

# Regulatory Framework for Takaful

International Conference on Mutual Insurance and Takaful  
Istanbul, Turkey  
13 November 2012



**BANK NEGARA MALAYSIA**  
CENTRAL BANK OF MALAYSIA

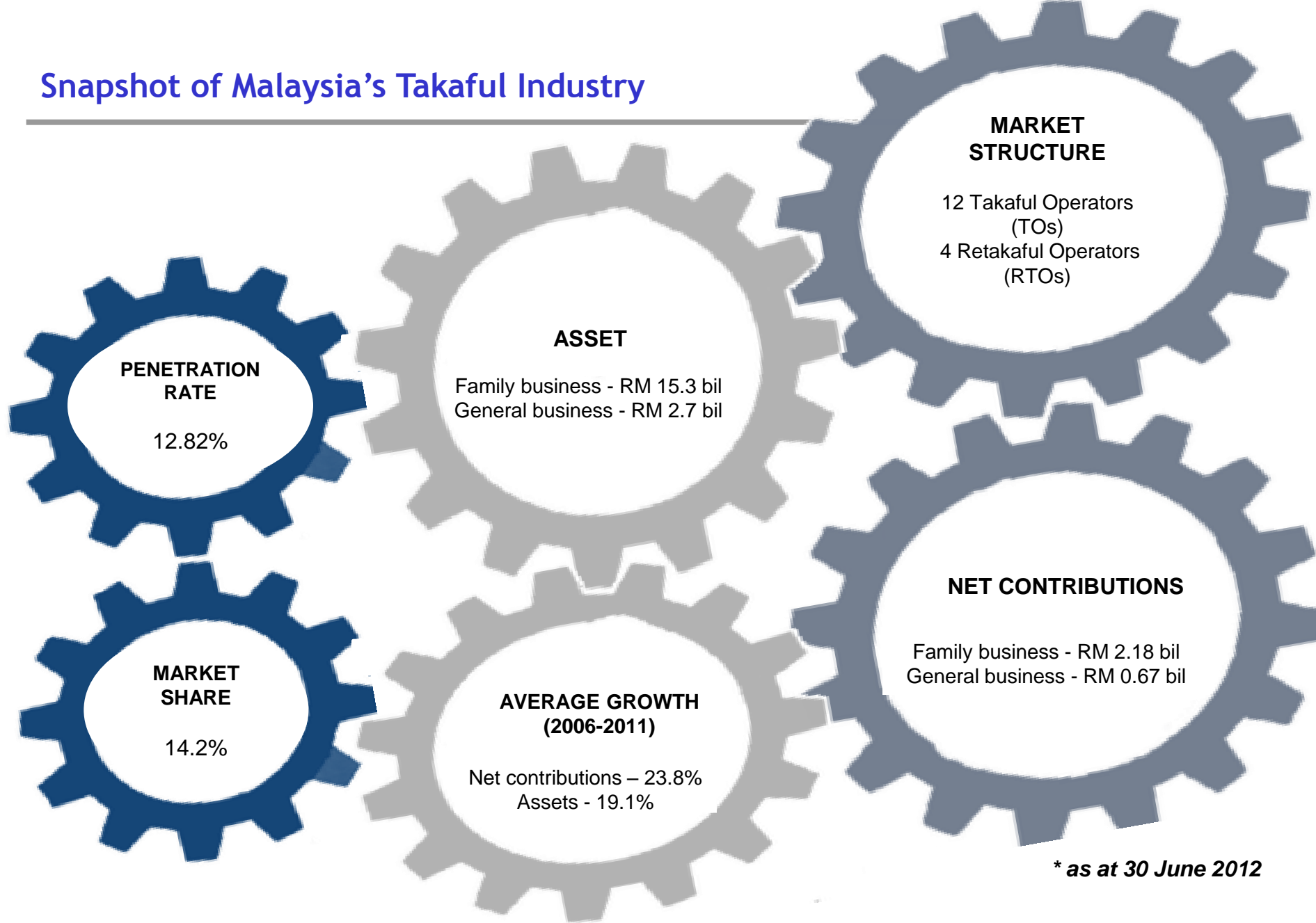
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**Director**  
**Islamic Banking and Takaful Department**

