

Research Article

Takaful and Public Auto Insurance in the Canadian Context

Alper Bilge* , Saim Kayadibi 

Islamic Economics and Finance Institute, Marmara University, Istanbul, Turkey

Abstract

Many studies have been done on *Takaful*, also known as Islamic insurance within the Muslim community. *Takaful* is seen as the permitted alternative to the conventional insurance system which is deemed forbidden in Islamic law by many scholars due to containing elements of interest (*riba*), uncertainty (*gharar*) and gambling (*maysir*). But little is known about the other Islamic alternative to conventional insurance, which relies on a government or public approach and is presently being applied in Canada. Another option to the dilemma Muslims have regarding conventional insurance should be welcomed in the Muslim community, especially if shown to be better than the current alternative(s). *Takaful* is a non-profit fund created by a group of people to compensate for losses of anyone in the group, which happen due to certain events. From this definition, *Takaful* can be referred to as mutual insurance. Also, *Takaful* is based on contributions or donations, not premiums. Any surplus in the fund can be given back to participants. However, profit can still be generated from investments in the fund and the *Takaful* operator can charge fees to manage the fund. The government, whether local or national, can similarly fulfill the functions of *Takaful*. Conceptual research relying on secondary data will be used in this article to discuss specifically the practice of public auto insurance in Canada and whether public auto insurance is better than private auto insurance. The hope is that after this research, public insurance will not only be considered a viable alternative to private insurance but also applied in Muslim majority states to cover all kinds of insurance that individuals need, whether it be health, auto, life, long-term disability, travel, and other types.

Keywords

Takaful, Public, Private, Insurance, Contract, Auto, Risk

1. Introduction to *Takaful*

Takaful originated from the need to create an Islamic alternative to the conventional insurance system. “The concept of insurance is well-rooted in Islamic economic systems” [3]. The etymology of *Takaful* is derived from the Arabic word “*kaf*” meaning to secure one’s needs [3]. Although there are scholars that say commercial (conventional) insurance is similar to mutual (cooperative) insurance, such that both types are either permitted in Islam or forbidden, “many scholars make the distinction that conventional insurance is *haram* whereas mutual insurance is *halal*” [7]. To make commercial

insurance *halal* according to these scholars, certain conditions should be imposed on it, giving rise to mutual insurance or *Takaful* [6]. *Takaful* is seen as the *Shari’ah* compliant alternative, involving the absence of uncertainty, gambling and interest [3]. Conventional insurance is considered *haram* in Islam by scholars exactly for these reasons - *gharar* to mean uncertainty, *maysir* to mean gambling and *riba* to mean interest.

The conventional insurance contract is perceived as a sale of money for money which leads to the two types of *riba* in

*Corresponding author: alperbilge1@gmail.com (Alper Bilge)

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loans: excess and delay *riba* [7]. In other words, *riba al-fadl* and *riba al-nasiah*. *Riba-al fadl* occurs when the insured receives more or less than what they paid in premiums, which is always the case. *Riba al-nasiah* occurs because the insurance premium payments and claims from policyholders do not happen at the same time. There is both a difference in amount (*riba al-fadl*) and a difference in time periods or a time lag (*riba al-nasiah*).

“But the idea of two types of *riba* existing in insurance contracts is not correct because the arguments presented have to do with different prohibitions, which are *gharar* and *maysir*” [7]. Unlike loan contracts, insurance contracts have no pre-determined “increase” that depend on time delay or amounts paid for, so the excess that the insured receives whenever received cannot be considered interest. Also, premium payments can be considered as co-operative contributions towards the availability of a useful social service [6].

However, another way *riba* can still be involved is if the investments made by the insurance company are interest-bearing. If the insured pay premiums to an insurance company which they know will invest their money into interest bearing investments, then that means they are assisting or taking part in *riba* and helping one another in wrongdoing. “No one can deny the involvement of *riba* in insurance because the insurance companies invest most of their funds in interest-based securities, such as government bonds, private debt securities, and money market instruments” [6]. “Some scholars have said that commercial insurance is permissible if the investments are not interest-bearing” [7].

Insurance contracts contain elements of *gharar*. “Linguistically, *gharar* means risk, peril and danger” [6]. In exchange for a premium, something uncertain is bought from the insurance company by individuals. Clearly in an insurance contract, the policyholder agrees to pay a specified amount of premiums (usually monthly), and the insurance company in return promises to pay a specified amount of compensation in case of disaster [6]. But how the compensation amount is derived in case of an accident is uncertain, along with the amount itself and timing [6]. The amount and timing is uncertain because the risk that is being insured cannot be fully foreseen from the beginning. “Insurance can be seen as the sale of the assurance of danger which does not exist yet and the sale of non-existing things is considered *gharar* according to Islamic law” [7]. In addition, the contract appears to favour the insurance company in instances where the policyholder must cancel his policy before it expires, “making the contract lopsided in favor of one party over the other” [6].

