic insurance company to receive reinsurance commission from a traditional reinsurance company. Nevertheless, the Islamic insurance company has the right to seek premium discounts from the traditional reinsurance company.

7/3 Islamic insurance companies should not accept any redistributions of insurance surplus forwarded by traditional reinsurance companies. Nonetheless, Islamic insurance companies can request premium discounts from traditional reinsurance companies.

#### **8. Shari'ah Controls on Practicing Islamic Reinsurance by Islamic Reinsurance Companies**

8/1 Islamic reinsurance companies should observe the Shari'ah controls on the activities of Islamic insurance companies indicted in Shari'ah Standard No. (26) on Islamic Insurance, with due consideration to the fact that the participants in this case are the insurance companies.

8/2 Formation of a Shari'ah Supervisory Board to supervise the process of establishing the Islamic reinsurance company, verify its contracts and documents, overview its applications and submit Shari'ah reports on its activities.

8/3 It is permissible for the Islamic reinsurance company to provide reinsurance services to traditional insurance companies, subject to the following conditions:

1. The contract to be used should be the Islamic reinsurance contract.
2. There should be no linkage.
3. Reinsurance should not involve a Shari'ah prohibited object.

#### **9. Financial Gains Received from Islamic Reinsurance Companies**

All financial gains which Islamic insurance companies receive from Islamic reinsurance companies are considered as lawful gains and should be credited to the account of policyholders (the participant companies of the reinsurance scheme), as part of revenues.

#### **10. Date of Issuance of the Standard**

This Standard was issued on 2 Dhul-Qa'dah 1430 A.H., corresponding to 21 October 2009 A.D.

## **Adoption of the Standard**

The Shari'ah Board adopted the draft of the Standard on Islamic Reinsurance in its 25th meeting held during the period of 2-4 Dhul-Qādah 1430 A.H., corresponding to 21-23 October 2009 A.D.

## **Appendix (A)**

### **Brief History of the Preparation of the Standard**

In its meeting No. (16) held in Al-Madinah Al-Munawarah, during the period of 7-12 Jumada I, 1427 A.H., corresponding to 3-8 June 2006 A.D, the Shari'ah Board decided to issue a Shari'ah Standard on Islamic Reinsurance.

On 12 Rajab 1427 A.H., corresponding to 6 August 2005 A.D., the General Secretariat decided to commission a Shari'ah consultant to prepare a juristic study on Islamic Reinsurance and Participation with Traditional Companies.

In a joint meeting held in the Kingdom of Bahrain, on 18 Safar 1428 A.H., corresponding to 8 March 2007 A.D., the Shari'ah Standards Committees (1) and (2) discussed the study, approved it and required the consultant to prepare the exposure draft of the Standard.

In a further joint meeting held in Manama, the Kingdom of Bahrain, on 15 Jumada I, 1428 A.H., corresponding to 31 May 2007 A.D., the Shari'ah Standards Committees (1) and (2) discussed the draft of the Standard and necessary amendments were made in the light of the discussions and observations of the meeting.

In its meeting No. (19) held in Makkah Al-Mukarramah, during the period of 26-30 Sha'ban 1428 A.H., corresponding to 8-12 September 2007 A.D., the Shari'ah Board discussed the draft of the Standard and made the amendments which it deemed necessary.

The General Secretariat held a public hearing in the Kingdom of Bahrain, on 8 Jumada II, 1429 A.H., corresponding to 12 June 2008 A.D. The public hearing was attended by more than thirty participants

representing central banks, institutions, accounting firms, Shari'ah scholars, academics and others interested in this field. The members of the Shari'ah Standards Committees (1) and (2) duly responded to several comments and observations that were made in the public hearing.

In its meeting No. (25) held in the Kingdom of Bahrain, during the period of 2-4 Dhul-Qadah 1430 A.H., corresponding to 21-23 October 2009 A.D., the Shari'ah Board discussed the draft of the Standard, incorporated the necessary amendments that it deemed appropriate, and adopted the Standard.

