

SHARIAH COMPLIANCE ON RETAKAFUL IN MALAYSIA

¹Nurwajihah Ajlaa Ali, ^{2*}Ruzian Markom

¹Faculty of Law, Universiti Kebangsaan Malaysia, nurwajihahajlaaali@gmail.com

²Faculty of Law, Universiti Kebangsaan Malaysia, ruzian@ukm.edu.my

Abstract

Retakaful is an Islamic alternative to the reinsurance industry in ensuring the stability of takaful companies. In Malaysia, the takaful operators need to depend on retakaful operators to ensure the takaful industry's long-term continuity by sharing the risk with the retakaful operators due to the small numbers of takaful operators. As a result, they reinsure their Takaful with the conventional reinsurance companies to meet the market demand. This practice continues to be acceptable based on an argument of unavoidable circumstances such as a necessity (darurah) and a dire need (hajah) due to insufficient retakaful companies. The Shari'ah issues arose on the needs for retakaful operators with conventional reinsurers or operators. Therefore, the paper aims to analyze the role of retakaful and its potential within the industry by identifying. Then it explores the Shari'ah principle and the arguments, existing rules, and regulations on the said issues. This study utilized the doctrinal research method with the content analysis. The data is collected from the library consisting of primary and secondary sources. The study's findings revealed that the Shariah scholars resolution plays essential roles in enhancing the roles of the retakaful industry based on darurah and hajah.

Keywords: Takaful; Retakaful; Reinsurance; Shari'ah; Regulatory; Risk-Sharing

1. Introduction

Takaful industry is an important component of Islamic finance in developing and sustaining other financial sectors like banking and the capital market in Malaysia. The development of Takaful began with effective regulation and supervision.¹ In 1984, the Takaful Act was enacted for the regulation of takaful business. Then, the Act was repealed, and the Islamic Financial Services Act 2013 was introduced in 2013.² The new Act enhanced the regulation and supervision of Takaful business in promoting financial stability and Shariah compliance. Shariah Advisory Council of the Central Bank of Malaysia remains the sole authority in Shariah's decision relating to Takaful and other financial sectors.³ In the early stage

¹ Wan Norhayate Wan Daud et al., "Takaful Rules and Regulations for ASEAN Countries: Takaful Player Perspectives," in *Proceedings of the 30th International Business Information Management Association Conference, IBIMA*, 2017.

² S. N. Jamil and J. Jamal, "Importance of Islamic Financial Services Act 2013 in Takaful Industry After the Repealed Takaful Act 1984," *Diponegoro Law Review* 1, no. 1 (2016): 17–27.

³ Bagas Heradhyaksa and Ruzian Markom, "Jurisdiction of Sharia Supervisory Board in Indonesian Takaful Industry," in *IOP Conf. Ser.: Earth Environ. Sci.* 175 012177, 2018, 1–7.

of the Takaful operation, the focus was on strengthening the principles of Takaful, such as permissible takaful interest⁴, nominations⁵ and status of Takaful Agents.⁶

1.1. Why Retakaful?

Retakaful is a modern contract. It is a risk mitigation tool for takaful operators. It played an important role in addressing the risks of loss faced by the takaful industry. Thus, the takaful services and facilities of retakaful are very important as a vehicle for generating growth and development of takaful operations.⁷ The contract of retakaful is the insurance equivalence of reinsurance. An arrangement under which a Takaful company (i.e. the insurer) agrees to assume all or portion of the specified risks of another takaful company (i.e. the ceding company).⁸ In modern times, the takaful sums insured have become so large, particularly in the non-life takaful business, that even the largest takaful operator may not be able to meet from its resources all possible losses singly. An operator has to spread its portfolio of liabilities among other operators, which ultimately protects it against the risk of huge losses. In retakaful, the party that cedes or transfers the risks (the cedant) is a takaful operator. The party that underwrites and offers capacity for the ceded risks is called the retakaful operator. A retakaful contract governs the relationship between the two parties; thus, the retakaful operators have direct and close relations with the takaful operators.

1.2. Shariah Issues on Retakaful

In the early years of the takaful business, takaful operators' reinsurance capacity was mostly encountered with reinsurance companies whose operations did not comply with Shari'ah. Retakaful, in principle, protects a primary takaful against unforeseen or extraordinary losses. Due to the small size of the takaful business, some takaful operators needed to cede out large claims risk to conventional reinsurance whenever possible.⁹ They can protect against major

⁴ Cheah You Sum, Hasani Mohd Ali, and Ruzian Markom, "Legal Issues Concerning Insurable Interest and Permissible Takaful Interest at the Time of Death under Conventional and Family Takaful Contract," *International Journal of Business and Society* 19, no. 3 (2018): 353–67.

