



Takaful: Concepts and Practical Issues

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Agenda

- What is takaful and where are we now?
 - Takaful
 - Basic terminology
 - Market landscape
- Where does takaful come from?
 - Shariah
 - Insurance DOs and DON'Ts in Islam
 - Contracts making up takaful
- Challenges in implementation
 - Shariah interpretation
 - Product development
 - Specialized risks
 - Investments
 - Capital management
 - Rating considerations
 - Other issues
- Summary

What is Takaful?

(And where are we now?)

- Takaful
- Basic terminology
- Market landscape



Takaful

- Islamic alternative to conventional insurance
- What is wrong with conventional insurance?
- Various objections by Muslim scholars against the use of conventional insurance
- In the 1970s and 80s, specific *fatwas* issued by religious authorities cementing the fate of conventional insurance in Muslim majority areas

Basic terminology

- Life Insurance: Family Takaful
- General Insurance: General Takaful
- Policyholder: Participant
- Insurer: Takaful provider
- Premiums: Contributions

- New concepts:
 - Shariah
 - Haram: Riba, Gharar, Maisir
 - Halal: Tabarru, Wakalah, Mudharabah, Qard hasan

Market landscape

- Statistics vary widely, for various reasons
- 2007 estimated contributions (combined general and family takaful)
 - USD 1.7bn – 3.4bn
- Future projections of contributions
 - USD 14bn by 2010
 - USD 7.7bn by 2012
- Estimated number of takaful operators
 - Current: ~ 150
 - 2006: ~ 90
 - 2002: ~ 40
- Geographic split
 - Malaysia and Saudi Arabia EACH contribute about a quarter of the global contributions
 - Most of the rest: Indonesia, UAE, Bahrain, Qatar
 - Iran gets left out due to definition problems
- Growth
 - Globally 20% - 25%, over the last 4 - 5 years (till 2007)
 - 2008, early numbers look strong
 - Future projections: 17% – 25% over the next 5 years

Where does takaful come from? (And how is it different?)

- Shariah
- Insurance DOs and DON'Ts in Islam
- Contracts making up takaful

Shariah

- Islamic Law
 - Halal & Haram
- Sources of Shariah
 - Sources of Islamic finance
 - Quran
 - Sunnah (& Hadith)
 - Ijma
 - Qiyas
- Objective of man-to-man injunctions
 - Benefits to society
 - Equity and fairness

The DOs and DON'Ts of conventional insurance

- **What is haram and what is halal?**
- **Haram (disallowed):**
 - Interest
 - “Riba”
 - Uncertainty
 - “Gharar”
 - Differentiate from risk
 - Gambling
 - “Maisir”
- **Halal (allowed):**
 - Risk pooling
 - Profit sharing
 - Fee for services

