PAST, PRESENT AND FUTURE OF ISLAMIC INSURANCE

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The Origin and Background of Islamic Insurance

The earliest known history of a more specific Islamic insurance is generally accepted as having been in the early second century of the Islamic era. At that time, Arab Muslims had started to venture out on long trading journeys to India and South East Asia as well as other countries and continents. Due to the nature of these journeys, they often faced risks of incurring losses, owing to natural disasters and other problems such as piracy. Using the Islamic principles of mutuality and co-operation, those Arab Muslim traders eventually agreed to set up and contribute to a fund, which would then be used to compensate anyone among them who had suffered losses through any mishap.

There are many encyclopaedias justifying the fact that the nature of insurance practice had originated from the ancient Arab practices, whereby it became a custom among the tribes of Arabia that if any member of a tribe was killed by a member of a different tribe, the heir of the victim would be paid with an mount of blood money as a compensation by close relatives of the killer. In one of the disputes, the Holy Prophet (SAW) decided as follows:

> Narrated by Abu Hurairah (R), he said that once two women from Huzail clashed when one of them hit the other with a stone which killed her and the baby in the victim's womb. The heirs of the victim brought an action to the court of the Holy Prophet (SAW) who gave a verdict that the compensation for the foetus to be a male or female slave while the compensation for the killed woman is blood money (diyat) to be paid by the 'Aqila' (the relatives of the father's side) of the killer.

The practice of insurance based transactions could also be discovered from the period of the second Caliph, Umar(R). During this period, the doctrine of 'Aqila' had even been encouraged by the government to be practised by the people. Umar(R) had commanded that a 'Diwan' of Mujahideen be established in various districts and those whose names were recorded and contained in the 'Diwan' owed each other a mutual co-operation to contribute sincerely the blood money for manslaughter committed by one from their own tribe. Hence, it

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is presumed here that the application of the doctrine of 'Aqila' had further been developed during the period of the second Caliph of Islam.

During the nineteenth century, Ibn Abidin (1784-1836), a Hanafi lawyer was the first person to discuss the idea of insurance and its legal entity. He was also the first person to discover insurance in the context of a legal constitution, it being no longer a customary practice.

In the twentieth century, a well-known Islamic jurist, Muhammad Abduh, issued two 'fatwas' which mentioned that an insurance transaction is like the transaction of 'Al-Mudharabah' financing technique while the other was that transactions which are similar to endowment or life insurance are legal.

How The First Islamic Insurance Companies Were Formed

With the establishment of the Dubai Islamic Bank and the Islamic Development Bank as the starting point of the Islamic Banking Movement, H.E. Prince Mohammed-El-Faisal-Al-Saud of Saudi Arabia took the initiative for the establishment of a number of Islamic Banks. In one such initiative in February 1976, he held discussions with H.E. Gafar Nimeiry (the then President of the Democratic Republic of Sudan) and asked for permission to establish an Islamic Bank to be operated in Sudan. Executive and Legislative authorities in the Sudanese Government at all levels gave every encouragement and acceded to the proposal. In August 1977 the Faisal Islamic Bank was registered as a public limited company under the Sudanese Company Act 1925.

When Faisal Islamic Bank was established, the Bank authorities initiated studies on the establishment of a co-operative insurance company. In this respect the opinion of the Bank's Shariah Supervisory Board (SSB) was sought. The SSB studied the scheme at its first meeting. Studies continued and several steps followed. The Memorandum of Association and Articles of Association were prepared by the Faisal Islamic Bank authorities. The SSB proposed some amendments which were implemented. The SSB ensured that the scheme was sound from a Shariah point of view as well as feasible from a practical point of view. Therefore, the Islamic Insurance Company Ltd. Sudan was incorporated as a Sudanese Public Company (under the Companies Act 1925) in January 1979. This was the first ever insurance company established in the world to transact business according to the Islamic Shariah. The entire authorised capital of this company had been subscribed by the Faisal Islamic Bank. The company enjoys numerous concession and exemptions. All its assets and profits are exempt from all types of taxes. Further, the assets of the company are not subject to confiscation, nationalisation etc. The company is also exempt from the application of Acts regulating insurance in Sudan.

In Malaysia, the Islamic Insurance Company was established as a private limited company (in accordance with Companies Act 1965) in November 1984 and started its operation from August 1985 as a composite insurance company. This was made possible by the Malaysian Government who in 1982 took a positive step by forming a special body known as the 'Task Force' for the study of the establishment of Islamic Insurance in Malaysia. This task force was formed on the basis of the recommendation of the National Steering Committee on Islamic Banking, which highlighted in its report to the Malaysian Government the need for Islamic Insurance. The Committee felt that it was necessary in order to cater for the insurance requirement of the Islamic Bank which was about to be launched. Members of the task force were drawn from personalities and groups representing religious scholars, legal experts, economic and insurance practitioners. The members of the task force visited a number of Islamic countries and also had discussions with three Islamic Insurance companies already established or about to the established. Finally, in its report to the Government, the task force suggested that an Islamic Insurance company should be established in Malaysia as soon as possible. The Malaysian Government then promulgated legislation entitled 'The Takaful Act', which regulates the Islamic Insurance (Takaful) of Malaysia. It may be of interest to note that in Malaysia the Islamic Insurance Company (known as the Syarikat Takaful Malaysia) is practically a subsidiary of Bank Islamic Malaysia Berhad, which owns 51% of the paid up capital of the Takaful company. The balance of 49% of the shares is owned by the various State Religious Councils and State Religious Foundations within Malaysia.