# Agenda ...

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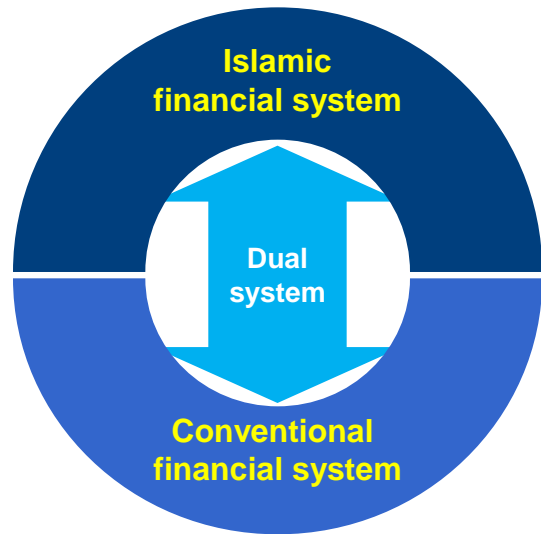
- **Snapshot of Malaysia's Takaful Industry**
- **Dual Financial System in Malaysia**
- **Fundamentals for Sound Takaful Development in Malaysia**
- **Regulatory and Supervisory Framework in Malaysia**
- **Regulatory Requirements For Takaful**
  - Takaful Operational Framework
  - Shariah Governance
  - Risk-Based Capital Framework
- **Moving Forward**

# Snapshot of Malaysia's Takaful Industry



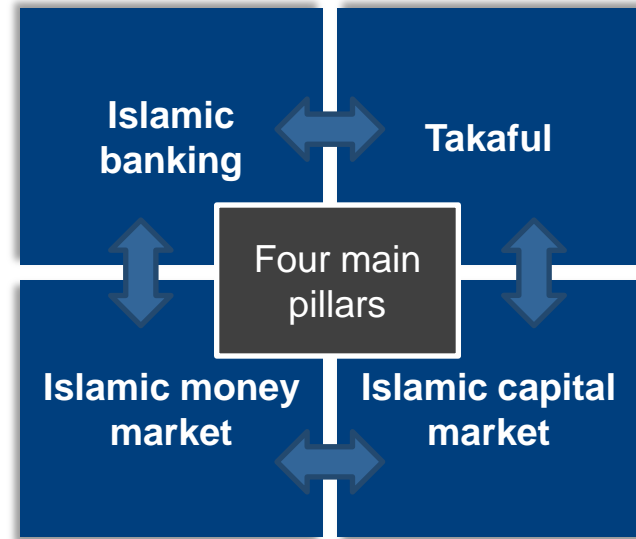
*\* as at 30 June 2012*

# Takaful in Malaysia developed as component of comprehensive Islamic financial system operating in parallel with conventional financial system



## Dual Financial System

The mandate for developing dual financial system explicitly codified in Central Bank of Malaysia Act 2009



## Comprehensive Islamic Financial System

- Ensure sustained industry viability via optimised synergies from interlinkages
- Underpinned by :
  - ◆ Strong & diversified players
  - ◆ Wide range of products & vibrant financial market

# Fundamentals for sound takaful development in Malaysia ...



## Facilitative Legal Framework

Takaful Act 1984 (TA) provides platform for separate regulatory structures

## Robust Shariah governance structure

Foundation for Shariah governance setting in TA :

- Business aims & operations must be Shariah compliant
- Takaful operator (TO) to establish Shariah Committee (SC)

## Inception stage

Instituting foundations of Islamic finance

## Effective & efficient consumer protection

Establishment of BNM LINK, Financial Mediation Bureau & dedicated division in High Court