## Appendix (B)

### The Shari'ah Basis for the Standard

- Impermissibility of commercial reinsurance is based on the fact that the idea of commercial reinsurance depends on the idea of commercial insurance and involves Shari'ah-prohibited Gharar. As related by Muslim, Ashab al-Sunan and others, quoting Abu Hurayrah, the Prophet (peace be upon him) prohibited *Bay' al-Gharar*<sup>(2)</sup> (aleatory sale). Gharar, as defined by several Fiqh scholars, indicates uncertainty about the outcomes, or the consequences, or end result of something.<sup>(3)</sup> According to some contemporary Fiqh scholars Gharar is similar to or part of betting or gambling.<sup>(4)</sup> A number of resolutions on prohibition of Gharar have also been issued by Islamic Fiqh Academies including the Resolution of the Islamic Fiqh Academy -Makkah Al-Mukarramah in its 1398 A.H. Session, endorsing the Resolution of the Supreme Council of the Ulema of the Kingdom of Saudi Arabia in its 10<sup>th</sup> Session held in Riyadh on 4 Rabi' II, 1397 A.H., and Resolution No. (9) 9/1 of the International Islamic Fiqh Academy.
- Permissibility of cooperative insurance stems from the fact that cooperative insurance companies are based on cooperation and donation rather than on exchange-based dealings. It is a well-known as Fiqh axiom that Gharar does not affect donation-based contracts. Permissibility of cooperative insurance can also be derived from several Verses of the Glorious Qur'an

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(2) "Sahih Muslim", *Kitab Al-Buyu'* [3: 115]; "Sunan Abu Dawud" [2: 22], (H: 3376); "Sunan Al-Nasa'i" [2: 21]; "Sunan Ibn Majah" [2: 73]; "Sunan Al-Tirmizi" [3: 532]; "Sunan Al-Darami" [2: 16]; "Al-Muwatta'" [2: 66]; "Musnad Ahmad" [1: 201, 2: 367 and 397]; "Sunan Al-Bayhaqi" [5: 22]; and "Musnaf Ibn Abu Shaybah" [8: 19], Part 2.

(3) See: "Sharh Al-'Inayah Ma'a Fath Al-Qadir" [5: 192]; "Tabyin Al-Haq'iq" [4: 46]; "Al-Taj Wa Al-Iklil" [4: 36]; "Fath Al-'Aziz Bi Hamish Al-Majmu'" [8: 127]; "Matalib Uli Al-Nuha" [3: 25]; "Al-Qawa'id Al-Nuraniyyah", (P. 166); and "Nazariyyat Al-'Aqd", (P. 224). See also Sheikh Siddiq Al-Darir: His valuable book on "Al-Gharar Wa Atharuhu Fi Al-Uqud", Salih Kamil Lil-Rasa'il Al-Jami'iyyah, (P. 54).

(4) See: Dr. Hussein Hamid: "Al-Gharar", (P. 72).

and Prophetic Hadiths which instruct people to cooperate. In this regard, a number of resolutions have been issued by the Islamic Research Academy of Al-Azhar in addition to the Resolution of the Islamic Fiqh Academy -Makkah Al-Mukarramah and Resolution No. (9) 9/1 of the International Islamic Fiqh Academy which states: "Indeed, the contract which respects the origins of Islamic dealings is the cooperative insurance contract which is based on donation and cooperation..." Moreover, permissibility of cooperative insurance contract has never encountered dispute from any contemporary Fiqh scholar.<sup>(5)</sup>

In addition to what has been stated above, the underlying reasons for permissibility of solidarity reinsurance and impermissibility of commercial reinsurance can be summarized in the following essential differences between the two systems:

- a) The commercial reinsurance company is an exchange-based financial contract which aims to make profit out of the reinsurance itself, and therefore should become subject to the rulings on exchange-based financial contracts which can be affected by Gharar. In the contrary, in solidarity reinsurance the contract is based on donation and cooperation and thus cannot be affected by Gharar when the contract involves it.
- b) The company in the Islamic reinsurance contract is an agent of the reinsurance account, whereas in commercial reinsurance the company is a principal party who signs the contract in his own name.
- c) The company in commercial reinsurance owns the reinsurance premiums against commitment to pay the reinsurance amount, while in Islamic reinsurance the company does not own the contributions, which are owned by the reinsurance account.
- d) In Islamic reinsurance the remaining part of the contributions and the returns on it -after expenses and compensations- go to the account of the policyholders (such amounts represent the surplus distributed among participants), whereas this cannot be imagined in commercial

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(5) A Fatwa issued by the Shari'ah Board of the Al Rajhi Banking Company for Investment, Fatwa No. (40).

reinsurance, because the contributions are owned by the company by virtue of the contract and through actual possession. The contributions in the case of commercial reinsurance are even considered as revenue and profit.