The Current Scenario in Islamic Countries

The Muslim World has at its disposal resources which can be utilised for economic development. For example, Malaysia and Indonesia possess rubber, tin, timber and oil. The wealth of oil has been a blessing to Iran, Saudi Arabia, Kuwait, U.A.E , Bahrain, Oman, Qatar, Iraq, Libya, Algeria, Morocco, Tunisia, Nigeria and so on. Natural gas is available in Afghanistan, Bangladesh, Pakistan & Iran. Cotton is grown in Pakistan, Yemen, Syria, Egypt, Sudan, Syria, Tanzania & Uganda. Bangladesh has jute, tea, and fish. Pakistan & Egypt grow rice. Yemen, Tanzania and Uganda grow coffee. Nigeria grows cocoa and groundnuts. Phosphates are available in plenty in Morocco, Tunisia, Egypt, and Jordan. Some of the Muslim countries are also rich financially. They are the Kingdom of Saudi Arabia, Kuwait, U.A.E, Qatar and Brunei. Per capita income of these countries is higher than that of the U.S.A. They are known to be the richest countries of the world. This has been attributed to huge export of the oil resource of these countries and very small populations.

The huge financial resources of these countries can be best utilised for the development of their own economies and for the economies of the other Muslim countries. Some of the Muslim countries (Indonesia, Bangladesh, Pakistan) are very rich in terms of human resources but they are not blessed with financial resources. There is ample scope for combining the natural resources, financial resources and human resources of Islamic countries for the advancement of the economy of all the Islamic countries.

In the recent past there has been a continuous awareness among the Islamic countries for coming closer to one another for economic cooperation, and increasing the ties and friendship and brotherhood through joint and united efforts in all their activities. Emergence of Takaful as an alternative to the conventional insurance system has paved the way in the right direction for further cooperation.

What Role Can Takaful Provide to the Muslim Ummah?

In the recent past, the Muslim world has been stirred with an endless enthusiasm and impetus to occupy its real place among the community of nations and contribute its due share and duties to humanity. Takaful is a service to the Muslim Ummah (community) as a welfare scheme. Introduction of Takful is an example how the principles of Islamic Shariah can help to create new socio-economic mechanisms based on equity, justice and fair play.

The objective of Islamic economy is to create an exploitation-free society and the upliftment of the entire society as a whole. The Takaful system, which has been working for the welfare of mankind is not in contradiction with Islam. The objective of the Islamic economic system is the promotion of welfare of people which lies in safeguarding their faith, their life, their posterity and their property. By ensuring and safeguarding these elements of the people, Takaful serves public interest and, therefore, can play a most important role.

An exploitation-free society which Islam envisages, has provisions for adequate capital formation. The Prophet of Islam disapproved of begging and encouraged capital formation. He advised a poor companion to sell all his belongings to purchase an axe for collecting firewood to sell in the market. The Takaful system will facilitate capital formation of individual households. This will motivate every individual to accumulate savings under Family Takaful and the collective surplus funds will be invested in the capital market. This will facilitate further utilization of resource and greater employment.

As the Islamic countries are likely to shun the venoms of nationalism and reap the fruits of Islamic Brotherhood, they should enhance trade among themselves. Islamic countries possess agricultural, industrial and financial resources. They need to exchange these resources through trade and commerce. A general Takaful scheme will facilitate trade, commerce and best utilization of these resources. It is found that most Muslim countries are not self-sufficient in all types of required goods and services. This creates the root from which trade prospects among the Muslim countries stem.

Material progress in full measure is desired by Islam. But on the other hand one main objective of Islam is to change and build up people's outlook and values. This makes it possible to establish justice in economic matters. This can be achieved not only by applying laws only but also through a voluntary socio-economic system. Takaful is considered as a socio-economic device through mutual cooperation and mutual complementarity as envisaged in Islam. The first policy of the Prophet (P.B.U.H) which was put into operation was the establishment of a brotherhood between emigres (Muhajirs) and inhabitants of Medina (Ansars). The Prophet encouraged both the Muhajirs and Ansars to engage in limited partnership. The Ansars owned the cultivated fields and the Prophet insisted that the Muhajirs engage in cultivation in these fields without assuming ownership rights. The Takaful mechanism encourages this kind of limited partnership as a mode of investment and can play a key role for the betterment of Muslim Society throughout the world.

How Takaful Suits an Islamic Economic System

Islam is the second largest religion in the world with one and quarter billion followers. In all, Muslims form a majority of the population in over forty countries. Muslims live in 184 countries comprising about 20% of world population. Islamic countries and other countries with a significant Muslim population in the recent past have encouraged the provision of financial services, including insurance, under Islamic principles. As a result more than sixty Takaful/ Islamic Insurance companies have been established for providing insurance coverage both in the life and non-life sectors. These insurers generally known as Takaful operators are found not only in Islamic countries but also in Europe, North America and Australia. This type of modified insurance mechanism is expected to further influence the supply of and demand for insurance in the Muslim community.