The insurance contract can be thought of as a luck-based transaction or a game of chance, which defines *maysir* or gambling and this is strongly condemned in the Qur'an. “Gambling in insurance is on both sides” [6]. Either the insured or the insurer will end up benefitting when individually considering insurance contracts [7]. From the perspective of the individual policyholder, he or she hopes for a chance to gain a large amount of money by chance and this depends on

luck [6]. The insurance company likewise would hope that the claims they pay out are less than the premiums received from policyholders. This makes the insurance contract like gambling because of the dependence on luck.

However, people do not buy insurance with the aim to get rich, only to secure themselves from future risk. The motive is to protect oneself against future events causing loss instead of gain in the event of winning. As mentioned in a famous hadith of the Prophet (saw), “actions are but by their intentions” (*Sahih al-Bukhari, Hadith 6689*). Another difference between insurance and gambling is that with gambling, there was no risk before the game started but once the game started, the players are all at risk because there is betting and wagering involved on possible outcomes of the game. With insurance, the risk of disaster or calamity happening to an individual was always there, whether the person is insured or not. “So, it is hard to say if the insured are gambling” [7].

Insurance can be thought of as a co-operative system which aims to help others instead of a zero-sum game which is what normally occurs in the case of gambling. Furthermore, “the huge amount of money a gambler wins do not compensate for any actual loss, and it also does not perform any useful social or economic role” [6]. “Whereas in the case of insurance, one is protected from pure risk or peril entailing only losses, which is very discouraging to economic activity” [6]. This is due to the fact that individuals are considered risk-averse and if an option were available to transfer risk to a third party for a reasonable premium payment, they would do it.

To elaborate further on the three reasons why most scholars in Islam have determined conventional insurance to be *haram*, it appears that the strongest argument presented is that insurance contracts contain *gharar*, although there are scholars that have valid counter-arguments against this prohibition as well [4]. *Gharar* exists because if you look at insurance transactions individually, the insured could receive more or less than what they paid in premiums. The same is likewise true for insurance companies except they have an advantage by knowing what those insurable risks are in advance due to the law of large numbers, thereby being able to make a profit. *Riba* appears to only be involved if the investments made by the insurance companies are interest bearing, although there is an argument from a few scholars that what the insurance company does with one's money should not concern him. However, in the financial system today, insurance companies invest in interest-bearing assets and we can prevent this from happening by not dealing with those companies. Finally, it is hard to see the connection between insurance and gambling as what is being sought is protection from risk, not easy gains.

Besides refuting the *haram* aspects of insurance, the same proponents of insurance also argue the reasons why insurance is fundamentally permissible. They have mentioned the great need for insurance due to public interest and necessity. As well as comparing insurance to the permissible financial contracts that have been practiced before, during and after the time of Islam. They are the following: *wadi'ah*, *al-aqilah*,

wala al-Muwalat, *hibah/tabarru*, retirement pensions, and *mudarabah*.

According to these scholars, an insurance policy is similar to *Wadi'ah* or a deposit contract, which “is an agreement between two parties in which one party gives money to another to be kept for the purpose of safety” [6]. Another transaction during the time of the Prophet (*saw*) was *al-aqilah*, meaning that the tribe of the killer that would be responsible for the payment of blood money [6]. This was a type of mutual insurance that was practiced back then. Another contract practiced around that time was *wala al-Muwalat*, where a stranger asks a local to be his guardian and be liable to pay any compensation for any wrongful act committed by him in exchange for inheriting all property owned by him if he passes away [6]. This again is a contract like insurance.

Insurance can be thought of as a social policy for the public interest. It can be used to bring good and avert harm in society. A transaction that eliminates hardship and offers a comfortable life for human beings is in line with what is mentioned in the Qur'an, “Allah (*swt*) intends every facility for you. He does not want to put you into difficulties” (Surah Al-Baqarah, 2: 185) [6]. However, scholars against insurance argue that there is more harm in insurance than benefit due to the unlawful elements of *gharar*, *riba* and *maysir* which they believe exist in insurance. There is one exception where the *haram* is considered *halal* and that happens in the case of *darurah* or necessity. “*Darurah* means not taking action that will lead to the perishing of human life or a bodily organ [6].” Scholars for insurance argue that necessity justifies insurance because of the great need to avert dangers that cause one to lose their wealth. “But scholars against insurance argue that if there is an alternative to insurance (conventional), namely mutual insurance, then it is not allowed to engage in insurance as there is a *halal* alternative” [6].