⁵ YS Abubakar, MA Zahid, and R Markom, "Effect of Nomination Under Life Insurance and Family Takaful," *ISRA International Journal of Islamic Finance* 195, no. 2632 (2014): 1–23.

⁶ M. A. Z. Ahmad Samsuri and J. Jamal, "Takaful Agent Must Foster Public Understanding of Takaful," *Diponegoro Law Review* 2, no. 2 (2017): 245–58.

⁷ Setiyawan Gunardi et al., "Retakaful From Syariah Perspective: A Comparative Study," *Chinese Business Review* 12, no. 9 (2013): 616–24.

⁸ INCIEF, *Takaful Realities & Challenges* (Petaling Jaya: Pearson Malaysia, 2012).

⁹ Asmak Ab Rahman, Wan Marhaini Wan Ahmad, and Ahmad Hidayat Buang, "Can a Takaful Company Reinsure with a Reinsurance Company?," *African Journal of Business Management* 5, no. 30 (2011): 11768–78.

claims incidents that could drain the fund and the experience of unpredictable claims that would impact the fund's stability. The practice continues to be acceptable by the takaful operators based on the argument of unavoidable circumstances, namely necessity (*darurah*) and dire need (*hajah*) due to lack of retakaful capacity and to protect the interest of policyholders.¹⁰ As a result, this has created a huge demand for retakaful capabilities that can be supported and provide Shari'ah-compliant capacity by Shari'ah-compliant capitals. Therefore, Shari'ah issues concerning retakaful on the financial capabilities of the retakaful to manage the risks of takaful operators. The retakaful operator's needs to collaborate with conventional reinsurers or obtain coverage from the conventional re-operators. The commission received in retakaful, perceived as conflicting with the Shari'ah, needs to be addressed to enhance the role and position of retakaful within the takaful industry. This paper aims to analyze the role of retakaful and its potential within the industry by identifying the nature and concept, objectives, and operational mechanism. Then it explores the Shari'ah principle and the arguments, existing rules, and regulations on the said issues.

2. Methods

This study utilized the doctrinal research method with the content analysis. Both were applied in understanding concept, structures, issues and Shari'ah law. The main approaches used include historical, philosophical approach; comparative, and analytical and critical approach. The method is based on the paper's objectives: to analyze the role of retakaful and its potential within the industry by examining the Shariah compliance. Data collection from the library consisting primary and secondary sources such as statutes, books, articles, and internet sources.

3. Results and Discussion

3.1. The Definition and Nature of Retakaful

The word retakaful is the combination of two different words: 're' and 'takaful'. The word 're' is originally loan words from Latin which means 'again' or 'again and again' to indicate repetition, or with the meaning 'back' or 'backwards' to indicate withdrawal or backward motion. In contrast, the word takaful is derived from the Arabic word 'kafala' which means, guarantee,

¹⁰ Bank Negara Malaysia, *Kompilasi Keputusan Syariah Dalam Kewangan Islam*, 3rd ed., 2007.

warrant, liability, and protection.¹¹ Theoretically, retakaful or Islamic reinsurance is a form of risk mitigation. The Takaful ceding business uses a conventional reinsurer or retakaful operator to reinsure original insured risks against a potentially adverse situation if the insured risks were beyond the usual underwriting or claim.¹² Through this mechanism, takaful operators can transfer (share) all or part of their liabilities to retakaful operators to reduce the risk coverage in the event of a claim arising under the takaful contracts they enter. Hence, through risk-sharing, the retakaful scheme broadens the distribution of risks among participants, protects takaful operators against potential financial losses, and protects participants' interests.¹³

Retakaful does not differ from takaful operations since the Shari'ah principles applying to Takaful also apply to retakaful operations.¹⁴ The main difference is that the participants in retakaful operations are the takaful operators, whereas, in Takaful, the participants are individual persons, namely policyholders or organizations being covered.¹⁵ The Resolution of Organization of Islamic Cooperation (OIC) Fiqh Academy stated that the Shari'ah principles of takaful structure and operation apply equally to retakaful structure and operation. The Shari'ah forbids certain conventional insurance contract components such as *riba'* (interest), *maysir* (gambling) and *gharar* (uncertainty); thus, retakaful activities aim to avoid these forbidden components to comply with Shari'ah's principles.¹⁶

3.2. Objectives and Significance of Retakaful

The main objectives of retakaful are¹⁷: a) to protect the takaful operator from the risk of insolvency, underwrite the interests of the participants, establish cooperation between the participants and invest the accumulated fund in an Islamic way; b) to adapt the practice of underwriting to takaful operators; and c) to allow the takaful operator to make use, without

¹¹ Abu Umar Faruq Ahmad, Ismail Bin Mahbob, and Muhammad Ayub, "The Nature of Retakaful: Risk-Sharing or Transferring Risks?," in *Takaful and Islamic Cooperative Finance*, ed. S. Nazim Ali and Shariq Nisar (Cheltenham: Edward Elgar Publishing, 2016), 171–91.