## World class talent pool & IF learning hub

- Establishment of IBFIM, INCEIF & ICLIF
- Fund for Shariah Scholars in Islamic Finance

## Strong institutional framework

- Dedicated department in Bank Negara Malaysia for Islamic Banking & Takaful
- Establishment of Malaysian Takaful Association

## Institutional Capacity Enhancement

Minimum paid-up requirement increase to RM100 m

## Robust Shariah governance structure

- Establishment of Shariah Advisory Council of BNM (SAC)
- Restrict SAC members to sit in SC of TOs

## Intermediate stage

Institutional building, activity generation & market vibrancy

## Facilitative Legal Framework

Development of Islamic Financial Services Act

## World class talent pool & IF learning hub

- TO to have Appointed Actuary
- Creation of ISRA as IF research centre
- Publication of Shariah standard

## Strong institutional framework

Increase no. & diversity of players e.g. TO (12) and RTO (4)

## Institutional Capacity Enhancement

- Risk-Based Capital Framework
- Takaful Operational Framework

## Robust Shariah governance structure

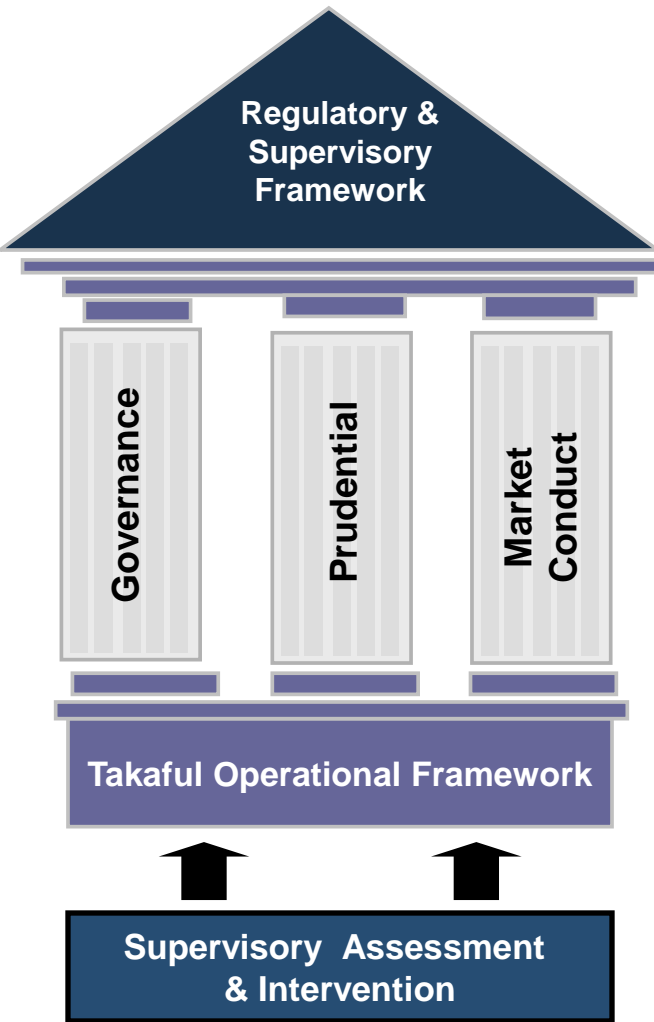
CBA amendments:

- SAC as a highest authority for the ascertainment of Islamic law on IF
- Rulings of SAC shall be binding on IFIs, courts or arbitrators

## Advanced stage

Strategic positioning & international integration

# Regulatory and Supervisory Framework in Malaysia ...



## Objectives

- Preserve financial stability & public confidence
- Prevent risk of contagion & systematic failure
- Ensure good market practices
- Promote high standard corporate & Shariah governance

## Pragmatic approach to regulation

- Leveraging on established field of conventional system
- Separate rules to address takaful industry peculiarities
  - Shariah-compliant in all aspects of the takaful operation
  - Balance between interests of shareholders & participants
  - Separation of funds between shareholders & takaful fund
- Efficient and forward looking supervision under Risk-Based Supervisory Framework