There is an element of gift or *hibah* in the insurance contract, proponents of mutual insurance argue. The same scholars argue that some *gharar* or uncertainties are acceptable if insurance is based on the principles of *tabarru* or donation. The insurance premiums then would be likened to monthly donations to a preferred charity but with potential financial benefits for the donor. However, a gift requires no compensation and in insurance, the insured pay premiums with the expectation of receiving compensation in the future [6]. There should be no condition of getting anything back from the insurance company if insurance is truly based on *tabarru*. From this sense, commercial insurance is just like mutual insurance. A further point is that even if the *tabarru* principle was followed, dispute could follow later when the insured seeks compensation for damages and the insurance company states that the contributions paid were merely donations, thus having no liability.

“An insurance policy is similar to a retirement pension scheme” [6]. However, an analogy between insurance and pension cannot be drawn up that easily. The system of pension is generally imposed by the state for the benefit of workers,

recognizing their service. The amounts deducted from their salary are to be refunded when they retire and any surplus received on top is regarded as reward for their work [6]. In addition, that pension money belongs to the workers rather than the government whereas in insurance, the insurance premiums paid belong to the insurance company to be invested by the company in any manner desired.

Insurance can also be compared to *mudarabah*, which is a type of profit-loss sharing involving two distinct parties: the party who can contribute money and the party who can contribute time and effort. Such contracts existed prior to Islam but have been accepted as permissible by all Islamic scholars. “*Mudarabah* involving multiple investors (the party with money) can be compared to group insurance, which is a form of insurance that provides benefits to a number of persons under a single contract” [6]. The insured are considered the investors and the insurance company is the agent that devotes their time and effort to manage and invest their funds. Scholars against insurance argue that there are differences between *mudarabah* and insurance. One difference being that in *mudarabah*, the investors share in profit and loss whereas in insurance, the insured do not share in any loss.

After studying both sides of the insurance argument, namely whether commercial insurance is *halal* or not and if not *halal*, what can be done to make it *halal*, the conclusion reached by the proponents of *Takaful* is that commercial insurance can be permissible if certain conditions are incorporated in it. They maintain that the concept of insurance that exists today did not exist during the time of Islam but has similarities to Islamic transactions such as *wadi'ah*, *hibah* and *mudarabah*. These scholars agree on the principle of *bear the burden of each other*, which aims to help disadvantaged groups from unexpected future material risks [6]. They further agree that insurance should be considered as the price of a service instead of a *ribawi* loan [6]. Also, they see no similarities between gambling and insurance. Regarding *gharar*, because of the general need for insurance to protect oneself and others against future economic risk, they argue that it is permissible for *gharar* to exist [6].

Insurance, whether commercial or mutual, does not follow the principles of *tabarru* as the participants paying the premiums expect something in return. Although the AAOIFI (Accounting and Auditing Organization for Islamic Financial Institutions) definition of *Takaful* mentions payment of contributions as donations, in practice insurance is expected to cover all risks of loss of the participants. So, it cannot be said that commercial insurance is *haram* whereas mutual insurance is *halal* based on this argument that some scholars have. Insurance can be likened to a retirement pension scheme or the pooling of resources to help the needy (which include the policyholders) instead of a *tabarru* contract. The nature of insurance is also like *waqf*, meaning endowment and retention of property or wealth for a specific purpose [3]. The emphasis of insurance in general is on mutual co-operation and solidarity.

The main conditions for *Takaful* or to make commercial insurance *Shari'ah* compliant are: sincerity, investment policy, business policy, accounting standard, surplus distribution, and cause of death [6]. "The parties involved must sincerely intend not to engage in an insurance contract for the purpose of material gain; akin to gambling" [6]. Furthermore, the premium contributions from participants should be invested in *Shari'ah* compliant investments instead of *riba* based institutions [6]. Investment income generated by the pool of funds held by the *Takaful* operator (TO) should be distributed on the principle of profit-loss sharing [6].

The participants of the fund must share in losses, unlike conventional insurance. Another *Takaful* model besides *mudarabah* in this regard is *wakalah*. *Wakalah* is a principal-agent relationship, where the principal would be the participants and the agent would be the *Takaful* operator. The TO receives a pre-defined fee or commission for managing effort [3]. In either case, participants stand to lose their funds when investment returns are negative. With the *mudarabah* model, the TO can receive a percentage of the profits whereas with the *wakalah* model, the TO receives no percentage from the profits but receives a fee for services.