¹² Mohammed Burhan Arbouna, "The Operation of Retakaful (Islamic Reinsurance) Protection," *Arab Law Quarterly* 15, no. 4 (2000): 335–62.

¹³ Aznan Hasan, "Shari'ah Issues in The Operation of Retakaful and Reinsurance: A Preliminary Exploration from Shari'ah Perspective," *IJUM Law Journal* 19, no. 2 (2011): 150–78.

¹⁴ Arbouna, "The Operation of Retakaful (Islamic Reinsurance) Protection."

¹⁵ Mohamed Yusuf and Rosmi Yuhani, "Revisiting and Redefining the Concept of Retakaful and the Viability of Its Model in Malaysian Takaful Industry," *Business and Management Quarterly Review (BMQR)* 2, no. 4 (2011): 20–32.

¹⁶ Bank Negara Malaysia, *Resolusi Syariah Dalam Kewangan Islam*, 2010.

¹⁷ Arbouna, "The Operation of Retakaful (Islamic Reinsurance) Protection."

paying interest, of the deposit reserves kept by the retakaful fund in the interest of its client as a means of making the reinsurance industry an interest-free company.

The significance of retakaful is also to provide additional underwriting capacity, address tragic/catastrophic losses, expand into new markets/product lines, provide value-added services and expertise, and a cost-effective capital replacement. As a result, these significances of retakaful show that it is an effective tool to support the growth of takaful operators and retakaful operators and, at the same time, to reduce claims and losses that would ensure good progress of their respective pools.

3.3. Operational Mechanism of Retakaful

In practice, there are two forms of retakaful¹⁸:

- a) Treaty: A form of agreement in which the retakaful operator agrees to cover all risks as set out in the scope of agreement/treaty with the takaful operator.
- b) Facultative: A treaty that allows a takaful operator to select any case or policy to be retakaful or otherwise.¹⁹

Therefore, retakaful operated in the following ways:

- a) the individual policyholders (participants) of the takaful products do not involve directly in the retakaful contracts even though the contributions in retakaful are paid using a portion of the takaful participants' fund),
- b) in the event of running a deficit to the retakaful funds due to unforeseen claims by its participants, the retakaful operators provide a qard (a loan injection into retakaful funds) to cover liability. The amount of the loan shall be paid in subsequent years or deducted from any refundable surplus in the following years²⁰, and;
- c) retakaful can be operationalized based on similar structures implemented in Takaful either on Al-mudharabah, Al-wakalah or hybrid models incorporating al-mudharabah and al-wakalah.²¹

¹⁸ Amirul Afif Muhamat, Mohamad Nizam Jaafar, and Mohd Shamsuri MD Saad, *Essential Components of Takaful Operation* (UTEM Press, 2019).

¹⁹ Bank Negara Malaysia, *Resolution No 47, Shariah Resolution in Islamic Finance*, 2nd ed., 2010.

²⁰ Ahmad, Mahbob, and Ayub, "The Nature of Retakaful: Risk-Sharing or Transferring Risks?"

²¹ Sheila Nu NuHtay et al., "Retakaful (Islamic Reinsurance): Historical, Shari'ah and Operational Perspectives," *World Applied Sciences Journal 30 (Innovation Challenges in Multidisciplinary Research & Practice)*, 2014, 185–90.

Table 1.
List of Reinsurance and Re Takaful Companies

List of Retakaful		List of Reinsurance	
1	Swiss Reinsurance Company Ltd. (Swiss Re Retakaful),	1	Ambra Versicherung AG
2	Munchener Ruckversicherungs-Gesellschaft (Munich Re Retakaful)	2	Asia Capital Reinsurance Malaysia Sdn Bhd
3	Malaysian Reinsurance Berhad	3	Malaysian Reinsurance Berhad
		4	Munchener Ruckversicherungs-Gesellschaft
		5	Swiss Reinsurance Company Ltd
		6	Toa Reinsurance Company Ltd.

Source: Bank Negara Malaysia 2021. <https://www.bnm.gov.my/retakaful-operators>

Table 2.
List of Takaful Companies in Malaysia

Family Takaful		General Takaful	
1	AIA PUBLIC Takaful Bhd	1	Etiqa General Takaful Berhad
2	AmMetLife Takaful Berhad	2	FWD Takaful Berhad
3	Etiqa Family Takaful Berhad	3	Great Eastern Takaful Berhad
4	Hong Leong MSIG Takaful Berhad	4	Syarikat Takaful Malaysia Am Berhad
5	Prudential BSN Takaful Berhad	5	Takaful Ikhlas General Berhad
6	Sun Life Malaysia Takaful Berhad	6	Zurich General Takaful Malaysia Berhad
7	Syarikat Takaful Malaysia Keluarga Berhad		
8	Takaful Ikhlas Family Berhad		
9	Zurich Takaful Malaysia Berhad		