Takaful has grown not only as an innovative financial instrument, but also on religious principles. The purpose of religion is the well- being of mankind. Islam is a religion which seeks to order human life so as to make it actualise the pattern intended for it by its Creator. Islam is not only a religion but an ideology in the sense that the Shariah, its law, has given the Muslims a pattern of life with which to order their lives. The Shariah is comprehensive, embracing all human activities, defining man's relations with God and with his fellow men. The Shariah grew out of the attempts made by early Muslims as they confronted immediate social and political problems to devise a legal system in keeping with the code of behaviour called for by the Quran and the Hadith. The purpose of Islam is always to inject morality into the fabric of human relations. How a Muslim earns his livelihood, how he spends his wealth and how his wealth is to be disposed of after his death, all these are the stuff of Islam. In Islam, the human aspect is more important than the material one. It relies more on moral, ethical and human aspects than on the material aspects. This is something unique in the Islamic Economic system.

Prophet Mohammad said,

"*One who eats to his heart's content, while his neighbor starves, is not a Mumin*"

Helping neighbours, poor relations and the distressed contributes to an exploitation-free society based on the principle of brotherhood.

Understanding the fundamental principles of the Islamic Economic System is necessary in order to have a better understanding of the role of Takaful and its suitability in the Islamic economy. For example, the right of private ownership accorded by Islam is not absolute and unconditional. The ownership is a kind of trust only. An individual may privately own and manage any kind of wealth, but he can not do with them whatever he likes. He is to regulate the uses according to the Shariah Law. An individual can make joint investment to earn profit from his investment. Takaful is a means whereby investments of surplus funds are made by the Operators and profits are distributed to the Participants i.e. to the owners of the capital.

Another fundamental principle of the economic system of Islam is that it stands for equitable distribution of wealth. Islam encourage people to be selfless helpers for one another by arousing in them feelings of sympathy. Takaful is a system where people are encouraged to contribute money for mutual help in times of need. Thus, Takaful comes to the help of distressed fellows by means of mutual cooperation and joint guarantees.

The Islamic Economic system combats the accumulation of wealth and its concentration in the hands of a small minority. The Islamic Law of inheritance provider for the shifting and distribution of wealth in a manner unknown in other legal and economic systems. It divides the estate of the deceased over a wide range of beneficiaries and not on a single heir to the exclusion of others. The nominee in a family Takaful scheme is only a trustee, and the policy money needs to be distributed to all the heirs.

The Islamic system requires that wealth should be utilised as an instrument to serve the interest of the community at large. In the Islamic way of life, some special kind of levies are imposed. The objective behind them is to provide financial assistance to the people in lower income brackets with the money of the relatively better off people. In Islam, there are various kinds of compulsory levies ranging from a very high rate of 20% of income to the minimum of 2.5% of income. These levies are for the poor and needy. This is an automatic mechanism of balancing income in society. Islam makes it obligatory for every Muslim who possesses a certain limit of annual income to pay a certain percentage of it for the destitute and needy. This is called Zakah. It is such an important part of Islam that the instruction of the payment of Zakah always comes next to Salat (prayer). The prophet described Zakah to be one of the five pillars of Islam.

The Takaful companies which create a fund to meet unforeseen losses of individuals, and also the contributions and donations made by the Participants in a Family Takaful Scheme, become Zakatable assets. A Takaful Operator, therefore, must arrange payment of Zakah out of these funds for the poor and the needy. There are broadly eight heads of expenditure of Zakah, each of them includes people in need of financial assistance. All the poor and destitute temporary, or permanent, are covered by the financial assistance system of Zakah. The Takaful system, therefore, not only provide security for the people who participates in the schemes of Takaful but it is also a means for providing financial assistance to the needy people of the community and a mechanism of obligatory social security.

Zakah is of course not a substitute for income tax. It is imposed on capital. Zakat has to be levied annually whether it is invested or not. Therefore, it is prudent for the owners and managers of the fund to invest it in productive purposes. As a result, it is an inducement for all the resources and wealth of the economy to be employed continuously in productive activities. By implementing a Zakah system within the mechanism of Takaful, it helps develop the economy towards growth and prosperity.

How Takaful is Beneficial

It has been estimated that annual overhead expenses of property insurers account for about 30% to 50% of their earned premiums. This means a major portion of the premiums paid by the policy holders would be used for doing the business and earning profit for the shareholders. Therefore, it is obvious that the insured and the society obtain the benefits of insurance jointly against the cost of obtaining this service. However, it can be seen that the cost of operating the Takaful business will be comparatively lower under the Islamic system. It is well understood that when the surplus (profit) is shared by the policy-holders, the cost of obtaining the service would be lower in the Islamic Insurance (Takaful) system, at least to the extent of surplus funds being returned to the policy-holders.

Moreover, the insureds in the conventional companies have to bear the costs for losses which are intentionally caused or exaggerated. Although, there are no reliable estimates as to the extent of losses that are intentionally caused, insurers are well aware that many claims are being paid against losses which are intentionally caused by some unscrupulous insureds in order to collect on their policies.

It is also observed that there is a tendency to exaggerate the extent of damage and losses that result from purely unintentional loss occurrences. There are a lot of examples. When it is known that an insurance company is involved there seems to be an unmistakable tendency to exaggerate the extent of loss by surveyors, repairers, medical practitioners, solicitors as the case may be. This is done in collusion with the dishonest insureds.

It is expected that the costs of exaggerated and intentional losses would be much lower, if any, under the Islamic insurance system. This is mainly because the insureds under this system are those God-fearing individuals who want to lead an honest life and as such should not indulge in such unfair and unethical practices for the temporary gains in worldly affairs. Since the Islamic insurance companies will be basically operating on the principles of 'Mutuality' it is very logical that the net underwriting gain of Islamic Insurance companies will be higher compared to corruption-prone conventional insurance.

