

Bangladesh: The need for takaful regulations



The Takaful Act is necessary for the continued development of takaful and ensure a level playing field for the insurance industry in Bangladesh, says **Mr Kazi Mohd Mortuza Ali**, Managing Director of Prime Islami Life Insurance.

Takaful has evolved into a viable alternative to conventional insurance and is able to attract a wide range of customers, both Muslim and non-Muslim. For example, in Sri Lanka, some 15% of takaful policyholders are non-Muslims. Prime Islami Life Insurance of Bangladesh has approximately 9% non-Muslims as its policyholders.

In Bangladesh, there are now three life and three non-life takaful companies which were licensed in 2000 under the Insurance Act 1938. Though the Insurance Act is not equipped to deal with takaful or Islamic insurance, the success of these companies on the back of demand for Shariah-compliant products have led to as many as 13 conventional life and non-life insurance companies offering takaful products through windows or projects.

Insurance and legal experts in Bangladesh feel that the age-old Insurance Act is not at all suitable for takaful operations because insurance has a new meaning and philosophy under the takaful system.

Fate of the Takaful Act

A committee formed by the Government of Bangladesh submitted drafts of two separate insurance laws in 2007, one meant for conventional insurance and the other for Islamic insurance. The committee also lodged a draft of the Insurance Regulatory Authority Act, which envisaged an independent regulatory body for insurance industry to supervise both conventional and takaful companies.

The Advisory Council of the past caretaker Government later gave the green light for the Insurance Act and the Regulatory Authority Act. However, the Council did not give appropriate attention to the much-desired Takaful Act, which is necessary to ensure a level playing field for all the players in the insurance industry.

Later, the caretaker Government promulgated two ordinances, The Insurance Ordinance 2008 and The Insurance

Regulatory Authority Ordinance 2008. These two Insurance Ordinances have now lapsed as the present government did not table these in parliament within the constitutional mandated period. The main features of the new laws include an increase in paid-up capital, provision for mandatory solvency margins for the insurers and selling general insurance business only through registered broker houses. It also does not allow takaful companies to sell non-takaful products and vice versa.

Demand for takaful

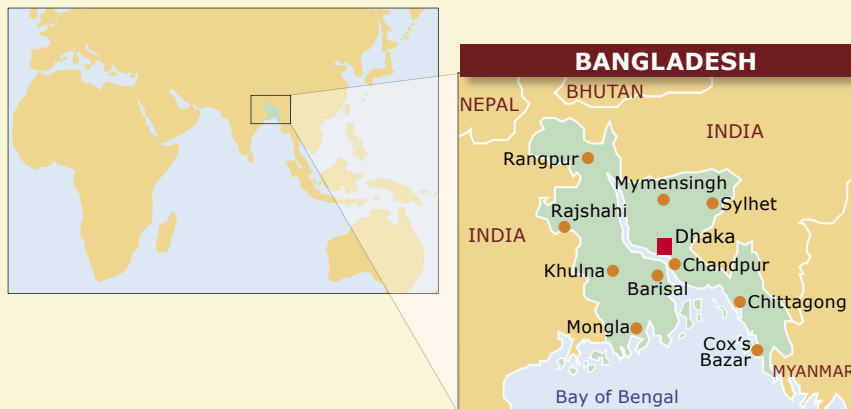
There is no doubt that the people of Bangladesh are eager to buy takaful products and suppliers are also keen to be regulated by Shariah-based rules. In fact, more than 70 entrepreneurs have already applied for licences to operate takaful companies in Bangladesh. This shows great potential for takaful to surpass the conventional insurance companies in the coming decade, and logically, the government should take a serious view towards supporting the orderly development of the takaful industry in terms of acceptable business models. A sound regulatory and supervisory system is necessary for maintaining an efficient, safe and stable takaful market.

Takaful has already gained wide support from consumers, entrepreneurs, professionals and the ulemas (Muslim scholars) in Bangladesh and throughout the world.

The Regulatory Authority also earnestly feels that the Government should promulgate the Takaful Act with the new Insurance Act and the proposed Regulatory Authority Act. The proposed Takaful Act will provide benchmarks for the regulatory body to address issues such as risk management and financial stability for the nascent takaful industry of Bangladesh. This will certainly enhance consumer protection in terms of both risk and disclosure.

Supervision of takaful companies

Takaful is basically a contract of co-operation between the individual and the pool of insureds. The takaful operator manages underwriting and gets remuneration for that, either as mudarib or as wakeel. The takaful operator acts as administrator of the scheme and pays the benefits from the takaful fund. In the event of a shortage in the takaful fund, the operator should provide an interest free loan to the takaful fund to cover the deficiency. The shareholders' fund also has to be kept separate from policyholders' fund and surplus from investment of sharehold-



ers fund belongs to shareholders only. These differences between takaful and conventional insurance clearly have regulatory implications.

Bangladesh's Department of Insurance, the regulatory body, requires insurers to disclose relevant information on a timely basis in order to give stakeholders a clear view of their business activities and financial position and to facilitate the understanding of the risks in which they are exposed. The precise details of the financial disclosures for a takaful operation need to reflect the features of its structure and business. There are several issues such as corporate governance, transparency, as well as market conduct, which are critical to the regulatory and supervisory framework of the takaful industry and need to be addressed in an integrated way.

For example, if a regulator is to adopt capital adequacy principles for takaful, it ought to have a clear view of the financial risks and where those are located. This, in turn, is strongly influenced by the model chosen and the relationship between the shareholders and policyholders' funds.