Source: Bank Negara Malaysia 2021. <https://www.bnm.gov.my/retakaful-operators>

Table 1 and 2 shows that the number of retakaful companies in Malaysia is still small compared to the number of takaful companies operating in Malaysia. As of January 2020 Bank Negara Malaysia has reported that there are three (3) retakaful operator companies operating in Malaysia which are a) Swiss Reinsurance Company Ltd. (Swiss Re Retakaful), b) Munchener Ruckversicherungs-Gesellschaft (Munich Re Retakaful) and c) Malaysian Reinsurance Berhad. Out of these three (3) retakaful companies operating, only one is locally owned while foreign entities own the other two (2) companies. Also, for conventional reinsurance, there were six (6) companies operating in Malaysia which are a) Ambra Versicherung AG, b) Asia Capital Reinsurance Malaysia Sdn Bhd, c) Malaysian Reinsurance Berhad d) Munchener

Ruckversicherungs-Gesellschaft, e) Swiss Reinsurance Company Ltd and f) Toa Reinsurance Company Ltd., whereas there were fifteen (15) takaful companies altogether in Malaysia.

3.4. The Shariah and Legal Framework of Retakaful

The practice of retakaful has been endorsed in a few regulatory frameworks, policies, and resolutions by the relevant authority.

3.5. Shariah Advisory Council of Central Bank of Malaysia

The SAC, in its 47th meeting dated 14 February 2005, has resolved that a takaful company is not allowed to accept inward retakaful, whether on a treaty or facultative basis from a conventional insurance company and reinsurance company. Besides, a takaful company is given the flexibility to distribute its risks based on outward retakaful to the conventional insurance company and reinsurance company subject to conditions.

3.6. Resolution of Organization of Islamic Cooperation (OIC) Fiqh Academy

The concept of Takaful and retakaful has been endorsed by the Shari'ah Resolution of Organization of Islamic Cooperation (OIC) Fiqh Academy (Resolution No. 9) as follows:

"The Commercial Insurance Contract, with fixed periodical premium, which commercial insurance companies commonly use, is a contract which contains major elements of risks which voids the contract and therefore, is prohibited (haram) according to Shari'ah. The alternative contract, which conforms to Islamic dealings' principles, is co-operative insurance, which is founded based on charity and cooperation. Similarly, in the case of reinsurance based on the principles of co-operative insurance".

This resolution explains that retakaful is like Takaful and is based on the co-operative and risk-sharing concepts set out in the Shari'ah's objectives (maqasid) and has been decided as having complied with Shariah requirements, based on the application of the same takaful principles.²²

3.7. AAOIFI (Accounting & Auditing Organization for Islamic Institution)

The Accounting and Auditing Organisation for Islamic Financial Institution (AAIOFI) issued a decision in 2012 regarding on issue of retakaful. The AAOFI in its Shari'ah Standard

²² Mohd Sabree Nasri, "Takaful Semula Dalam Industri Insurans: Tinjauan Khusus Menurut Perspektif Islam Dan Undang-Undang," *Journal of Law & Governance* 1, no. 1 (2018): 49–61.

No. (41): Islamic Reinsurance (Revised Edition) 2015 refers to 'Islamic Reinsurance' (retakaful) as:

Retakaful (Islamic Reinsurance) refers to the agreement among insurance companies, on behalf of the insurance funds under their management, to devise a mechanism for avoiding part of the risks that the insurance funds may encounter. Based on such agreement, a reinsurance fund with a distinct legal personality and independent financial liability are formed by making contributions to the insurance clients' insurance funds because of donation. The reinsurance fund, thus formed, assumes the task of covering part of the risks encountered by the insurance funds. Reinsurance, as described above, constitutes the Islamic alternative for the reinsurance provided by traditional reinsurance companies, which is based on an exchange of the reinsurance premiums and compensation rather than on donation commitments.

Many conventional terminologies were adopted under this definition, such as 'insurance companies', 'funds' and 'reinsurance funds'. It is believed that the usage of these terminologies shows no difference between Takaful and insurance and retakaful and reinsurance.²³

3.8. Islamic Financial Services Act 2013 and Takaful Act 1984 (Repeal)

In 2013, the Malaysian Government introduced the Islamic Financial Services Act (Act 759) (IFSA 2013), which replaced the Takaful Act 1984. This Act provides more transparency in the financial industry, including Takaful. In general, there is no specific section in IFSA 2013 that relates to retakaful. Previously, the Takaful Act 1984 has specifically provided for retakaful under Section 23. The only section that emphasized the concept of retakaful is in the Financial Services Act 2013 under Section 2 (Interpretation), where retakaful refers to:

...takaful cover arranged by a takaful operator with a second takaful operator on the risks of the takaful fund it administers, wholly or partly, and includes any similar arrangement by a branch of takaful operator in Malaysia with its branch outside Malaysia (the head office of the takaful operator being, for this purpose, treated as a branch).