How Takaful Came Into Being in Malaysia

In the early eighties, Malaysia legitimised the operation of Takaful companies with enactment of the Takaful Act by parliament, vesting with the Central Bank of Malaysia (Bank Negara) the authority to regulate the Islamic insurance industry and to monitor the compliance of companies with the letter of the law. Syarikat Takaful Malaysia Sendivian Berhad, STMB, a subsidiary of Bank Islam Malaysia Berhad, was the first to obtain a Takaful operation license in Malaysia under the new Act. It was incorporated on 29 November 1984 with an authorized capital of RM 100 million and a paid-up capital of RM 10 million, and commenced its operation eight months after its incorporation. Since its establishment, STMB has been actively involved in Islamic Life Insurance-Family Takaful and General Takaful, each with its own unique characteristics.

The aim of the General Takaful Scheme is to provide compensation in case of accidents, much like any conventional insurance fund. The difference is the mutual nature of the fund where the source of funds for any claim settlement with an insured is the contributions made to the fund by other participants. Upon receipt of premium payments, STMB acts as trustee to invest the money in acceptable opportunities and to channel back into the fund the returns on theinvestment less the operating costs. After settling all the claims, any residual amount will be distributed between STMB and the participants based on a previously agreed-upon ratio. The coverage period under this scheme is shorter than the Family Takaful Plan.

In attempts to promote greater competition, possibly leading to a wider selection of Islamic insurance products as well as lower premiums, a second license was issued to MNI Takaful Sdn Berhad to operate Islamic Insurance in Malaysia. Eighty percent of the shares of the new company are owned by Malaysia National Insurance Sdn Berhad, the largest local insurance company. As the public may have the misconception that there are few differences between STMB and MNI Takaful, and since STMB was already well established in the Takaful market, MNI had to find ways and means to highlight its uniqueness. The marketing strategies of MNI Takaful were to increase public awareness of Takaful, to make Takaful more accessible to its customer at "any time, any place, anywhere," to utilize the technological means in meeting their objectives faster, and to establish cooperative efforts with other financial institution in promoting Takaful. It has assembled a strong marketing force and sales executives, as well as a highly motivated group of agents. The company has also explored other channels - banks and posts offices, for example - to reach potential customers. At present, there are everal other Takaful operators. They are basically following the Mudarabah model of Islamic Insurance. Some of there are practising Takaful operation as the Wakal Model, wherein reasonable service charges are being borne by the participants.

How Takaful Was Launched in Singapore

A 1990 convention tolaunch the Association of Muslim Professionals (AMP) was probably one of the first occasions when the idea of Islamic insurance was brought to the attention of Singaporeans. Together with Islamic banking, Islamic insurance was viewed not only to promote the economic development of the Muslim community in Singapore, but also to help Singapore's aspiration to be a front-runner in the race for financial market superiority in the region. Five years later, in September 1995, Islamic insurance was officially launched by two separate Muslim groups - a joint venture consisting of Ampro Holdings Singapore and NTUC Income, as well as another cooperation between the Singapore Malay Teachers' Multi-Purpose Cooperative Society (SKSGMS) and Keppel Insurance.

The Ampro-Income tie-up is targeting, as its primary market, the 15% Muslims of of the 3 million Singaporeans. The main aim of this tie-up is to ensure that Muslims in Singapore are provided with means to obtain insurance coverage that does not compromise their religious beliefs. The reasons why NTUC Income was chosen for this cooperation, and not the others, may be the company's relatively large number of Malay insurance agents, and the fact that NTUC Income is not an only-and-all revenue generating entity.

Keppel Insurance whose products are marketed through a cooperative subsidiary set up with paid-up capital of $500,000, on the other hand, acts only as an underwriter in their endeavour with SKSGMS. While Ampro emphasizes its Takaful Fund as its single product, Keppel prefers to offer a wider spectrum of products, ranging from Group Family Takaful to whole-life insurance, endowment and other investment-linked products. Their strategy is to invest about 75% in Singapore's more stable and mature stock market and 25% in Malaysia.

One common type of Islamic insurance instrument currently available to the 18-65 year olds in the Singapore market is the Family Takaful Fund which combines the life insurance element of Family Takaful with a direct investment scheme. Here, in addition to the fundamental objective of promoting a more equitable and just position among the parties involved through its profit-sharing program, policyholders' family members are provided with financial support in the event of unfortunate accidents. In order to comply with the Shariah, policyholders are informed of how their money is used, the source of the profits, and also how the profits are shared.

To join the scheme, a minimum single-premium contribution of $ 4,000 must be paid, either in cash or from the policyholder's retirement account in the Central Provident Fund (CPF). The amount of coverage expands as premium contribution increases, and the holders of the policy may choose to take up any of the supplementary benefits - Permanent Total Disability, Personal Accident, and Hospitalisation. The maturity of the policy varies from 10 to 40 years, and the premiums received are guaranteed to be invested in halal stocks - those of businesses that do not violate the Shariah. The profits generated from such investment activities are distributed among policyholders as bonuses. Policyholders may surrender parts of the units under their name at any time, or may purchase additional units if they so desire.