Revenue recognition must be recognized on a cash rather than accrual basis so that profit can only be distributed when received. The surplus after all premiums have been paid, claims settled, investment returns generated and administrative costs incurred should be distributed back to the participants of the fund, as that pool of money is considered their property and according to AAOIFI standards on *Takaful*, the operator does not share in the surplus [6]. Finally, in the case of life insurance or other types of insurance where death benefits are to be paid out, the cause of death should not matter whether the death is natural, by suicide or killed while committing a crime [6].

It is these conditions that make *Takaful* stand out from conventional insurance. There is no gambling involved when parties have the sincere intention not to make a profit from engaging in this form of insurance. On top of that, the *Takaful* operator cannot benefit at all from the participants insurance premiums because the surplus must be distributed back to the participants so they cannot exploit the participants. The fund is non-profit by nature. There is no *riba* involved either because the funds held by the *Takaful* operator are not invested in interest bearing investments. Furthermore, the insurance contract itself is not considered a *ribawi* contract because the contract does not imply the literal definition of *riba*, meaning excess or increase. Finally, *gharar* is minimized to an acceptable level in the *Takaful* setup mainly because any surplus funds in the pool will be returned to the participants. On a group level, *gharar* can even be considered non-existent as all premiums and available funds will cover the participant claims and expenses involved in managing the funds, with no profit made by the *Takaful* operator in the event of fund surplus [4]. Due to the cooperative and collective nature of the *Takaful* fund, this insurance setup is free from the prohibitions

of *riba*, *gharar* and *maysir*.

Besides *Takaful*, another possible solution to the prohibitions associated with the conventional insurance system are governments that provide insurance. Public insurance can be thought of as non-profit just like *Takaful* because government is inherently not-for-profit. Government is not there to make a profit from its citizens for any money (usually in the form of taxes) these entities collect are spent on programs, paying down debts and spent on costs with administering the state. There are many well-paid employees inside the government including its leaders but there are no shareholders. The two ways governments can receive funding to provide public insurance to its citizens are: taxes and mandatory insurance premiums. So far, the researcher has not heard any Islamic scholar being quoted saying it is *haram* to pay either taxes or insurance premiums to a government that can utilize these funds for the public interest. It is also noteworthy to mention that if the state requires its citizens to buy insurance and there is no Islamic alternative in that state such as *Takaful*, that is fine from a *Shari'ah* perspective [4].

The same conditions that turn conventional insurance into *Takaful* does not necessarily apply in public insurance. Most conditions such as sincerity, business policy and surplus distribution will not apply. Sincerity does not apply if the government mandates its people to become insured as people have no choice in the matter. Governments do not normally share their profits and losses with their people but generally, any profit or loss that befalls government from the investment returns or in the operations of the insurance fund (premium and claim imbalances), can be shared with their people through lower or higher taxes or premiums. The aim of government again is to not make a profit. Regarding surplus distribution, that depends on how the government intends to utilize the surplus funds but this will generally be done with the public interest in mind. Certainly, the government can decide to distribute the surplus funds back to the participants but the entity can have other uses for these funds to serve the public.

One condition which *Takaful* follows in principle but governments providing public insurance may not is to invest only in *Shari'ah* compliant investments and avoid interest-bearing instruments. The Canadian provinces that provide public insurance do not follow this principle as they are non-Muslim states. However, an Islamic state can follow this investment policy. Other conditions such as cause of death can similarly be agreed to by an Islamic state.

Like typical insurance companies or *Takaful* operators, governments are also able to provide different types of insurance. Currently, many governments around the world already provide universal health care, mainly for humanitarian reasons. Very few governments provide automobile insurance, which is mainly being handled by private insurance companies today. Due to the difficulty of finding a state to live in where public automobile insurance exists, the focus of this research will be on public auto insurance rather than universal

health care. Specifically, three provinces in Canada will be reviewed: British Columbia, Saskatchewan, and Manitoba. In all three provincial states, drivers must pay insurance premiums to “Crown corporations” to be insured so no additional taxes are levied on the residents living in the provinces. Crown corporations are corporations in Canada structured like private corporations but are owned by the government, thereby making them publicly owned. Seeing that these provinces still provide public auto insurance despite the rest of Canada relying on private insurance companies to provide the same, there is expected to be some benefits to this system that the conventional insurance system does not have. These benefits will be discussed further in this article.

