Shariah law as regulatory requirement for Takaful undertakings

Prepared by

Prof. Abdussalam Ismail Onagun

Managing Director

11th African Islamic Finance Summit

5th March 2024

at Ambassador Hotel, Hargeisa, Somaliland

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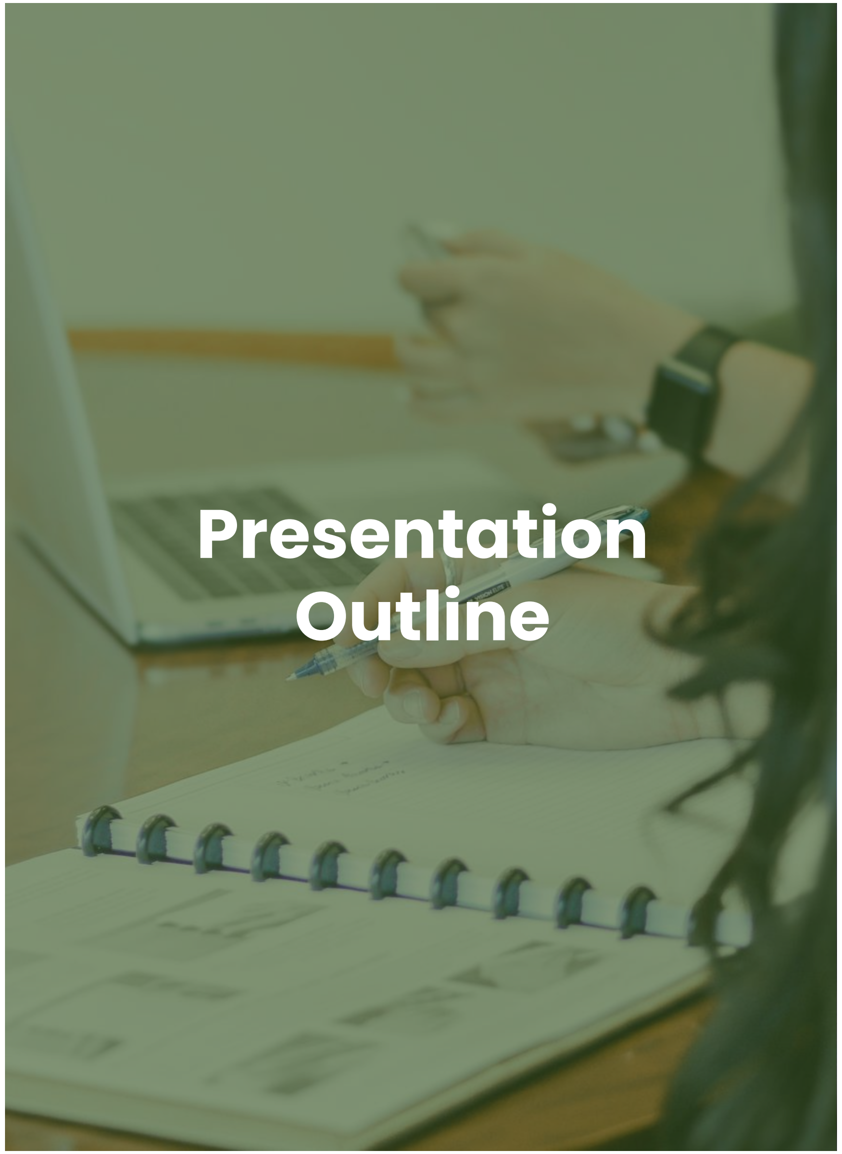

01 Why Shariah in Islamic financial System

02 The Concept of Shariah business law and Shariah rulings

03 Shariah as the basis for Surplus Distribution

04 Shariah as Regulatory requirement for Takaful Business

05 Conclusion and Recommendation

Shariah as regulatory requirement for Takaful undertakings

Introduction

- The Takaful undertaking is one of the developing and growing segments in the contemporary world of Islamic finance. It is Shariah justified scheme adapted in the economy as an alternative to the conventional insurance.

- In 1985, the Islamic Fiqh Academy, organization of Islamic countries, resolved that conventional insurance is haram (forbidden) for it contains element of gharar (uncertainty) and riba (usury).