- e) In Islamic reinsurance the returns earned from investment of the principal amount of the contributions go to the account of the policyholder after deduction of the Mudarib's share by the company, whereas in commercial reinsurance such returns go to the company.
- f) Islamic reinsurance aims to achieve cooperation among the participating companies rather than profit, whereas commercial reinsurance aims to achieve profit from the reinsurance process itself.
- g) In Islamic reinsurance the company makes profits by investment of its funds in addition to its share in the Mudarabah, as it assumes the role of the Mudarib and the reinsurance account assumes the role of Rab al-Mal.
- h) In Islamic reinsurance companies the participant and the reinsurance client are in fact the same person even if legally considered as separate personalities, while in commercial reinsurance companies they are completely different.
- i) An Islamic reinsurance company observes the rules of the Islamic Shari'ah and the Fatwas issued by its Shari'ah Supervisory Board, whereas the case is not so for commercial reinsurance companies.
- j) When the allocations deducted from the solidarity reinsurance fund remain unpaid until the time of liquidation they are spent on charitable purposes and are not given to the participants, whereas in commercial reinsurance companies such funds go to participants.
- The Islamic reinsurance contract is considered as a binding donation contract, because it is analogous to Munahadah (contribution of travelers to a pool of food victuals) or to pledge of donation. Both of the Islamic Fiqh Academy of the Muslim World League and the International Islamic Fiqh Academy stipulated in their resolutions referred to earlier that Islamic reinsurance is based on donation.



The fact that the Islamic reinsurance contract is binding can also be derived from what has been emphasized by Imam Malik about donation. According to Imam Malik a gift in general becomes valid before possession, and this was also said to have been the viewpoint of Ali and Ibn Masood. The Hanbali scholars hold that a gift is binding even if it is not possessed, except in things that are measured in terms of volume and weight.<sup>(6)</sup> Ibn Rushd (the grandson) said: "Scholars were in disagreement regarding possession...Malik said: "The contract is valid on acceptance, and possession of the gift should be enforced quite like the case in sale..."<sup>(7)</sup>

Ali and Ibn Mas'ud are reported to have said: "*Gift is permissible if it is known, whether it is possessed or not*". It is also reported that Abu Bakar and Omar considered the gift to be binding only when it is possessed.<sup>(8)</sup> Therefore, Malik seems to have taken all these viewpoints into consideration. He derived from the viewpoint of Ali, Ibn Masood and the others that the contract as such is binding, whereas he took the viewpoint of Abu Bakar and Omar to mean that possession is a necessary condition for completion of the contract so as to leave no room for the Dhari'ah (excuse) mentioned by Umar.<sup>(9)</sup>

The fact that a pledge of donation is binding can also be derived from the Hadith of the Prophet (peace be upon him) who said: "*The person who retreats from a gift that he offers is like the dog which licks up its vomit*".<sup>(10)</sup>

- The ruling that the company, which assumes the role of the agent in Islamic reinsurance, should not guarantee is based on the unanimous agreement among Fiqh scholars that an agent should not guarantee except in case of transgression, negligence or breach of the contract.
- The necessity of mentioning the nine principles of Islamic reinsurance in the articles of association of the company stems from the need for reinforcing the donative nature of the contract and laying the Shari'ah foundation

(6) "*Bidayat Al-Mujtahid*" [2: 53]; "*Al-Mughni*" by Ibn Qudamah [5: 64]. See also: "*Bada'i' Al-Sana'i*" [8: 3960]; and "*Al-Ghayah Al-Quswa*" [2: 655].

(7) "*Bidayat Al-Mujtahid*" [2: 534].

(8) See: "*Al-Muwatta*" [2: 46]; and "*Nasb Al-Rayah*" [4: 12].

(9) "*Bidayat Al-Mujtahid*" [2/53].

(10) "*Sahih Al-Bukhari*" [5: 19]; and "*Sahih Muslim*" (H: 1622).

for this important aspect of the company. In the absence of emphasis on these principles which distinguish Islamic reinsurance from commercial reinsurance, Islamic reinsurance may become an exchange-based reinsurance contract, and hence becomes vulnerable to nullification by Gharar, as has been indicated earlier. For illustration of these distinguishing principles of Islamic reinsurance, several Fatwas have been issued including: Fatwa No. (12/11) issued by the 12<sup>th</sup> Al Baraka Seminar on Islamic Economics, and Fatwa No. (42/3) issued by the Shari'ah Supervisory Board of Al Rajhi Company, as well as the Fatwas of the Shari'ah Supervisory Board of Faisal Islamic Bank, Islamic Insurance company – Jordan<sup>(11)</sup> and Islamic Insurance Company of Qatar.