2. Public Auto Insurance in Canada

In Canada, most of the population is served by private auto insurers. “However, three western provinces - Manitoba, Saskatchewan, and British Columbia - use publicly owned Crown corporations to provide automobile insurance to their citizens” [1]. Another province, Quebec, uses a hybrid model where bodily injuries are covered by the government whereas vehicle damage is covered by private insurers. “Having three public auto insurers seems to contradict the trend of many Crown corporations being privatized in Canada over the past several decades” [1]. The main argument for privatization is competition of many firms in a regulated market. In other words, the insurance market should be a free market. However, one key reason why these Crown corporations still exist and were not privatized yet, is their ability to provide “low, consistent prices for automobile insurance over divergent components of the population, over a long period of time” [1]. There are four main reasons government is able to price lower auto insurance premiums compared to private firms. Governments are not required to make a profit. Also, any investment income generated from the insurance proceeds are for the benefit of policyholders, thus further reducing costs. Moreover, operational costs (such as underwriting) and commission/broker fees are lower in the public model [2]. In addition to being able to provide low and consistent prices, the government enjoys a monopoly position in the auto insurance market, leading to well-paying jobs, financial reserves and benefits conferred on special interest groups such as auto body repair shops [1]. A monopoly position implies that private auto insurers cannot operate in those jurisdictions with public auto insurance. Providing well-paying jobs are considered given policy priorities of any government. Having access to financial reserves, in this case arising from insurance premiums paid by residents, can be valuable at times such as during budget deficits. Finally, with special interest groups involved that stand to benefit from a public auto insurance model, a change to a private auto insurance model becomes more difficult.

The history of Crown corporations in Canada started after WW2, under the Keynesian ideology. Keynesianism states

that direct intervention into the market by the state is acceptable if not required, thereby leading to the creation of many Crown corporations. Most of these corporations have been privatized later due to neoliberal beliefs (ex. free market capitalism). “Nowadays, state-owned enterprises are on the rise especially in China, given their role in economic development” [1]. In Canada, Crown corporations are still significantly involved in multiple industries but only three when it comes to providing auto insurance - Insurance Corporation of British Columbia (ICBC), Saskatchewan Government Insurance (SGI) and Manitoba Public Insurance (MPI). These three public auto insurers have managed to end direct political interference in their business dealings, being problematic in the past [1]. Much like how today’s central banks operate in the world; business dealings should be free from public influence.

How auto insurance works for residents living in one of the three provinces mentioned, is that all drivers are obligated to purchase the compulsory component of their insurance from the government but they are also able to purchase optional coverage from the same, making it comprehensive [1]. “Normally, this process of buying auto insurance is streamlined with vehicle registration and driver licensing when dealing with a public auto insurer” [2]. This streamlining also ensures that there are fewer uninsured vehicles on the roads - since there is no chance of an individual to get licensed and/or register their vehicle without buying insurance, which is possible under jurisdictions with private auto insurers. The money deposited from the drivers into these collectively owned driver trust funds (plus investment income) roughly equals the money distributed by the Crowns to claimants minus administrative costs [1]. Claims generally cover bodily injuries, vehicle damages and accident benefits such as massage therapy. Administrative costs can be further broken down into acquisition costs, insurance premium tax and general administrative expenses. “Premiums are subject to regulated pricing structures established by authorities and are generally based on non-profit approach with lower operating costs” [2].

Saskatchewan’s SGI is the oldest of the three auto insuring crowns, created in 1945 by the CCF (Co-operative Commonwealth Federation) government [1]. “It was created as a social welfare measure to reduce accident-related poverty, as the province had to cope with citizens injured from auto-related accidents” [1]. Fewer than 10 percent of drivers carried auto insurance prior to the start of public auto insurance in Saskatchewan, part of which were due to high costs [1]. “In addition, significant sums of money were leaving the province as the substantial majority of insurance companies were operating outside of Saskatchewan” [1]. The creation of SGI met with remarkably little resistance from industry or citizens [1]. “Auto insurance was one of the twelve types of insurance originally offered by SGI” [1]. Currently, SGI only offers auto insurance. “SGI also handles drivers’ licenses and vehicle registrations as well as manage comprehensive driver

education and harm reduction programs on behalf of the province” [1].

The other two insuring crowns were created in the 1970s. The creation of ICBC was a goal of the NDP (New Democratic Party; social democratic) government at the time. It was considered a viable means to resolve problems such as lack of competition, high costs and accusations of price collusion among providers [1]. “There were problems with managing claims and paying injured drivers and their families” [1]. “BC (British Columbia) also had high numbers of uninsured drivers on the roads, which the government wanted to eliminate” [1]. All this led to a government proposal to create the ICBC, which the provincial insurance sector was unable to counter-campaign against [1]. In addition to the functions of SGI, ICBC collects fines and promotes safe driving through other public agencies [1].

Like the ICBC, MPI was created by an NDP government due to the same if not similar reasoning. “Auto insurance rates were high, adequate coverage was rare, and private insurance firms treated accident victims and their families poorly” [1]. The leader of the provincial government in Manitoba that time noted how a public monopoly in the auto insurance sector could substantially reduce transaction costs (such as higher court costs or delayed payments) [1].