This provision recognizes the close relationship between the takaful operator and the retakaful operator. For this reason, Takaful has similar characteristics to retakaful in its contractual dimensions, except for some aspects that are specific to the operating context of retakaful.²⁴

²³ Ibid.

²⁴ NuHtay et al., "Retakaful (Islamic Reinsurance): Historical, Shari'ah and Operational Perspectives."

3.9. Takaful Operational Framework (TOF 2019)

Bank Negara Malaysia had also specifically issued guidelines for retakaful through Takaful Operational Framework (TOF) in 2013 and revised TOF 2019. TOF 2019 requires the takaful operator to have arrangements compatible with the sound retakaful principles for the recovery of liabilities regarding risks incurred or undertaken by the operator during its takaful business. In summary, retakaful operators must follow all these regulatory and supervisory mechanisms in regulating the operation of retakaful, thus appreciating the significance of regulation and supervision relating to takaful business management.

3.10. The Role of Retakaful Industries in complementing the Ecosystem of Islamic Finance

Retakaful plays essential roles in complementing the ecosystem of Islamic finance. The industry faces many challenges in the course of implementation. At the early stage, reinsurance capacities for takaful operators were primarily fulfilled by conventional reinsurance companies whose activities are not Shari'ah compliant. This practice is acceptable by some takaful operators based on arguments of unavoidable circumstances, i.e., necessity (*darurah*) or dire need (*hajjah*) due to the lack of retakaful companies in the market. Jurists agreed on the need to allow Takaful to reinsure with conventional reinsurance companies. Certain conditions have been established to limit this permission. Lack of reinsurance ability and the need to protect the funds of policyholders and shareholders have determined the use of reinsurance because of the small numbers of takaful operators and the limited size of their funds.²⁵ Therefore, takaful operators had reinsured with conventional insurance and established reinsurance companies. Shari'ah Advisory Council (SAC), Bank Negara Malaysia has approved this practice because currently existing and operating retakaful operator companies are very limited and the need to protect the interests of participants of takaful plans.²⁶

For example, PRUBSN Takaful, in its general Takaful, needed to cede out large claims risk to retakaful whenever possible. The 2014 flood events that the PRUBSN Takaful's certificates covered the event's large claims risks. In certain cases, there was a proposal to cede its portfolio to a reinsurance company. The plan to cede to the reinsurance company was due to limited retakaful operators, and the business portfolio is too small to attract any retakaful operators to participate. Attempts were made to source a retakaful solution, but the company could only

²⁵ Arbouna, "The Operation of Retakaful (Islamic Reinsurance) Protection."

²⁶ Bank Negara Malaysia, *Shariah Resolutions in Islamic Finance*, 2nd ed., 2010.

obtain a 90% retakaful arrangement. Because of this reason, the company needs to still resort to reinsurance on the 10% portion of the portfolio. The Shari'ah Council, at its meeting on 22 January 2015, agreed that PRUBSN would approve the company's reinsurance quote to take up the remaining 10% of the general takaful fund to ensure that PRUBSN continues to cover the fund and its participants from the risk of claims and uncertainty.²⁷

3.11. Differences of Opinion Among Jurist Regarding the Rules for Takaful Operators To use Reinsurance Services from Conventional Reinsurance Companies

There are differences of opinion among jurists regarding the rules for takaful operators to use reinsurance services from conventional reinsurance companies. Some of the view reinsurance from conventional reinsurance companies is allowed, while others not.²⁸ It is believed that these practices can establish a strong opposition to the objectives of takaful activities. Collaboration between Islamic and non-Islamic insurance companies may be regarded as a mixture of truth and lies as emphasized in the Holy Quran, which has no place in Islam's basic teachings. The obligation for takaful companies to use conventional reinsurance services to protect the risks borne by them is based on the principle of emergency.²⁹ In an emergency, such protection is required due to the takaful operator's financial capacity constraints in bearing the risk. Suppose the risk is not insured with a conventional reinsurance company. In that case, the takaful operator will likely not pay the takaful participant if the takaful participant makes a takaful claim. The reinsurance transactions between takaful operators and conventional reinsurers must be regulated by the rule of necessity described in Islamic law.

However, takaful companies can distribute risk based on dire need (hajah) requirements by outflow takaful to insurance companies and established reinsurance companies if no takaful company or retakaful company is believed to be capable of absorbing a takaful risk. As stated earlier, in PRUBSN Takaful, justification was given in allowing PRUBSN to accept reinsurance of the remaining 10% of the general fund since there is an element of mashaqqah (hardship). It is darurah (necessity) to cede the said portfolio to the reinsurer based on three (3) Islamic legal maxims, namely; specific harm is tolerated to prevent a more general one, 'harm is to be eliminated to the extent possible, and 'a greater harm is eliminated utilizing a lesser harm'. These

²⁷ ISRA, *Selected Resolutions of the Shariah Committee of Prudential BSN Takaful Berhad* (Petaling Jaya: ISRA, 2020).