- However, the Academy approved the use of mutual form insurance that conforms to the principles of the Shariah as an alternative to conventional insurance.

Why Shariah in Islamic financial System

Financial System

Financial system is the system that allows the **transfer of money between savers and borrowers**

Financial Institutions

Financial institution is an **institution** that provides **financial services** in form of **financial intermediaries** for its clients or members

Islamic Financial System and Islamic Financial Institution

The financial system and Financial Institution that comply with ***Sharī`ah*** **rules and principles**

The Concept of Shariah business law and Shariah ruling

Sharī`ah business Law:

it is the practical divine law deduced from its primary sources: the Qur'ān, Sunnah, consensus (ijmā'), analogy (qiyās) and other approved secondary sources of Shariah. .

Sharī`ah ruling:

It is commendations or regulations related to the acts for the subjects divined by *Sharī`ah*

why Takaful insurance

Concept of Takaful Insurance

- A contract whereby a group of participants (*mushtarikin*) agree among themselves to support one another by contributing a sum of money into a common fund, which will be used for mutual assistance of the members against specified loss or damage.

Concept of Takaful undertakings

- A business arrangement whereby a *Takāful* operator manages one or more underwriting funds (*Takāful* funds) belonging to the *Takāful* participants

Takaful undertaking Models

1. Mudārabah model

- In a Mudārabah model, the Takaful Operator acts as a Mudārib (entrepreneur) and the Takāful participants as Rabb-ul-mal (capital provider). As Mudārib, the TO manages both investment and underwriting (of risk) activities on behalf of the Takāful participants. In return, the TO is remunerated by a predetermined percentage share in the investment profit and/or underwriting surplus, which usually would be stated explicitly in the Takāful contract.

Takaful undertaking Models

2. Wakalah model

- Under this model, the TO and the Takāful participants form a principal–agent relationship whereby the TO acts strictly as a Wakīl (agent) on behalf of the Takāful participants as the principal, to run both the investment and underwriting activities. In return for the service rendered by the TO as Wakīl, the TO receives a management fee, called a Wakālah fee, which is usually a percentage of the contributions paid.

3. Wakālah–Mudārabah Model

- Under this model, the Wakālah contract is adopted for underwriting activities, while the Mudārabah contract is employed for the investment activities.

Shariah law as basis for Surplus Distribution

- The Takaful undertaking is win & win model of insurance where the Takaful participants who didn't make claims entitle to surplus. The Takaful fund belongs to Takaful participants and the operator is the manager of the Takaful fund. This is based on the Shariah requirement in the Takaful undertakings.

- According to IFSB, Takaful undertakings is a business arrangement whereby a Takāful operator manages one or more underwriting funds (Takāful funds) belonging to the Takāful participants.

- The term surplus in Takaful is actually the excess contribution over claims payments in the Takaful fund. A surplus in Takaful operations is the total contribution paid by the Takaful participants (insured) less the total value of claims paid (adjusted for any claim recoveries from re-Takaful/reinsurance), less operator fees charged, and less reserves for outstanding claims

Shariah as Regulatory requirement for Takaful Business

- Shariah is a regulatory requirement for Takaful business driver of all segments of Islamic financial institutions which include Takaful undertaking. And before receiving license to operate Takaful business its must have in place Shariah experts who will oversight the activities and operations of the Takaful entity.

- In any country where Takaful insurance business exist among the regulatory requirement from the Takaful authority like National Insurance Authority of Somaliland is the Shariah supervisory Board which this board will oversight the Shariah assurance and control of Takaful operation. Before the license is granted.

- In accordance with IFSB standards "any IIFS shall have in place a strategy for Shariah compliance, using various instruments in compliance with Sharī`ah rules and principles.

Conclusion and Recomendation

- Shariah in Takaful undertakings remains the best alternative insurance as it helps to promote financial inclusion. Takaful undertakings is a market with great potential and is currently witnessing remarkable achievements in various countries in the African region and around the globe.

- Shariah in the Takaful industry offers a huge untapped potential for growth and prosperity as more and more Muslims and Non-Muslims worldwide are seeking better opportunities each day to satisfy both their financial and spiritual needs.