**Regulatory framework for insurance broadly applicable... but requires adaptation to be more takaful-attuned**

**Legal framework being strengthened by Islamic Financial Services Act to enable more comprehensive regulation and supervision of the takaful industry**

# Regulatory Requirements for Takaful ...

Shariah compliance in all aspects

<b>Prudential</b>	<b>Governance</b>	<ul style="list-style-type: none"> <li>Duties &amp; responsibilities of board of directors, senior management, appointed actuary &amp; external auditor</li> <li>Minimum expectation for TO on outsourcing of takaful activities, functions or processes</li> </ul>	<ul style="list-style-type: none"> <li>Duties &amp; responsibilities of the Shariah Advisory Council &amp; Shariah Committee</li> <li>Fiduciary duties of takaful operator (TO)</li> <li>Stature of participants in takaful</li> </ul>
	<b>Assets, Investments &amp; Liabilities</b>	<ul style="list-style-type: none"> <li>Diversification rules, basis for valuation &amp; safekeeping of assets</li> <li>Investment limit permissible</li> <li>Determination &amp; provisioning of liability</li> </ul>	<ul style="list-style-type: none"> <li>Invest in Shariah-compliant instruments</li> <li>Management of takaful fund</li> <li>Accounting treatments</li> </ul>
	<b>Solvency</b>	<ul style="list-style-type: none"> <li>Capital adequacy based on risk profiles</li> <li>Stress test process that commensurate to nature, complexity &amp; sophistication of the business</li> </ul>	<ul style="list-style-type: none"> <li>Qard to rectify deficit in takaful fund</li> </ul>
	<b>Product Requirements</b>	<ul style="list-style-type: none"> <li>Sound risk management practices in developing, managing &amp; controlling product risk</li> </ul>	<ul style="list-style-type: none"> <li>Shariah endorsement on product</li> <li>Fees, charges &amp; surplus distribution</li> </ul>
	<b>Reporting, market conduct &amp; market protection</b>	<ul style="list-style-type: none"> <li>Disclosure &amp; presentation of reports &amp; statements</li> <li>Minimum standard on product transparency &amp; disclosures</li> </ul>	<ul style="list-style-type: none"> <li>Separation of funds</li> <li>Disclosure on aqad, fees, profit sharing ratio</li> </ul>