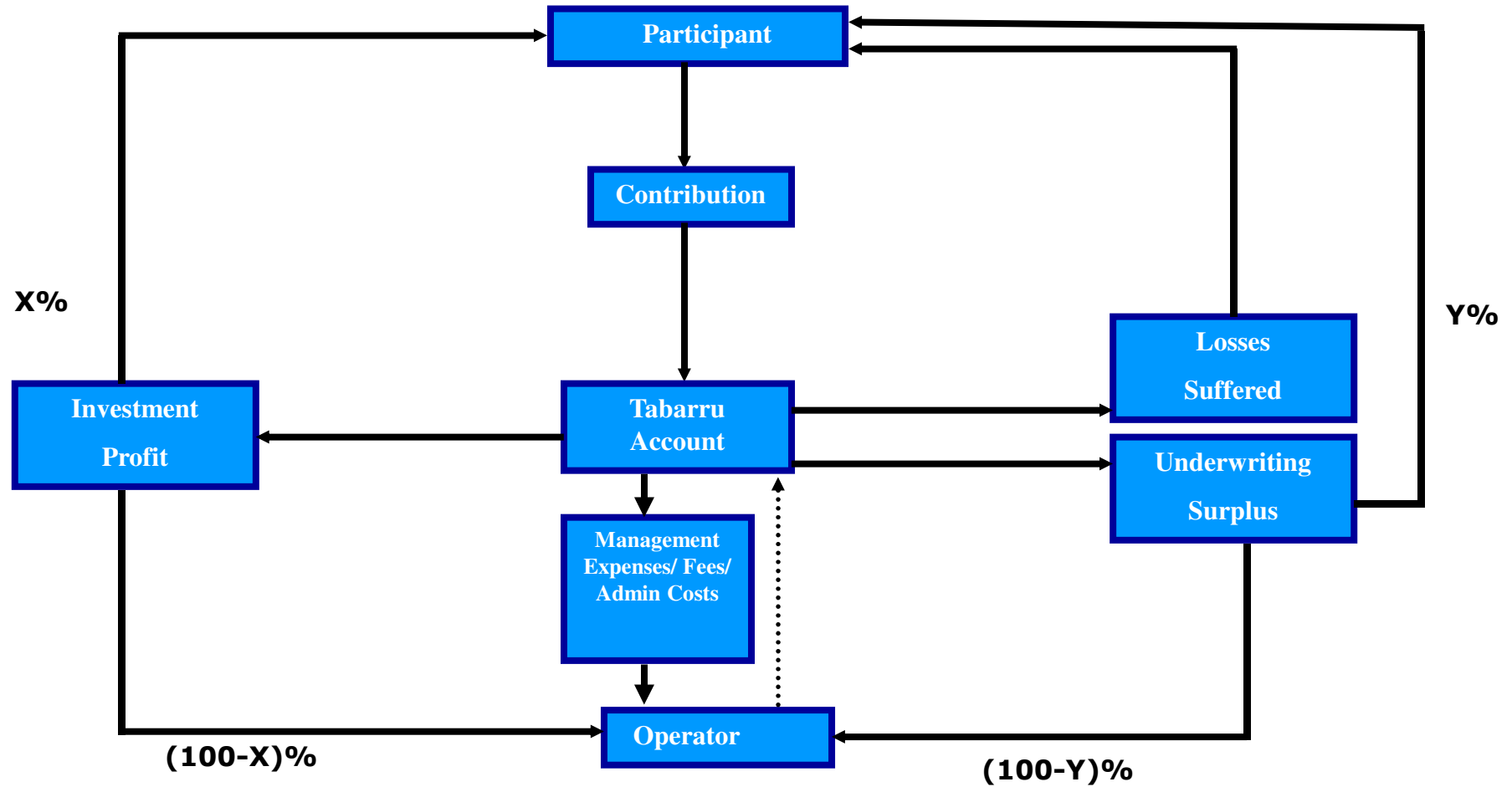
Islamic finance contracts

- A large number of contracts allowed by scholars to cover various needs
- Most relevant to insurance:
 - Fee for services
 - “Wakalah”
 - Profit sharing
 - “Mudharabah”, others...
 - Donation
 - “Tabarru”
 - Loan (interest free)
 - “Qard hasan”



A model for general takaful

An illustrative model



Challenges

- Shariah interpretation
- Product development
- Specialized risks
- Investments
- Capital management
- Rating consideration
- Other issues

Shariah interpretations

- Equity!
 - Is Mudharabah allowed?
 - At what stage is it allowed?
 - How do you minimize “gharar”?
 - How much disclosure is full disclosure?
 - Or is at least equitable?
- Other issues that will be highlighted as we move through the slides
 - Product innovation
 - Product pricing
 - Market penetration
 - Investments
 - Underwriting risks
 - Others

Product development

- Types of benefits/coverages
 - What is equitable?

- Pricing & marketing
 - What is equitable?

- Surplus sharing
 - What is equitable?

Specialized risks

- How do you pool them?
- Re-takaful availability
- Underwriting concentration for re-takaful operators

Investments

- Limited assets
 - What assets are allowed to be invested in?
 - Are there even options?

- Asset & liability mismatch

- Concentration risk

Capital Management

- Risk based capital
 - Limited investment assets
 - Higher charge

- Limits on risk mitigation strategies

- Diversification benefit
 - If each fund is separate, should there be any diversification benefit?
 - What is the risk-adjusted capital?

Rating considerations

- Separation of funds
 - Fungibility of assets

- Qard hasan – is it obligatory?

- Other issues:
 - Investments
 - Concentration of risks
 - Rate of return

Other Issues

- Reinsurance
 - Outwards
 - Inwards
 - Co-insurance
- Taxation
 - Zakat
- Where does the segregation of *halal* and *haram* end?
 - Can bars be covered?
 - How about credit card loans?
 - Can credit cards be accepted?

Summary

Summary

- Concept of risk sharing is not only accepted, but is encouraged in Islam
- However, Shariah scholars object to the way conventional insurance companies conduct business
- These objections led to the advent of modern-day takaful (limited or no *riba*, *gharar*, *maisir*)
- Explosive growth starting early – mid 2000s
- However, various issues are still unaddressed
 - Shariah interpretations
 - Investment options
 - Regulatory issues
 - Capacity considerations
 - Others

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