All three public auto insurers were created by socialist provincial governments who wanted to nationalize insurance, making sense as the left side of the political spectrum desires public ownership of the means of production [1]. However, governments on the right side of the political spectrum (Conservatives) have also used Crowns to meet particular goals in certain industries such as oil or transportation [1]. “The Bank of Canada and CBC (Canadian Broadcasting Corporation) were created by a Conservative prime minister in the 1930s” [1]. This follows from the Conservative tradition that state intervention is acceptable if it promoted business enterprise and economic development [1]. “However, neoliberalism since the mid-1970s questioned the value of state interventionist policies, including the use of public enterprises” [1].

Going back to why these insuring Crowns continue to exist, the reasons can be summarized as follows: low consistent costs for drivers, natural monopolies, ancillary value, vested interests, political issues, and provincial decision making. Governments can provide lower costs not only for reasons discussed earlier but also due to lower transaction costs arising from being a monopoly. These costs tend to be stable for the population since increasing insurance rates would cause political problems for the party in charge but also under a monopoly, there is no risk of the market becoming less competitive due to private firms leaving or forming oligopolies. And as a monopoly, the insuring Crowns face lower transaction costs due to their unitary arrangement in the auto insurance sector. “This type of unitary arrangement brings significant efficiencies associated with uniform insurance claim policies and procedures as well as standardized repair

payment and administration processes” [1].

Ancillary value arises from other functions by the insuring Crowns, such as driver’s license and vehicle registrations in addition to collecting driving and parking infraction fines [1]. “Recently, MPI and SGI worked with Canadian and American border services to issue enhanced driver licenses that enable crossing the border without the need for a passport” [1]. In addition, the insuring Crowns provide well-paying jobs to its citizens. If these Crowns disappear, those jobs may also be lost since many private auto insurance firms are headquartered outside of the provinces these Crowns operate in [1]. Like how any private insurance firm controls large pools of capital, these Crowns are no different. “MPI has their assets entirely invested within Manitoba in the form of provincial, municipal, hospital and school bonds” [1]. The British Columbia government announced it would take funds from ICBC in 2010, perhaps due to budget shortfalls or lack of revenues. These points show how large pools of capital within reach are desirable to any government. Stakeholders that would be affected if the Crowns no longer function would be the provincial insurance brokers that hold licenses which are considerably expensive, the auto body shops that rely on one set of rules for administrative and financial processes, and the Crown’s workforces that are unionized [1].

“Automobile insurance rates are a politically significant household cost” [1]. A premier in New Brunswick (a province of Canada) almost lost an election over the significant rise in auto insurance prices that occurred in his province, even though the auto insurance market in that province was regulated and competitive, because voters held the government responsible [1]. Basically, a steep rise in auto insurance premiums can cause political issues. “Canada, being a large country with a small population, relies on automobiles for most of its transportation needs, and any increase to auto costs is not well tolerated by the masses” [1].

For any government to implement a public insurance system, there will be large establishment costs in the beginning. “Establishing a public insurer will require a significant investment of time and financial resources” [2]. Most of the financial resources will be sent to the capital reserve that any insurer needs to make payments to claimants. The capital reserve is required for emergencies such as when premiums collected fail to be enough to process all claims. This is especially true for catastrophic injuries which may require millions of dollars. Most of the investment in time will be devoted to the training of new staff needed to run the new government agency. Perhaps thousands of staff will need to be hired at the beginning, of which many may be from private insurers. These staff need to be recruited, trained, and accommodated. Other expenses include information technology systems (software and hardware), legal advisory and other subcontractor or professional fees.

In addition to these costs, it is noteworthy to mention that public insurers may not necessarily operate as efficiently as private insurers [2]. The reasons for this are that government

does not have the profit motive or the same incentives to run as private insurers do, and are subject to political decision making. Some political decisions that can impact public insurance are government-imposed rate freezes and lack of funding for non-insurance operations (such as driver education). With prudent management, cost-effective operations and independence from the government, these problems can be overcome [2].

Another drawback with public insurers is that there will be limited choice available to consumers compared with private insurers. Private insurers can give a range of auto insurance options and prices depending on consumer needs and can also bundle auto insurance with other forms of insurance such as home insurance to provide a discount. However, the government cannot do the same, unless of course the government had a monopoly in all forms of insurance and not just auto. Still, the government will be unable to provide the range of prices and options that private insurers can since they will likely implement a one size fits all approach for all its citizens when it comes to insurance.

In general, despite the drawbacks mentioned of public auto insurance, it is still an idea worth pursuing primarily because of the potential lower insurance costs for consumers. Private systems generally cost more due to required profit making by private firms, whether from premiums collected or from the investment income generated, and the additional operational and commission/broker fees involved.