How Islamic Insurance Has Grown in Indonesia

In May 1995, the (then) Minister for Research and Technology B.J. Habibie officially declared PT Asuransi Takaful Umum operational as the first Islamic institution to provide general insurance. On February 24, 1996, PT Syarikat Takaful Indonesia was set up as a holding company for PT Asuransi Takaful Keluarga's life and PT Asuransi Takaful Umum's general insurance operations.

PT Asuransi Takaful Keluarga is the only Islamic life insurance company, among Indonesia's one state-owned, 37 privately owned, and 16 joint-venture life insurance companies. Following its inception, PT Asuransi Takaful Umum set its goal to reach a premium target of Rp 3 billion by the end of 1995. The first Director of PT Syariakat Takaful Indonesia, Rachmat Husen, thought it would be possible that in just six months Asuransi Takaful Umum should have the capability to collect that amount of premium. In early December 1995, having been entrusted by an American oil company to manage their insurance fund, Takaful Umum not only achieved its premium target on time, but surpassed it at Rp 3.19 billion. By December 1996, PT Asuransi Takaful Umum's gross premium increased by 34% to Rp 4.30 billion. The company recorded an increase in pretax profits of 188.21% amounting to Rp 758 million as of December 1996, from Rp 263 million at December 1995.

PT Asurani Takaful Keluarga, similarly, experienced a large increase of 207.41% in life insurance and annuity premiums - from Rp 3.24 billion as of December 1995, to Rp 9.96 billion by December 1996. In terms of profits, however, this company did not perform as well as ATU - it showed a deficit of Rp 409 million in December 1995 and Rp 923 million in December 1996. Despite the losses, in terms of membership, PT Asuransi Takaful Keluarga Currently ranks 13th among the 56 registered life insurance companies with the Dewan Asuransi Indonesia (DAI).

The Indonesian Takaful industry has further spread its market base by penetrating the oiland gas industries, which traditionally have been monopolized by Pertamina owned insurance companies. It has established ties and cooperation with various Islamic organizations, such as Muhammadyah and Nahdlatul Ulama whose combined members total more than 40 million. The market is not fully tapped yet and the Takaful industry is set to grow further in Indonesia.

The Efforts Taken for Islamizing Insurance in Pakistan

The insurance contract is an important contemporary issue which has attracted the attention of Shari'ah scholars and Islamic economists. In Pakistan many scholars wrote articles and books regarding the Islamic status of insurance business. But very little work has been done on the alternative system of insurance which should satisfy Islamic principles and objectives. Only two efforts are known by now. One is by Mufti Muhammad Shafi, an eminent Shariah scholars and the other is by the Council of Islamic Ideology of Pakistan. Mufti Muhammad Shafi, while responding to a questionnaire from Majlise-e-Tahqiqat Shariya Lucknow in 1964, not only analysed the existing insurance business but also proposed an alternate modelof Islamic Insurance. The Council of Islamic Ideology (CII) Pakistan reviewed the existing insurance practices and suggested an Islamic alternative. The council examined the laws governing the insurance business in the country in 1984. It analysed eleven such clauses and expressed its opinion about them in a brief report to the government, which was in March 1984. The council further decided to constitute a working group to analyse the existing system and frame a new system of surety and assurance in accordance with Islamic teachings. The working group included besides the Ulama members of the council, economists, the heads of the government insurance companies and other insurance experts. The working group prepared a preliminary report on insurance, but due to the expiry of the tenure of the council, this effort was discontinued.

In 1990 a new council came into existence which decided toform another group to complete this task. The working group comprised of six members of the council and four representatives of major insurance corporations. The group also benefited from the expertise of around twenty scholars and insurance experts to understand the nature and functioning of the present system and to develop an alternative system. The group prepared a report in 1992 and submitted it for consideration by the government. In this report the group reviewed the history of insurance and its present forms. It also looked into the status of insurance from the Shariah point of view and found that in the present form it involves the elements of Riba - speculation and gambling. The group also reviewed the functioning of Islamic insurance (Takaful) companies, working in different Muslim countries, for developing a practical model for Islamic Insurance and suggested an alternative system based on the concept of Mudarabah and Waqf. But no practical step has yet been taken for the Islamization of insurance.

What is the Potential of the Takaful Industry?

In contemporary Islamic countries, the role and importance of Takaful has not been duly recognized by the policy makers. Even the growth of conventional insurance is not very satisfactory. If we look into the present scenario of the insurance sector of the D-8 member countries, we find a dismaying picture. The following tables show insurance density of D-8 member countries and middle-east oil-rich countries.

TABLE A: INSURANCE DENSITY OF D-8 ISLAMIC COUNTRIES

Country	Population (million)	Per capita GDP	Per capita Premium Non-Life	Life	Total
Bangladesh	135	$ 1,260	$0.6	$0.7	$1.3
Egypt	65	$ 2,900	$ 9	$ 2	$ 11.0
Indonesia	210	$ 3.770	$ 8	$ 6	$ 14.0
Iran	68	$ 5,200	$ 23	$ 3	$ 26.00
Malaysia	23	$ 10.750	$ 62	$ 78	$ 140
Nigeria	107	$ 1,380	$ 7	$ 1	$ 8
Pakistan	132	$ 2,300	$ 2	$ 1	$ 3
Turkey	64	$ 6,100	$ 21	$ 4	$ 25