- The basic elements and conditions of the Islamic reinsurance contract are derived from its nature as a contract which is binding to the two parties in addition to the special nature of the insurance contract with regard to the subject matter of insurance.
- The reinsurer and the client should honor their commitments because the reinsurance contract is binding to both parties. According to Shari'ah, the two parties should honor what they agree upon as long as it does not contradict with the rules and principles of Islamic Shari'ah. This can be derived from the Quranic Verses and Hadiths which instruct people to observe commitments and conditions they agree upon, including the Verse: *{“O you who believe! Fulfill (your) obligations”}*<sup>(12)</sup> and the Hadith of the Prophet (peace be upon him) who said: *“Muslims are at their conditions”*.<sup>(13)</sup>
- The basis of the ruling that the reinsurance company may assume the responsibility of managing the reinsurance account against a fee or free of charge is the nature of the agency (Wakalah) contract which Fiqh scholars unanimously declare as permissible with or without remuneration. This point of view is supported by the 12<sup>th</sup> Al Baraka Seminar on Islamic

(11) See: *“Fatawa Al-Ta`min”*, Dallah Al Baraka Group, reviewed by Dr. Abd Al-Sattar Abu Guddah and Dr. Ezz Al-Din Mohammad Khojah, (pp. 99-108).

(12) [Al-Ma`dah (The table):1].

(13) Related by Al-Bukhari with dogmatizing comments from his side: *“Fath Al-Bari”* [4: 251]; *“Al-Tirmidhi”* - with *“Tuhfat Al-Ahwazi”* [4: 584] and he said a good and authentic Hadith.

Economics (Fatwa No. 12/11), the Islamic Fiqh Academy of the Muslim World League (Fatwa No. 961) and the Supreme Council of Ulama of the Kingdom of Saudi Arabia (Fatwa No. 51).

- Permissibility for the company to invest the funds of the reinsurance account is based on the Mudarabah contract which Fiqh scholars unanimously declare as permissible. Such contract entails prior specification of profit sharing ratios so that the reinsurance account can get its share of the profit as indicated by a number of Fatwas including: Fatwa of the Shari'ah Supervisory Board of Faisal Islamic Bank,<sup>(14)</sup> Fatwa No. 12/11 of the 12<sup>th</sup> Seminar of Al Baraka and Shari'ah Standard No. (13) on Mudarabah.
- Necessity of observing conditions in general, including commitment of the company to present Qard Hasan (benevolent loan) to the reinsurance account, is based on the commitment to honor pledges that are binding to only one party of the contract. Honoring such pledges is emphasized by a number of distinguished Fiqh scholars, and is well supported by Shari'ah Texts and Traditions. One of these texts is the Verse: **{“O you who believe! Fulfill (your) obligations”}**, which is taken to mean any Shari'ah-acceptable commitment. Several Hadiths have also indicated enforceability of honoring contracts, pledges and promises.<sup>(15)</sup> In this respect also Fiqh Academies and Shari'ah Supervisory Boards have issued resolutions including: Resolution No. (40-41) 2-3/5<sup>(16)</sup> of the International Islamic Fiqh Academy, and the Fatwa of the Shari'ah Supervisory Board of the Islamic Insurance Company –Jordan.<sup>(17)</sup>
- The ruling that the participant should bear the burden of proving, is based on application of the general rules of evidence which state that evidence is to be provided by the alleger. This rule is supported by explicit indications from the Qur'an and the Sunnah and the viewpoints of knowledgeable Fiqh scholars. A Fatwa in this regard has also been issued by the consolidated Shari'ah Supervisory Board of Al Baraka (Fatwa No. 14/6).

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(14) See: The Book titled *“Al-Mudarabah Fi Kutub Al-Madhahib Al-Fiqhiyyah”*; and *“Al-Mawsu'ah Al-Kuwaytiyyah”*, the term Mudarabah.

(15) For more details see: *“Mabda' Al-Rida Fi Al-'Uqud”*, a comparative study [2: 1161] and its reliable references.

(16) See the Journal of the Academy, No. (5) 2/754-965.