3. Government vs Market Insurance

The arguments reviewed regarding both private and public insurance, or rather government and market insurance, dealt largely with operating costs and transaction fees. Despite private firms supposedly being more efficient than government due to incentives and competition, the government is also efficient in the context of insurance for different reasons. An interesting difference between government and market insurance is that government insurance becomes mandatory, where driver licensing and vehicle registration is streamlined with buying insurance. Whereas in private market insurance, buying insurance is voluntary [5]. There was also the difference of private firms having more options for insurance coverage.

Another big difference between government and market insurance is how the risks are handled and population treated. Both types of insurance feature low-risk and high-risk individuals. “However, market insurance is structurally different in order to reduce risks so that low-risk members have greater benefit” [5]. “With the law of large numbers, private insurers aggregate uncorrelated risks to achieve lower levels of reserves for expected losses” [5]. In other words, when more people are pooled together and the risks that occur to each person are independent, less reserves are required for unexpected insurance claims than if each person were to insure themselves. In addition, market insurers charge premiums

according to the risk levels of everyone. In the case of auto insurance, this happens when young drivers face higher premiums or drivers who have repeated accidents. “What this does is ration high-risk driving which benefits society by reducing accidents and makes insurance more attractive to low-risk drivers” [5]. “The third way private insurers reduce risk is through insurance benefit design, which seeks to control moral hazard (lack of incentive to guard against risk for one protected by it)” [5]. This is done using deductibles, co-insurance, and exclusions of coverage in high-risk scenarios [5]. A deductible is basically a specific amount that must be paid by an individual relating to an accident or risk before an insurance company gets involved. Co-insurance comes on top of a deductible, in that it is a specified percentage of the costs one will pay after the deductible is paid, and from there the insurance company pays the rest. Assuming that the coverage is not excluded in the insurance contract. All three ways contribute to make insurance premiums beneficial for low-risk members of insurance pools despite the operating costs or transaction fees and the subsidizing of high-risk members [5].

How government insurance compares is that since it is compulsory, all available taxpayers (in the example of auto insurance, all drivers) are insured. With more people insured, operating costs should be lower per person as well as reserve requirements. Also, the risks being insured in terms of money become more predictable and quantifiable. However, government insurance is not as effective at reducing risk as market insurance is. Since government insurance is available to all citizens, the occurrence of many losses from a single event such as a natural disaster means that the government must cover all the damages and not just partially, like in the case of private insurers. A second point is that high-risk individuals pay either the same or a little more than low-risk individuals, but not substantially more as in the case of private insurers. This is because price discrimination is not encouraged as government should treat all individuals equally. In other words, the premiums being charged by the government is not appropriate to the risks each person can bring [5]. This benefits the high-risk individuals to the detriment of the low-risk. Finally, the insurance benefit design governments apply is not as robust or capable as the design private insurers apply. There are little deductibles and amounts of co-insurance, if any. Efforts by government to control moral hazard are seldom [5]. “Putting all these differences together, one can conclude that government insurance increases risk-causing activity” [5]. “One can also conclude that private insurers are rewarded for being able to reduce societal risks” [5].

This is not just about bad management or lack of incentives for government to perform better at delivering insurance. These are the principles of government insurance, unlike market discipline. The state must provide benefits to all citizens, cannot pick and choose and seemingly cannot price discriminate either when deciding premium amounts to

charge based on equality. Also, governments must keep voter interests in mind which limit its ability to control moral hazard. When it comes to natural disasters, it is hard to say if government increases risk from ensuring these events but there is an argument that the losses from these events increase with government insurance. This is because locations more prone to natural disasters are not considered when the government insures everyone, creating incentives for builders to build in those locations without having to face higher insurance premiums [5].

As a result, government insurance can end up creating economic and moral problems in society. "In cases where government insurance is funded by taxpayers, there is little to no chance of risk rationing" [5]. Even in the case of universal healthcare (government health insurance), moral hazard can exist. Lack of incentives to guard against risk cause economic losses for society, especially in the case of taxpayer funded government insurance. As for the moral dimension, it is noteworthy to consider that "no loss is every fully compensable" and "every loss is the loss of an alternative opportunity" [5]. This can be fully understood in the case of personal injuries that have lifelong effects but can also be understood from other types of losses that have economic impacts to the detriment of society. Government insurance, like all types of insurance in fact, has a wealth redistribution effect. This is where wealth flows from those who have avoided accidents to those who have not because without insurance, the chance of becoming poor remain high. One humanitarian reason for supporting government insurance is this wealth redistribution effect, that affect all citizens. However, to what extent can this "humanitarian" mechanism be defended if government insurance "increases the frequency and magnitude of loss to the society"? [5].