TABLE B: INSURANCE DENSITY OF MIDDLE EAST ISLAMIC COUNTRIES

Country	Population (million)	Per capita Premium Life	Non-Life	Total
UAE	2.6	$ 58	$ 252	$ 310
Qatar	0.6	--	$ 260	$ 260
Lebanon	4.3	$ 19	$ 93	$ 112
Kuwait	2.1	$ 16	$ 77	$ 93
Oman	2.5	$ 14	$ 52	$ 66
Saudi Arabia	20.5	$ 0.6	$ 37.5	$ 38.1
Syria	15.8	$ 0.1	$ 16.5	$ 16.6

If we compare insurance density of these Islamic countries with that of other leading countries of the world, we can understand where we really stand. For example, in South Africa the proportion of insurance premium to GDP is more than 20% in comparison to 3.5% in Nigeria. In Bangladesh insurance penetration is less than 1%, whereas in Japan premium per capita is approximately US $ 3,900, and in Malaysia it is approx US $ 140, and in Bangladesh it is less than $ 2.00 (two) only. This means that there is ample scope for growth of Insurance vis-a-vis Takaful in Islamic countries.

The Takaful market is bound to grow with the pace of the economy. The growth of the Takaful industry and the economic development of these countries are interdependent. Although the demand for Takaful is a reflection of income and wealth, it is to be noted well that risk consciousness is very low in Islamic countries. There is an urgent need to create a deeper understanding and awareness among the policy-makers of the role that Takaful can play to improve the well- being and quality of life of the Ummah.

Takaful has been designed to help and stabilize the financial situation of individuals, families and organizations. At the same time Takafukl operators can meet the financing needs of large projects, thereby helping the national economies by enlarging the set of feasible investment projects and encouraging economic efficiency. Takaful will definitely help to foster a more efficient allocation of capital and resources of Islamic countries, by way of promoting trade, commerce and entrepreneurial activities. A growing Takaful and Re-takaful market is an instrument for economic growth of the Islamic countries. In fact, the development of Takaful as an alternative to conventional insurance will contribute to economic prosperity of Islamic countries. On the other hand, with the growth and development of the economy, the Takaful Industry will grow.

It is obvious that Takaful is a suitable alternative to conventional insurance for Muslims. But, the pertinent question is how best it can serve the needs of the community. There is no doubt that Takaful has a vast potential for growth, and this potentiality will definitely increase in the coming years. However, the future of Takaful will largely depend on how the increasing potential is being exploited by the Takaful operating system, keeping in view the need of the Islamic economy and state of affairs in Islamic countries.

The religion and culture of Muslims are plus points for Takaful operators. But, that is not all. Political and economic stability of the Islamic States, professional maturity of the Takaful Operators, ability to design appropriate products and reducing management expenses including distribution costs, are some of the important factors for influencing the demand of Family Takaful. The factors which will influence the demand for General Takaful are growth of trade, commerce & industry as well as risk potentials and their severity and frequency. Of courses, risk awareness is another important factor.

The growth of both Family Takaful and General Takaful will depend on the marketing strategies, distribution network and adoption of improved information technology. Last, but not the least, the supply of Takaful in Islamic countries will depend mostly upon the support and sympathy of the policy-makers. If the concept of Takaful is not properly understood, the legislators may not subscribe to the idea of promoting Takaful, and the floating of Islamic companies under the Conventional Insurance Act will simply mislead consumers. Since an effective regulatory system play a great role in the dynamics of supply, it becomes the responsibility of the Regulatory Authority in Islamic Countries to frame appropriate laws and rules for facilitating the growth of Takaful for the benefit of the community and of course for the growth of the economy as a whole.

It is obvious that the interaction of demand and supply will determine the consumption of Takaful. The shift in demand for Takaful will occur as it is an innovative product and suits the socio-economic and religious teachings of Islam. Moreover, Islamic countries are likely to have economic growth both at the micro and macro level. However, the major increase in the consumption of Takaful will result from the increase in the supply of Takaful. The demand already exits. The extent to which it is tapped would depend on the extent to which the supply curve moves to the right.

What Are the Future Prospects of Takaful?

Currently, there are about sixty 'takaful' operators world-wide. During last twenty years, Islamic Insurance (takaful) has developed mainly in Sudan, Saudi Arabia, Iran, Malaysia, Brunei, Indonesia, Singapore, Bahrain, Bangladesh, Bahamas, Belgium, Switzerland, and in the USA. On the other hand, there are at present 45 countries in the world having some form of Islamic banking operations. Interestingly, Takaful is seen in the non-Muslim world as well. For example, in Singapore there are less than half a million Muslims (15% of the total population) but at least two operators are now providing takaful scheme there. In non-Muslim countries, the scheme is also likely to grow if the operators can prove their worth in comparison to conventional insurance products. In Muslim countries, Malaysia seems to be the single most successful country in terms of takaful. In Singapore, about 22% of the present takaful policy holders are non-Muslims.

Most Islamic countries suffer from the common attitude that insurance is undesirable. There is mass non-awareness among the Muslim about risk management and insurance, not to speak of takaful. In most of the Muslim dominated countries of the world, insurance still accounts for less than only one percent of the country's G.D.P. However various surveys have shown that the life and general insurance market has large potential to be exploited in Muslim countries, and in countries where Muslims are at least 10% to 15% of the total population. Takaful is likely to grow along with the conventional insurance schemes. But this is only when this new form of insurance should provide at least equal, and better value, as compared to the existing conventional insurance policies.