(17) *“Fatawa Al-Ta'min”*, (P. 106).

- The basis of permissibility of the two types of reinsurance is the various evidences of permissibility of insurance and the Fatwas issued by the 2<sup>nd</sup> Seminar of Al Baraka (Fatwa No. 2/9), the 10<sup>th</sup> Seminar of Al Baraka (Fatwa No. 10/3/5), and the Fatwas of the Shari'ah Supervisory Boards of Dubai Islamic Bank, Faisal Islamic Bank, Kuwait Finance House, Qatar Islamic Bank and the Islamic Insurance Company.<sup>(18)</sup>
- The basis of the rulings relating to the Islamic insurance and reinsurance contract is the general principles of contracts in the Islamic Shari'ah such as forbiddance of cheating and fraud, and necessity of commitment to the time specified for implementation of contracts. In addition to these general principles, the insurance and reinsurance contracts are also based on specific rulings pertaining to insurance coverage indicated by the Resolutions and Fatwas issued by the Islamic Fiqh Academy of the Muslim World League, the Supreme Council of Ulema and the Shari'ah Supervisory Boards of Islamic banks and Islamic insurance companies.<sup>(19)</sup>
- The jurisdictions of the company are based on its articles of association, the documents which regulate the contract, the general principles of contracts and conditions, insurance practices and the Fatwas issued by Shari'ah Supervisory Boards.<sup>(20)</sup>
- The rulings that relate to regulation of the relationship between the company and the policyholders are based on the articles of association of the company which specify whether the contract is a fee-based agency or not, in addition to the Mudarabah contract regarding the reinsurance fund.
- The reinsurance coverage is based on the general texts affirming the Hadith which states: "*No harm and no reciprocal harm*"<sup>(21)</sup> and the general rules and principles of Islamic Fiqh which stipulate that coverage should be for the actual harms and not at all for making a wealth out of it. The reinsurance coverage is also governed by the donative nature of the Islamic reinsurance contract and the Fatwas issued by competent bodies such as

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(18) "*Fatawa Al-Ta'min*", (pp. 193 -206).

(19) Ibid.

(20) Ibid.

(21) This is a Hadith narrated by Malik in "*Al-Muwatta`*", *Kitab Al-Aqdiyah*, (P. 464); "*Musnad Ahmad*" [1: 313 and 5: 527]; and Ibn Majah in his "*Hashiyah*" [2: 784].

Fatwa No. (3) of the 10<sup>th</sup> Seminar of Al Baraka and the Fatwas issued by the Shari'ah Supervisory Boards of Islamic banks and insurance companies.<sup>(22)</sup>

- The reinsurance surplus is based on the nature of the donation-based contract and what has been reported by Al-Bukhari about the practice of the Sahabah (companions of the Prophet, peace be upon him) in the case of Munahadah.<sup>(23)</sup>
- Permissibility of reinsurance with traditional reinsurance companies is based on the practical necessity arising from lack for Islamic reinsurance coverage and the dire public need which ranks up as necessity. Shari'ah recognition for necessity and dire public need is supported by a number of Texts in the Qur'an and the Sunnah. In this respect also a Fatwa has been issued by Faisal Islamic Bank of Sudan (Fatwa No. 5/3).

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(22) *"Fatawa Al-Ta'min"*, (P. 153).

(23) Al-Bukhari stated in his *"Sahih"* with *"Fath Al-Bari"* [5: 12]), *Bab Al-Sharikah Fi Al-Ta'am Wa Al-Nihd Wa Al-'Urud* ...because Muslims did not see any harm in Nihd, of which each of them used to eat a part, and he mentioned some Hadiths indicating what he had stated. In his Book *"Fath Al-Bari"* [5: 129], Ibn Hajar said: "Nihd is a practice in which all the people in companionship (on travel) provide the food. Each of them contributes the same quantity, yet some may consume more than others, even though, the remaining food is shared among them if they do not decide to keep it for another journey". This is exactly the reinsurance surplus, or quite similar to it.



## **Appendix (C)**

### **Definitions**

#### **Reinsurance**

The reinsurance contract is a contract according to which the insurance company transfers part of the risks of its insurance commitments to the reinsurance company. The insurance company, therefore, undertakes to pay to the reinsurance company part of the insurance premium paid by the participants, against commitment of the reinsurance company to bear part of the claims as per an agreement between the two parties. Islamic reinsurance has the distinctive characteristic of being based on the same principles of solidarity insurance, as indicated in Shari'ah Standard No. (26) on Islamic Insurance.