Similarly, some of the disclosures to participants will depend heavily on the details of the model chosen. If and when basic principles, mechanisms and features of different models of takaful are established in the Takaful Act, it will be much easier for the regulatory body to make progress in other areas such as in developing prudential rules and regulations for takaful operators.

Takaful is based on the principle of co-operation and mutual help for the good of the society at large. Currently there are several takaful models based on the contractual forms of *mudahraba*, *wakala* and *waqf*, or combinations of these. The existing models demonstrate the flexible and practical nature of takaful principles. It also raises the

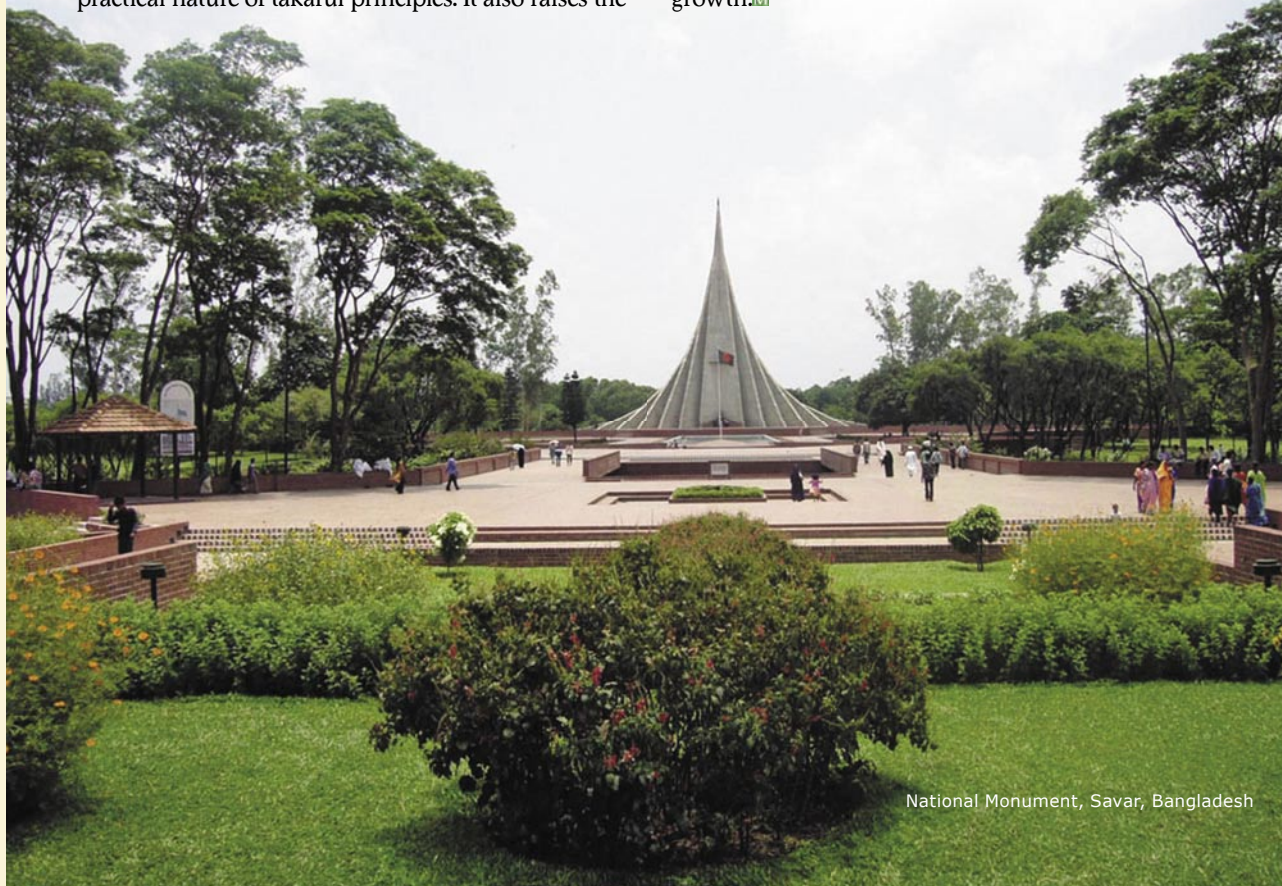
question of contractual relationship between policyholders and insurers and their respective rights and obligations.

The regulatory body needs to ascertain the type of risk peculiar and common to each model. Based on this, rules have to be developed to protect the rights of policyholders. Without having a suitable regulatory and supervisory framework for the takaful industry and adapting the relevant legal, governance, information and liquidity infrastructure, the regulatory body is likely to find it very difficult to facilitate the growth of Islamic insurance in Bangladesh.

Concluding remarks

In the absence of a Takaful Act with clear regulatory frameworks, prudential standards and codes of good practice, the potential of the takaful industry for growth and development may be stunted by related obstacles such as a lack of legal and regulatory certainty. Such problems need to be given immediate attention in order to facilitate the development of the nascent takaful industry. Failure to remove them immediately would have a negative impact on the pace of development of the entire insurance industry. The legal framework is a must to protect the policyholder's interests and also a key element to promote the takaful industry.

The people of Bangladesh have strong faith in their religion and this has been protected in the provisions of the country's constitution. The very first principle of our State Policy clearly and strongly emphasises that absolute trust and faith in the Almighty Allah shall be the basis of all actions of the Government. While people have supported the Islamic alternative of conventional insurance, it is not understood why some vested quarters should stand in its way to halt or hinder its smooth and sound growth. ■



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