The growth of Islamic Insurance companies would serve as the vehicle of the risk management process and provide means of investment and project financing of respective countries. But there is a marked absence of Islamic insurance in almost all Muslim countries mainly because of non-awareness. Therefore, there is the need to educate the Muslim population on the importance of insurance and on the availability of insurance product conforming to the needs of Muslims, on the basis of Sharial Law. There has to be coordinated and concerted efforts of all concerned in society to make Takaful popular.

The Role of Government in the Islamization of the Insurance System

By now, Takaful, like Islamic Banking has become a viable reality. Due to inherent Shariah principles which are universal in character, the Takaful business should be more appealing in the coming years for both the Muslim and non-Muslim communities.

Takaful (Islamic Insurance) has bright prospects and potentialities as a financially viable and competitive alternative insurance for Muslim Countries, because most of the Muslim Countries having Islamic Banks have also welcomed Takaful as a necessary complement to Islamic Banking. Islamic Banking cannot be fully Shariah based unless there is Takaful to take their insurance business. Therefore, Takaful like Islamic Banks, has proved its viable reality and is making strides of expansion in almost all the Muslim Countries.

The confidence and faith of Muslim countries in an Islamic economic system is gaining solid ground. The Heads of States and Governments of Bangladesh, Egypt, Indonesia, Iran, Malaysia, Nigeria, Pakistan and Turkey met in Dhaka on 1-2 March 1999 for the Second D-8 Summit with the objectives of implementing projects and programmes of co-operation that are of vital interest to their peoples. Among other issues, the heads of the State endorsed the proposal to enhance the capacity of existing the Retakaful company of Malaysia to meet the needs of member countries of D-8. It was further agreed that the experts of these countries will meet to draw-up a modus-operandi and formulate appropriate strategies to promote Takaful and Retakaful. It is heartening to note that Takaful operators are organising seminars and conferences on a regular basis and exchanging ideas and information to make Takaful viable.

Government has to perform an active role in Islamization of insurance in the country. Islamization may take place in two ways. The first way is to restructure the whole insurance sector on Islamic foundations and the second is to allow some Islamic insurance companies or some old firms to transform their business on Islamic lines keeping the existing set-up as it is. These two approaches require different strategies on the part of the government.

In the former case, the government may promulgate a regular detailed and codified law to reorganise the insurance industry in line with Shari'ah principles. This law should reflect the true spiritof mutual help and co-operation. All the elements making the present insurance practices un-Islamic (e.g. interest, gambling, gharar) should not be allowed in any circumstances. Some Islamic countries such as Malaysia and Sudan, have already enacted such laws which can be used as guiding examples.

However if the government opts for the latter approach, then it must make suitable changes in the existing Insurance Act to create a favourable environment fort new companies to be established on Islamic principles. Some laws are hurdles for running the business according to Islamic principles. Moreover the government must facilitate and encourage these companies by providing them incentives such as tax exemptions in their early period of establishment. This may help the existing conventional insurance companies to restructure their business on Islamic lines. A time frame may also be decided by the government for complete transformation of conventional Insurance business into Islamic Insurance.

Another function which the government should perform is the reinsurance arrangement. Presently insurance companies, have two kinds of re-insurance arrangement, (i) with the Sadharan Bima Corporation, (ii) with foreign insurance companies. In both of these arrangement, the insurance company enters into a similar type of contract with the re-insurer as one between an individual and the insurance company, including all un-Islamic elements of insurance. Government is arranging reinsurance through the Sadharan Bima Corporation in the existing set-up. For extending this service to the Islamic insurance companies government may establish a Fund, and all Islamic insurance companies should contribute a proportion of their written premium to this Fund. This proportion may be different for different policies. The objective of this fund should be to help the insurance companies in paying claims. A proportion of this fund may be invested in profitable ventures according to Islamic principles, and profit can be shared between the fund and the insurance companies.

By now Takaful, like Islamic Banking, has become a viable reality. Due to inherent Shariah principles which are universal in character, the Takaful business will be more appealing in the coming years for both the Muslim and non-Muslim communities.

There is no denying the fact that Takaful (Islamic Insurance) has bright prospects and potential as a financially viable and competitive alternative insurance for Muslim countries. Most Muslim countries having Islamic Banks have also helped to create takaful as a necessary complement to Islamic Banking because Islamic banking can not be fully Shariah based unless there are Takafuls to take their insurance business. Takaful, like Islamic Banking has proved its viable reality and has made strides of expansion in almost all the Muslim countries. The Governments of these countries ought to have strategic policies to promote and foster the growth of Takaful.

What are the Hindrances of Islamic Banking & Islamic Insurance ?

Banking and Insurance are the two fundamentals of modern trade and commerce. Banking provides security to the depositors and plays a vital role in development by financing the surplus fund to the deficit groups. On the other hand, Insurance provides security for the people as financial protection against accident, calamities and pathetic situations. Modern trade and commerce cannot be conceived without involvement of Banking and Insurance. But, the conventional systems of Banking and Insurance, which are based and linked up with interest, cannot be adopted by the Muslims as a Shariah-compatible systems. But, trading and equity financing as well as the principle of compensation and group responsibility are widely accepted in Islam.

Further, there is an intrinsic and inherent relationship between Islamic Banking and Islamic Insurance. It is a precondition for the success of Islamic Banking to cover its risk by a system accepted in Islam. This is possible by adopting the system of Islamic Insurance. On the other side, the progress of Islamic Insurance depends on a healthy growth of Islamic Banking.