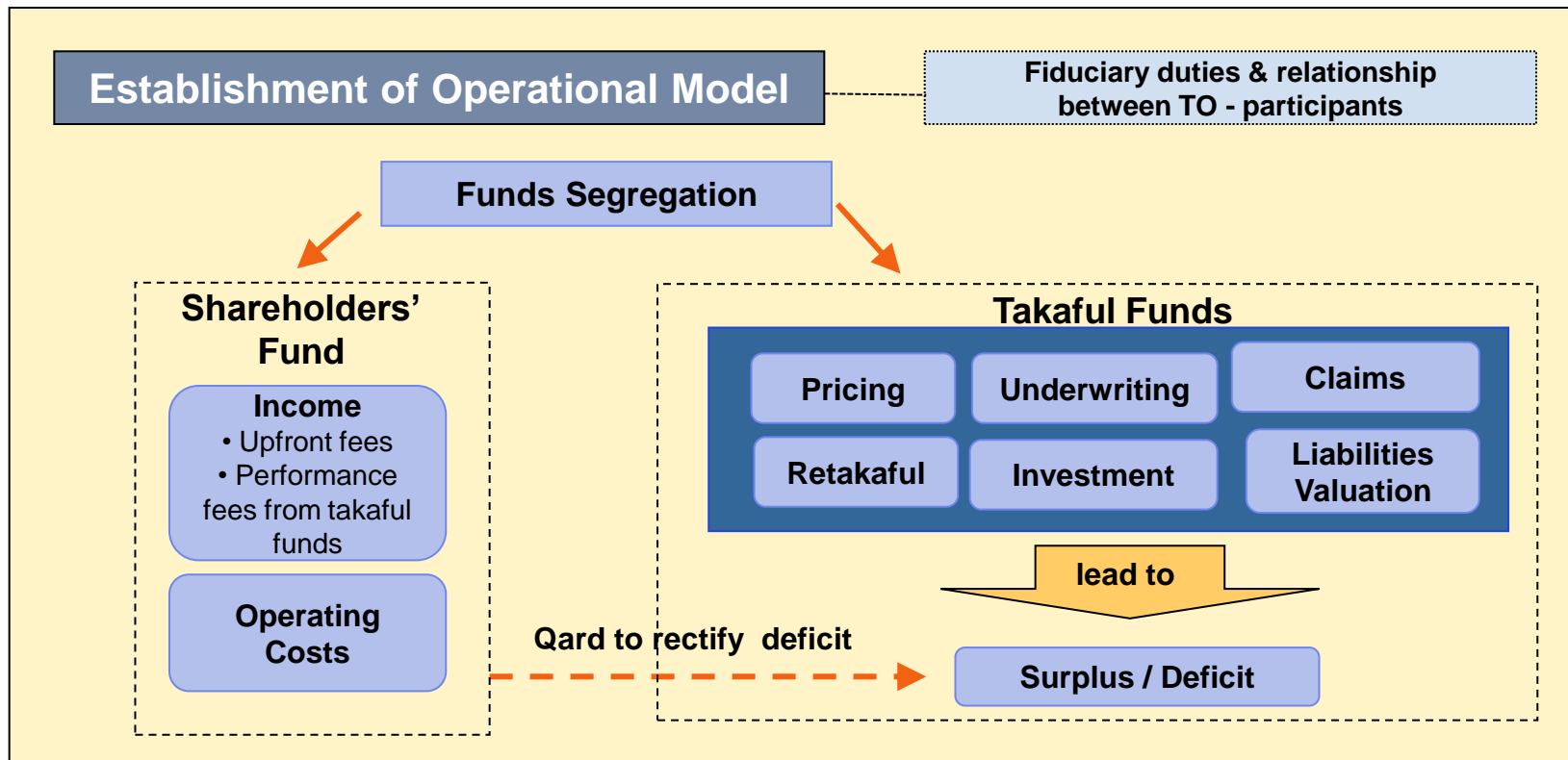
**Effective supervisory assessment on safety & soundness of TOs under Risk-Based Supervisory Framework**

# Takaful Operational Framework ...

## Objectives & Principles

- Ensure uniformity with Shariah
- Safeguard interests of the participants
- Promote prudent management
- Enhance operational efficiency
- Build healthy takaful funds
- Promote uniformity in practices

Outlines requirements in the following areas....