#### **Special Need**

Something that concerns a certain group of people, or the employees of a certain profession, as for instance the need for insurance for the employees in trade and industry sectors.

#### **Public Need**

Something that does not concern a certain group of people, or a certain country. Public need is the need that concerns everybody such as the need for Istisna'a.

#### **Reinsurance Commission**

A percentage amount of the contributions payable to the reinsurance company, paid to the Islamic insurance company for the efforts it exerts in mobilizing the reinsured insurance contracts.

#### **Reinsurance Profit Commission**

A percentage amount of the realized increase of revenues over expenses in the reinsurance agreement, paid to the Islamic insurance company as

a bonus for its excellent performance in managing the insurance operations in general, and the reinsured risks in particular.

### **Risk-Sharing Reinsurance**

The process of sharing the insured risk between the Islamic insurance company and other insurance companies, either due to lack of sufficient insurance capacity for such risk, or because of regulatory requirements of risk sharing with regard to the magnitude of the risk in question.

### **Financial Gains of Islamic Insurance Companies from Traditional Reinsurance Companies**

Reinsurance agreements between traditional reinsurance companies and Islamic insurance companies lead to the following financial gains to Islamic insurance companies:

- **Compensations for harms;** the reinsurance company bears a percentage of the risk cover -when the harm materializes- commensurate to the percentage of its share from insurance contributions.
- **Reinsurance commission;** which is a percentage amount of the contributions payable to the reinsurance company, paid to the Islamic insurance company for the efforts it exerts in mobilizing the reinsured insurance contracts.
- **Reinsurance profit commission;** which refers to a percentage amount of the realized increase of revenues (reinsurance contributions) over expenses in the reinsurance agreement (coverage), paid to the Islamic insurance company as a bonus for its excellent performance in managing the insurance operations in general and the reinsured risks in particular, and providing the best services to its customers. Such amount is paid in the form of an agreed upon percentage of the profits of the reinsurance company, as per the reinsurance agreement signed between the two companies. When the reinsurance company earns profits from the reinsurance contracts signed between the two companies, the reinsurance company pays the part of the profits agreed upon to the insurance company.

## **Appendix (D)**

### **A Model Reinsurance Agreement Issued by Islamic Insurance Company – Jordan**

1. The insurance company agrees with the reinsurance company on signing annual agreements with the aim of transferring part of the risk borne by the insurance company, to the reinsurance company.
2. The insurance company assumes beforehand commitment to transfer to the reinsurer the agreed upon part of the reinsured risk, and the reinsurer offers his acceptance. According to the conditions of the reinsurance agreements, the commitment of the reinsurer becomes valid since the time of signing the original insurance contract with the insurance client.
3. The insurance company assumes the commitment to pay the reinsurance contribution against the commitment of the reinsurer to pay its share of the claims, in addition to the commissions agreed upon for the contracts within the signed agreements. It can also be stipulated in the agreement that the insurance company shall obtain a share in the profits achieved by the reinsurer under the signed agreements.
4. The insurance company retains a percentage of the reinsurance contributions (40%) for fire agreements, general accidents and marine and health insurance, as a guarantee for honoring commitments from the side of the reinsurer. The amount thus retained is to be released after one year within the reinsurance agreement. During the period of its retention, the amount is to be invested with the Islamic Bank of Jordan through Shari'ah-acceptable modes of investment, and the reinsurer be given the part of the return agreed upon.
5. The return thus obtained by the reinsurer becomes part of his accounts, and is deductible from the commissions to be received from him, on the



basis of the fact that such amount is part of the cost of the reinsurance operation.

6. The reinsurer assumes the commitment to pay commission to the insurance company. Such commission is determined as a certain percentage of the reinsurance contributions. This amount does not represent a commission in the strict sense of the word. It is rather a contribution from the part of the reinsurer in the direct expenses borne by the insurance company, and which relate to the reinsured risks.
7. Such commissions enter into the accounts of policyholders as part of revenues in the account of the cooperative insurance fund.
8. The reinsurance agreement normally stipulates the right of the insurance company to obtain a specific percentage of the net profits achieved by the reinsurer under the reinsurance agreement.
9. Reinsurance profit commission is calculated at the end of the agreement period, and enters into the accounts of the policyholders as part of revenues.