²⁸ Hasan, "Shari'ah Issues in The Operation of Retakaful and Reinsurance: A Preliminary Exploration from Shari'ah Perspective."

²⁹ Arbouna, "The Operation of Retakaful (Islamic Reinsurance) Protection."

legal maxims indicate that a takaful company is given the flexibility to distribute its risks based on outward retakaful to a conventional insurance company but subject to priority should be given to takaful and retakaful company, no takaful company or retakaful company exists, either locally or internationally and the strength of the takaful and retakaful company is doubtful.³⁰ Therefore, a takaful company should not first cede to reinsurance, but before ceding to another reinsurance company, should try to locate another takaful or retakaful company. As such, an application to resort to a reinsurance undertaking can only be made after the company has exhausted all efforts to offer the undertaking to retakaful companies on the market.

On the other hand, Dr Aznan Hasan deliberated in his article that some scholars view takaful companies' reinsurance as not accepted because there is an element of *riba'* *gharar* and *maysir*, the same as conventional insurance.³¹ There was no need to use conventional reinsurance services due to Shari'ah-compliant retakaful operator companies' existence. Apart from that, some scholars such as Sheikh Muhammad Abd Latif al-Farfur gave general arguments on the forbidden of conventional reinsurance because it is the same as a conventional insurance contract.³² Simultaneously, Dr Yusuf Qasim believed that reinsurance activities could cause the taking of other people's property illegally. 'Abd Aziz al-Khiyat said that takaful companies could not reinsure with conventional reinsurance unless it is in the condition that is demanded by the law and when there are no Islamic reinsurance companies available. The reason for rejecting reinsurance is that if a transaction contains the element of *syubhah*, where it is likely to have an element of usury, it should be avoided. Besides, the method of *fiqh* "emergency allows a forbidden" cannot be used to support the necessity of using conventional reinsurance services.³³ The Muslim community that has never relied on conventional insurance and reinsurance systems has not suffered any harm or emergency before.³⁴ The hadith narrated by al-Tirmidhi and al-Nasai state that the Prophet Muhammad SAW told his people to stay away from something doubtful by doing something that is believed to be *halal*. As the Prophet Muhammad SAW said: "Leave what is doubtful to what is not doubtful". In the issue of retakaful, due to unauthorized elements in reinsurance operations, then takaful companies should avoid using conventional reinsurance services. In brief, the practice allowing the takaful operator cedes of Takaful to

³⁰ ISRA, *Selected Resolutions of the Shariah Committee of Prudential BSN Takaful Berhad*.

³¹ Hasan, "Shari'ah Issues in The Operation of Retakaful and Reinsurance: A Preliminary Exploration from Shari'ah Perspective."

³² *Ibid.*

³³ *Ibid.*

³⁴ Rahman, Ahmad, and Buang, "Can a Takaful Company Reinsure with a Reinsurance Company?"

reinsurance companies are based on darurah (necessity) or hajah (dire need) and subject to certain conditions that have been established to limit this permission.

3.12. The Need To Enhance The Financial Capabilities Of The Retakaful To Manage The Risks.

There are many challenges in implementing retakaful such as enhancing their capacity for large risks and new products as their main services. These challenges are compounded by the fact that the takaful industry has failed to keep pace with conventional insurance underwriting capabilities. The inability of retakaful operators to find suitable shariah-compliant investment instruments are highly rated with a good return in their core financial markets.³⁵ Due to the small numbers of takaful operators and the limited size of their funds, the takaful operators have caused the takaful operators to seek reinsurance from the established companies. The existence of takaful operators requires sufficient retakaful companies to distribute the risks faced by the takaful operators. As mentioned earlier, although as of January 2020, there were only four (4) retakaful companies operating in Malaysia, the number is still small. The list provides a ratio of takaful companies to retakaful companies at 4:15 or equivalent to 27 per cent; this ratio shows the retakaful companies still inadequate. As a result, they had to use conventional reinsurance services. If the professional opinions state that this ratio is still insufficient, then the said: "darurah situation" is still applicable.

Moreover, the inadequacy of retakaful company funds to cover the risk of takaful companies is one of the factors that cause takaful companies to seek reinsurance company services. There are still many takaful companies that still use conventional reinsurance services in protecting the risks they incur. The risk faced by takaful companies is due to the limited funds to pay the participants when they incur losses.³⁶ Retakaful companies need to ensure that they are adequately capitalized to protect the company's financial stability from unfavourable underwriting outcomes and stabilize claims ratios from one year to the next. By allowing greater flexibility in the size and form of risks accepted, retakaful would undoubtedly improve capability and insurers' profitability.