Due to inherent Shariah principles which are universal in character, the Islamic Banking and Takaful business will be more appealing in the coming years for both the Muslim and non-Muslim communities. There is tremendous possibility for the growth of Islamic Banking and Islamic Insurance. But, there are still lots of problems and hindrances in operating Islamic Banking and Islamic Insurance, some of which are as under:

1. Absence of appropriate legal framework for carrying out Islamic Banking and Insurance operations in most of the Islamic countries.
2. Shortage of trained manpower to conduct business complying with Shariah.
3. Absence of Shariah based securities.
4. Shortage of support institutions.
5. Absence of good relationships between the Management, entrepreneur and the Controlling & Legislative Authority.
6. Lack of public awareness.
7. Ignorance of the mass of people about Shariah principles and practices in business and commerce.
8. Predominance of a secular Western capitalistic economic system.
9. Lack of support from Government mechanism

How Islamic Banks and Insurance Companies Can Cooperate for Mutual Growth and Expansion

Islamic Banks have already attained considerable success in the Banking sector. It is just the beginning of Takaful business and it is likely to flourish in the Insurance sector in coming days. To attain the desired level by both Islamic Bank and Islamic Insurance, a strong relationship needs to be built up between Islamic Banks and Islamic Insurance throughout the world.

The following actions may be taken jointly by the Islamic Banks and Islamic Insurance Companies for their mutual growth and expansion and to face the challenges:

1. Efforts should be made to change the legal framework for conducting banking

and insurance operations according to Islamic Shariah.
2. Sufficient training and research institutes having logistics of modern technology may be established to train up the manpower.
3. To create public awareness; seminar, symposium etc. at both national and international level may be organised.
4. Islamic Money & Capital Markets should be developed.
5. Central Shariah Council should be set up both for Islamic Banks and Islamic Insurances.
6. As in Malaysia, both the Islamic Banks and Islamic Insurance Companies should be regulated by the same Regulatory Authority, the Central Bank.
7. Cordial and harmonious relationship between Islamic Banks and Islamic Insurance Companies should be developed.
8. Efforts should be made to establish more Islamic Insurance Companies and Islamic Banks.

Islamic Banking and Islamic Insurance systems have tremendous potential and prospect. The successful launching and operation of Islamic banks and insurance has established the fact that banking and insurance without interest is feasible, viable, competitive and sustainable in the face of competition from the conventional secular system. The gradual and successful globalisation of Islamic Banking and Islamic Insurance coupled with growing awareness of the people about its financial and social benefits makes it clear that the current century is going to be the century of Islamic banking and insurance vis-a-vis implementation of Islamic ideals for the betterment of the people at large and establishing equity nd justice for all.

How Islamic Insurance can Supplement the Transactions of Islamic Banks

Commendable performance of Islamic Banks has established the fact that interest-free financial institutions are very much feasible and necessary. Therefore, interest-free Islamic Insurance Companies are urgently required to supplement and support the activities of the Islamic Banking system.

With the formation of an Islamic Insurance Company, millions of people who are now not participating in insurance under the conventional system can be brought into the fold of an Islamic Insurance system. Thousands of small, medium and arge traders, entrepreneurs and industrialists will come forward to insure their properties through an Islamic Insurance Company. This will lead to a further expansion of the insurance market; a new expansion of the insurance market in a new dimension which thus will help towards further growth of the capital market of the country.

Although an Islamic Insurance Company would be registered under the Companies Act, the principle of mutuality will be the fundamental operating principle of the company. Therefore, it is likely that the insurance covers will be provided at actual cost. Since risks will be covered more economically, the people will be getting the services at a lower cost. Further, an Islamic character will establish 'Jakat Fund' and will initiate welfare oriented rehabilitation programmes for the poor. This will help to alleviate poverty in Islamic countries.

One of the prime objectives of an Islamic Bank is to offer contemporary financial services in conformity with Shariah and for that matter to undertake financial activities which are ethical, socially desirable and profitable, so that the bank can contribute towards economic development and prosperity of the mass. By establishing a subsidiary Islamic Insurance Company, Islamic Banks will be achieving their ultimate goal i.e. the establishment of economic and social justice by way of even distribution of wealth in the society, instead of accumulation of wealth in few hands.

For obvious reasons, Islamic Banks have been following a line of least risk and assured success. Naturally, the banks insist on collaterals against credit. However, due to non-availability of 'Islamic Insurance', they have to use the services of conventional insurance companies to cover risks to their assets, including investments and collaterals. With the establishment of an Islamic Insurance Company, the Islamic Banks will be able to avoid interest-based insurance, which is forbidden in Islam.

How the Superiority of Takaful Can Be Enhanced

Although a rosy picture of an Islamic Takaful Company has been drawn on the basis of better underwriting results, it must be remembered that the financial success of the company depends on the following factors:

a) Soundness of the management of the company.
b) Adequacy of reserves for all undischarged liabilities.
c) Soundness of investment of the company fund.

This means that an Islamic Takaful company ought to be managed by qualified and professional people. In fact, so far as business efficiency is concerned, there is no substitute for professionalism. In the case of Takaful companies, the executives and managers must be motivated by the idealism and philosophy of an Islamic system of insurance. Professional ability when backed by idealism, is sure to produce the very best results. In reality the human resources of the Takaful company will play the key role for its success and superiority over the conventional system.

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