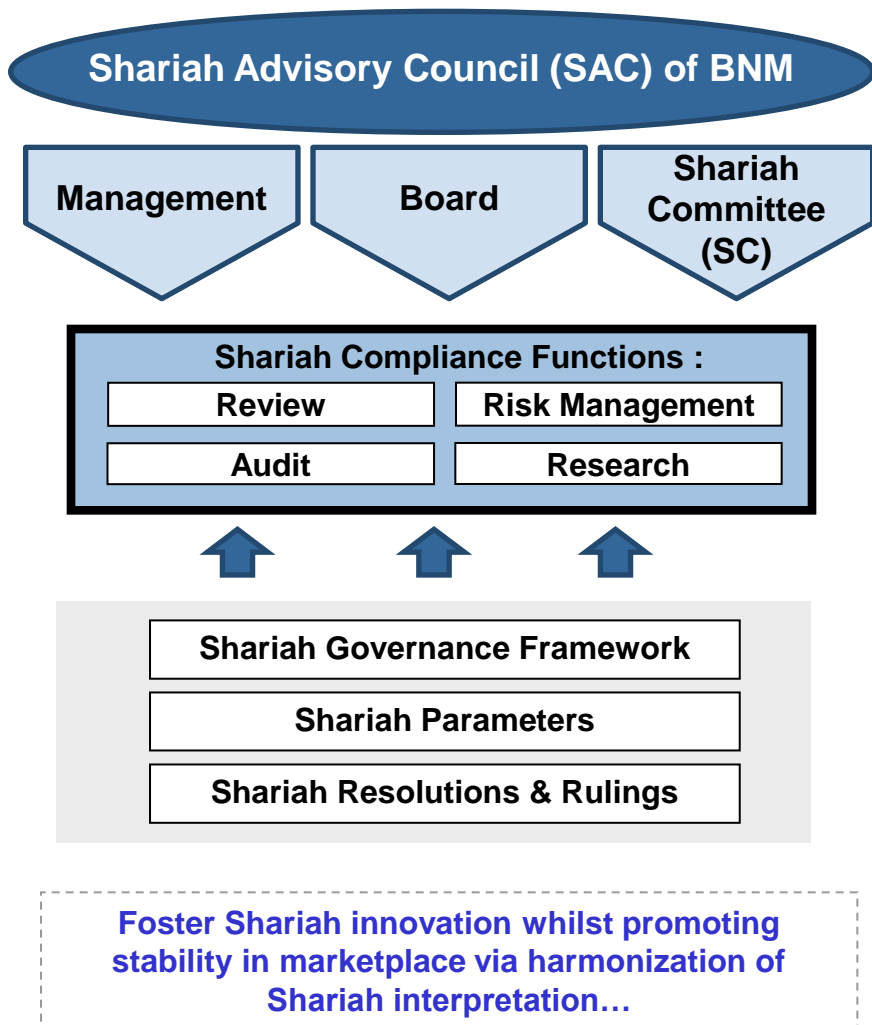


## Supported by:

- Effective governance & oversight
- Adequate disclosure & transparency
- Sufficient & competent resources
- Efficient processes & procedures