³⁵ Corneille Karekezi, "The Critical Role of Retakaful in Africa," *Middle East Insurance Review*, 2020, https://www.africa-re.com/uploads/content/download_translation/download/5fe31089-e74d-4c6d-9663-2ce144247384.pdf.

³⁶ Syarifah Nur Amalina Syed Nasaruddin, "Cabaran Dan Peluang Retakaful Di Malaysia," in *Proceeding of the 2nd International Conference on Economic & Banking*, 2016, 57–63.

Otherwise, most contracts used in retakaful operations are still using the same mechanism as those used in conventional reinsurance operations.³⁷ The terms used in reinsurance operations are not suitable for use in retakaful operations. Lack of standardization in the retakaful system can also hinder the growth of the retakaful industry. Retakaful standardization refers to different operating models, account standards and various Shari'ah interpretations.³⁸ Besides, an independent agency's 'rating' should be given to a retakaful company to show the importance of good performance in the takaful industry. The rating agencies will also constantly monitor the performance of each retakaful company, whether it will be upgraded or downgraded. Therefore, every retakaful company should always work hard to ensure that their rating level remains upgraded to a better level.

3.13. The commission received by the retakaful were perceived as conflicting with the Shari'ah.

The commission received by the retakaful operator were perceived as conflicting with the Shari'ah. The commission payments received is in the form of retribution, hence removes the element of *tabarru'* of the takaful contract concerned. Also, the payment is said not to be based on the actual cost of such premium management. On the other hand, commission payments are based on the pre-calculations or estimates on the percentage of premiums submitted to the insurance company to be paid to the covered risks. When the takaful company receives the payment, the question arises when it does not share the losses incurred by the reinsurance company.³⁹ In addition to the use of Islamic contract in its operation, retakaful does not earn commission as a profit or interest because this commission is subject to *riba* and dilutes the intent of creating a takaful operation. For example, the reinsurance commission, which the insurance company earns directly from the reinsurance contract, does not comply with the principles of Shari'ah.⁴⁰ In contrast, retakaful operation depends on the actual costs incurred by the takaful operator in the retakaful process.

³⁷ Mahomed Akoob, "Reinsurance and Retakaful," in *Takaful Islamic Insurance: Concepts and Regulatory Issues*, ed. Simon Archer, Rifaat Ahmed Abdul Karim, and Volker Nienhaus (John Wiley & Sons (Asia) Pte. Ltd, 2009), 143–55.

³⁸ Yusuf and Yuhasni, "Revisiting and Redefining the Concept of Retakaful and the Viability of Its Model in Malaysian Takaful Industry."

³⁹ Nasri, "Takaful Semula Dalam Industri Insurans: Tinjauan Khusus Menurut Perspektif Islam Dan Undang-Undang."

⁴⁰ Rahman, Ahmad, and Buang, "Can a Takaful Company Reinsure with a Reinsurance Company?"

4. Conclusions

Retakaful are very much needed in the takaful industry in Malaysia. The existence of awareness among customers, whether Muslim or non-Muslim individuals or organizations interested in purchasing products offered by takaful companies. With the rapid growth and development in the takaful industry, takaful operators need support from retakaful companies to share the risks borne by them. Retakaful is important for takaful companies because it will enable them to pay all claims made by their customers. However, to date, the existence of retakaful companies operating in Malaysia is very limited. Only four retakaful companies are licensed to operate in Malaysia compared to the relatively large number of takaful operators of 15 companies. Therefore, on the grounds of urgency and problems, the Shariah Advisory Council of Bank Negara Malaysia has issued a resolution requiring takaful companies to use conventional reinsurance services to protect the risks they bear from customers. However, the Shariah Advisory Council of Bank Negara Malaysia has set several conditions that must be complied with by takaful operators if they wish to use reinsurance services from conventional reinsurance companies. Therefore, because retakaful companies have a very important role in the takaful industry, some proactive measures need to be taken to maintain the benefits and sustainability of takaful products while rejecting products involved with elements prohibited by Islam; *riba*, *gharar* and *maysir*.

References

- Abubakar, YS, MA Zahid, and R Markom. "Effect of Nomination Under Life Insurance and Family Takaful." *ISRA International Journal of Islamic Finance* 195, no. 2632 (2014): 1–23.
- Ahmad, Abu Umar Faruq, Ismail Bin Mahbob, and Muhammad Ayub. "The Nature of Retakaful: Risk-Sharing or Transferring Risks?" In *Takaful and Islamic Cooperative Finance*, edited by S. Nazim Ali and Shariq Nisar, 171–91. Cheltenham: Edward Elgar Publishing, 2016.
- Akoob, Mahomed. "Reinsurance and Retakaful." In *Takaful Islamic Insurance: Concepts and Regulatory Issues*, edited by Simon Archer, Rifaat Ahmed Abdul Karim, and Volker Nienhaus, 143–55. John Wiley & Sons (Asia) Pte. Ltd, 2009.
- Arbouna, Mohammed Burhan. "The Operation of Retakaful (Islamic Reinsurance) Protection." *Arab Law Quarterly* 15, no. 4 (2000): 335–62.

