Takaful institutions prudential framework and financial safety net

TAKAFUL & RE-TAKAFUL (EUROPE)

By Ezzedine Ghlamallah

Currently, the governance standards for Takaful operators vary by jurisdiction, as in the absence of a uniform framework, countries have developed their own frameworks based on their own needs and experiences. Global regulation and industry self-regulatory organizations, such as the IFSB and AAOIFI, have made significant progress in developing standards for governance, financial reporting and compliance. These organizations fought consistently to gain broad support from regulators to implement these standards and best practices.

At the same time, Islamic financial institutions have encouraged product innovation away from fixed-rate lending transactions to promote profit-sharing contracts. Practitioners and regulators must work together to ensure that these standards can be implemented and be operational in real-life situations. It is not enough for these challenges to be addressed or implemented without the commitment and support of Takaful boards and executives.

Thus, Takaful operators need to improve their governance and risk management control processes. The importance of a Takaful operator-wide risk strategy should not be overlooked, and the support, as well as supervision, of boards of directors is a key factor in setting up a company based on the risk culture in the Takaful sector. The reputation of a Takaful operator depends essentially on the perception of customers in terms of its conformity with Islamic law and the guarantees of financial soundness offered to participants. It is clear that national and international regulatory initiatives will impact how Takaful operators interact with their customers and environment.

Takaful business strategies and models will need to be re-engineered, taking into account the expansion of regulation, growing competition from conventional insurers, pricing strategies and cost models. The General and Family Takaful solutions may need to be redesigned to accommodate a broader clientele, including non-Muslims, and will need to provide generic insurance coverage in all types of Takaful products. Product governance and processes need to be improved to ensure regulatory and Shariah compliance.

As stated in IFSB-8, a Takaful operator must reflect its prudential policies in its business processes through the design and implementation of controls, risk reporting and systematic compliance assessment.

> ***"The reputation of a Takaful operator depends essentially on the perception of customers in terms of its conformity with Islamic law and the guarantees of financial soundness offered to participants"***

The supervisory authority must take into account the implementation of formal requirements so that Takaful operators can report to it on risk management. The frequency and scope of these reporting requirements must be consistent with the nature, scale and complexity of a Takaful business.

The supervisory authority will consider whether the reports require independent external evaluation. In its risk management policy, Takaful covers the following aspects of underwriting and provisioning risks:

- the type and characteristics of the operator's business, such as the type of insurance risk that the operator accepts
- the manner in which contributions cover claims and expected expenses
- the identification of risks arising from operator obligations and the guaranteed redemption values of its products, and
- how the operator considers investment constraints, reinsurance and other risk mitigation techniques in the process of designing a new insurance product and the calculation of contributions.

Ezzedine Ghlamallah is the executive director of SAAFI which specializes in Islamic finance and Takaful solutions. He can be contacted at ezzedine.ghlamallah@saafi.fr.

IFN Sector Correspondents

CROWDFUNDING: Craig Moore
CEO, Beehive

DEBT CAPITAL MARKETS: Imran Mufti
partner, Hogan Lovells

EDUCATION: Dr Kamola Bayram, project director for training and research at the International Council of Islamic Finance Educators

ISLAMIC LEASING: Shoeb Sharieff
president, ijara CDC, ijara Community Development Corp

LAW: Paul McViety
partner, head of Islamic finance, DLA Piper Middle East

MERGERS & ACQUISITIONS: Burak Gencoglu
partner, Gencoglu & Ergun Law Firm

MICROFINANCE: Mohammed R Kroessin
head of Islamic microfinance, Islamic Relief Worldwide

PRIVATE EQUITY & VENTURE CAPITAL:
James R Stull, partner, King & Spalding

REAL ESTATE: Philip Churchill
founder partner, 90 North Real Estate Partners

RETAIL ASSET MANAGEMENT: Muzzammil Dhedhy, chief operating officer, Hejaz Financial Services

RISK MANAGEMENT: Dr Ken Baldwin
senior lecturer in finance, Coventry University

SHARIAH & CORPORATE GOVERNANCE:
Prof Dr Mohamad Akram Laldin
executive director, International Shariah Research Academy for Islamic Finance

SRI ETHICAL & GREEN: Dr Mohamed Wail Aaminou, general manager, Al Maali Consulting Group

TAKAFUL & RE-TAKAFUL (ASIA): Marcel Omar Papp
head of Retakaful, Swiss Re Retakaful

TAKAFUL & RE-TAKAFUL (EUROPE): Ezzedine Ghlamallah
director, Solutions Insurance and Islamic Finance (SAAFI)

TAKAFUL & RE-TAKAFUL (MIDDLE EAST):
Dr Sutan Emir Hidayat
assistant professor, head of Business Administration and Humanities Department, University College of Bahrain

IFN Correspondents are experts in their respective fields and are selected by Islamic Finance *news* to contribute designated short sector reports. For more information about becoming an IFN Correspondent, please contact sasikala.thiagaraja@redmoneygroup.com