# Shariah Governance ...



## Shariah as overarching principle in Islamic finance

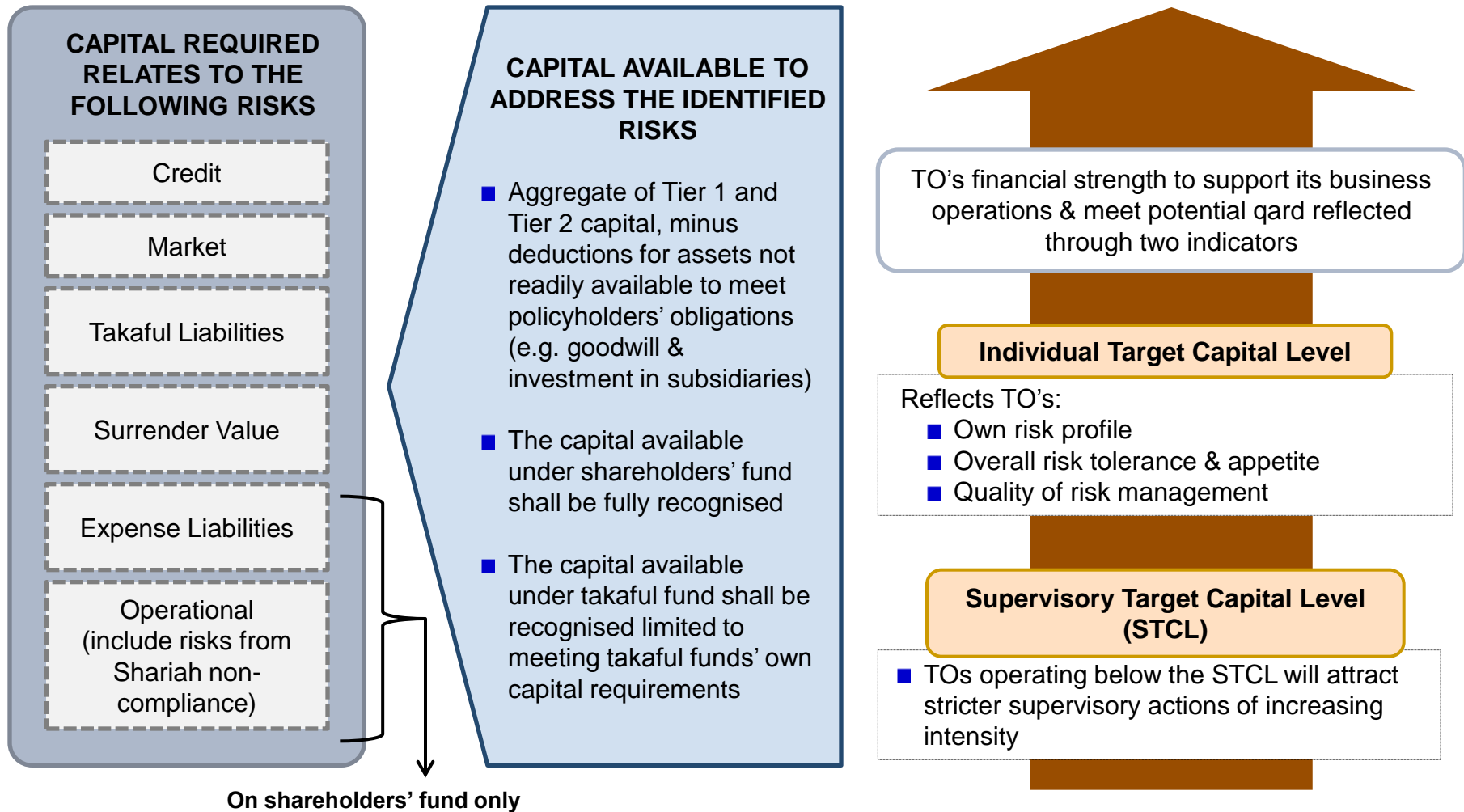
Proper governance provides assurance on Shariah compliance & confidence on takaful operation:

1. **SAC's legislative stature as highest authority** accorded under Central Bank of Malaysia Act 2009
2. SC of takaful operator **accountable on decision, views & opinions**
3. Board & senior management with **sufficient expertise & capability** on takaful (Islamic finance) issues
4. Function of Shariah risk management, research, review & audit to **provide check & balance**
5. SC member of another takaful operator shall not be appointed – **avoid conflict of interest & maintain info confidentiality**
6. Shariah parameters provide **guidance on main features, principles & rulings**
7. **Institutionalise mutual respect** by recognising differences of Shariah interpretations

# Risk-Based Capital Framework for Takaful Operators (RBCT) ...

## Objectives

- Enable all obligations under a takaful contract & costs of managing the takaful business are met
- Provide flexibility for takaful operator (TO) to operate at different risk levels as long as there is supporting capital
- Ensure availability of funds to provide interest-free loan (qard) should the need arise



## Future development & initiatives under Financial Sector Blueprint

### 1 Regulatory & supervisory regime

- Enactment of a comprehensive legislative framework for the conventional & Islamic financial systems respectively

### 3 Increase the diversity of players

- Issue new takaful licenses to institutions with specialised expertise
- Encourage international players to establish retakaful operations
- Promote greater involvement of takaful brokers

### 5 Talent development

- Promote standards & accreditation of Islamic finance programmes
- Introduce dedicated training programmes for Shariah graduates

### 2 Strengthen Shariah governance framework

- Establish a single legislated body as the apex authority on Shariah matters
- Strengthen International Shariah Research Academy for Islamic Finance to become a premier international research agency

### 4 Increase market efficiency

- Facilitate the development of standard retakaful documentation

### 6 Wide range of products & services

- A regulatory framework that facilitates the offering of affordable microtakaful