- Bank Negara Malaysia. *Kompilasi Keputusan Syariah Dalam Kewangan Islam*. 3rd ed., 2007.
- . *Resolusi Syariah Dalam Kewangan Islam*, 2010.
- . *Resolution No 47, Shariah Resolution in Islamic Finance*. 2nd ed., 2010.
- . *Shariah Resolutions in Islamic Finance*. 2nd ed., 2010.
- Daud, Wan Norhayate Wan, Fakhrol Anwar Zainol, Fauzilah Salleh, Ahmad Shukri Yazid, Suraya Ismail, Ruzian Markom, and Miss Nurdalila Mukhtar. “Takaful Rules and Regulations for ASEAN Countries: Takaful Player Perspectives.” In *Proceedings of the 30th International Business Information Management Association Conference, IBIMA*, 2017.
- Gunardi, Setiyawan, Nurdeng Deuraseh, Hailani Muji Tahir, and Sanep Ahmad. “Retakaful From Syariah Perspective: A Comparative Study.” *Chinese Business Review* 12, no. 9 (2013): 616–24.
- Hasan, Aznan. “Shari’ah Issues in The Operation of Retakaful and Reinsurance: A Preliminary Exploration from Shari’ah Perspective.” *IJUM Law Journal* 19, no. 2 (2011): 150–78.
- Heradhyaksa, Bagas, and Ruzian Markom. “Jurisdiction of Sharia Supervisory Board in Indonesian Takaful Industry.” In *IOP Conf. Ser.: Earth Environ. Sci.* 175 012177, 1–7, 2018.
- INCIEF. *Takaful Realities & Challenges*. Petaling Jaya: Pearson Malaysia, 2012.
- ISRA. *Selected Resolutions of the Shariah Committee of Prudential BSN Takaful Berhad*. Petaling Jaya: ISRA, 2020.
- Jamil, S. N., and J. Jamal. “Importance of Islamic Financial Services Act 2013 in Takaful Industry After the Repealed Takaful Act 1984.” *Diponegoro Law Review* 1, no. 1 (2016): 17–27.
- Karekezi, Corneille. “The Critical Role of Retakaful in Africa.” *Middle East Insurance Review*, 2020. https://www.africa-re.com/uploads/content/download_translation/download/5fe31089-e74d-4c6d-9663-2ce144247384.pdf.
- Muhamat, Amirul Afif, Mohamad Nizam Jaafar, and Mohd Shamsuri MD Saad. *Essential Components of Takaful Operation*. UTEM Press, 2019.
- Nasaruddin, Syarifah Nur Amalina Syed. “Cabaran Dan Peluang Retakaful Di Malaysia.” In *Proceeding of the 2nd International Conference on Economic & Banking*, 57–63, 2016.
- Nasri, Mohd Sabree. “Takaful Semula Dalam Industri Insurans: Tinjauan Khusus Menurut

- Perspektif Islam Dan Undang-Undang.” *Journal of Law & Governance* 1, no. 1 (2018): 49–61.
- NuHtay, Sheila Nu, Mustapha Hamat, Wan Zamri Wan Ismail, and Syed Ahmed Salman. “Retakaful (Islamic Reinsurance): Historical, Shari’ah and Operational Perspectives.” *World Applied Sciences Journal 30 (Innovation Challenges in Multidisciplinary Research & Practice)*, 2014, 185–90.
- Rahman, Asmak Ab, Wan Marhaini Wan Ahmad, and Ahmad Hidayat Buang. “Can a Takaful Company Reinsure with a Reinsurance Company?” *African Journal of Business Management* 5, no. 30 (2011): 11768–78.
- Samsuri, M. A. Z. Ahmad, and J. Jamal. “Takaful Agent Must Foster Public Understanding of Takaful.” *Diponegoro Law Review* 2, no. 2 (2017): 245–58.
- Sum, Cheah You, Hasani Mohd Ali, and Ruzian Markom. “Legal Issues Concerning Insurable Interest and Permissible Takaful Interest at the Time of Death under Conventional and Family Takaful Contract.” *International Journal of Business and Society* 19, no. 3 (2018): 353–67.
- Yusuf, Mohamed, and Rosmi Yuhasni. “Revisiting and Redefining the Concept of Retakaful and the Viability of Its Model in Malaysian Takaful Industry.” *Business and Management Quarterly Review (BMQR)* 2, no. 4 (2011): 20–32.