The government does take full advantage of the fact that because it is serving a larger population that any possible private insurer in the same country or state, this can significantly reduce the cost of insurance for everyone. However, the cost of insurance is still there even if it is provided by the government, and may still be considerably high. "The total insurance costs for the United States in 1994 were \$30,000 USD (United States Dollar) per citizen" [5]. Nevertheless, government insurance remains popular, as it is considered the cornerstone of the welfare state and all individuals seek to avoid risk whether there is a private insurance market available or not. Indeed, government provided insurance can be a solution in situations where there are no private insurers. Also, the government seeks to be inclusive and insure all citizens. "Finally, there is a wealth redistribution effect which is appreciated by all citizens although it really is a redistribution from the low-risk members to the high-risk members of society" [5]. "Yet there is still some benefit to the low-risk members which is why government insurance is still sustainable" [5].

4. Conclusion

The main objectives of this paper were to determine if public insurance can replace *Takaful* in the context of auto insurance and if public insurance is noticeably better than private insurance. Auto insurance was considered since government-provided health insurance is a common occurrence in the world and the next well-known insurance which is usually compulsory is auto insurance. The reason for wondering if public insurance can replace *Takaful* was not due to potential defects nor any Shari'ah compliance concerns but merely to research an Islamic alternative to *Takaful* which might benefit at least one Muslim state that plans on utilizing the concept.

The *Takaful* concept was studied to understand its origins, why conventional insurance is considered *haram*, what differentiates *Takaful* from conventional insurance and how public insurance compares to *Takaful*. To support the concept of public auto insurance, its application was studied in three provinces in Canada - Manitoba, Saskatchewan, and British Columbia. These provinces have had provincial auto insurance for at least 50 years up to this present day. The reasons for why these provinces still have public auto insurance were studied. Finally, the other side of the public vs. private insurance debate was looked at, supporting private insurance over public. The economic and moral rationale for market insurance were studied and why government insurance is considered popular by citizens.

Conventional insurance was found to be *haram* because it involved elements of *riba* due to investment into interest-bearing assets by insurance companies, the existence of *gharar* due to the sale of a non-existent thing which is the unforeseen accident, and an element of *maysir* to a lesser extent, if the parties involved had the intention to make more money from engaging in an insurance contract. *Takaful* corrected these non-Shari'ah compliant elements by making investments of participant funds free from *riba*, utilizing profit and loss sharing for any investment income or loss and contributing any fund surpluses back to the group of participants. Public insurance as a concept, can act like *Takaful*, since all surpluses of the fund eventually flow through to the public in terms of lower fees or more government services and all investment income or losses likewise are shared by all citizens. But the investments made by the funds collected through public insurance should be invested in the same way as *Takaful*.

In the three provinces of Canada studied that administer public auto insurance - Manitoba, Saskatchewan, and British Columbia - all drivers in those provinces are obliged to pay insurance premiums to Crown corporations; government-owned entities in charge of auto insurance. These provinces were found to have lower auto insurance premiums than the other provinces of Canada for various reasons but mostly because government is not seeking to make a profit. Public auto insurance started in these provinces with the Keynesian ideology - that it is acceptable, if not required for

states to intervene in the market. Buying auto insurance in these provinces is streamlined with vehicle registration and driver licensing, ensuring that all drivers are insured. Like *Takaful*, public auto insurance can be viewed as a not-for-profit, social policy for the benefit of its citizens. Besides being a social policy, public auto insurance has ancillary benefits as well, benefitting a wider array of people.

Some counter arguments against government insurance were the following: lack of incentives to run efficiently, political interference, limited insurance options, aggregation of correlated risks, inability to charge insurance premiums according to risk and absence of insurance benefit design to correct moral hazard. However, government insurance can certainly implement features of market insurance. Independence from the state can be maintained, as proven by the example of public auto insurance in Canada. Also, in the example of Canada, citizens pay insurance premiums to the government rather than taxes, so there is potential to implement market features of insurance to ration risk and reduce moral hazard.

Overall, public auto insurance is a viable alternative to *Takaful* operators providing the same. There can still be debates about whether public insurance is better or private but public insurance can be just as good as private insurance, if not better.

Abbreviations

TO	Takaful Operator
AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
ICBC	Insurance Corporation of British Columbia
SGI	Saskatchewan Government Insurance
MPI	Manitoba Public Insurance
CCF	Co-operative Commonwealth Federation
NDP	New Democratic Party
BC	British Columbia
CBC	Canadian Broadcasting Corporation
USD	United States Dollar

Conflicts of Interest

The authors declare no conflicts of interest.

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