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THE INVESTMENT INITIATIVE IN *TAKĀFUL*: ISSUES AND CHALLENGES

*Mohammad Mahbubi Ali and Muhammad Ali Jinnah Ahmad**

I. INTRODUCTION

The concepts of mutual assistance and charity often come to mind when *takāful* (Islamic insurance) is mentioned. This is understandable given that *takāful*, in the generic sense, has played an essential role in risk sharing in Muslim history. However, another feature has been added to the modern practice of *takāful*. The current *takāful* scheme has added the investment element to its products, one of a number of features that it shares with conventional insurance. The investment feature has become an inherent part of *takāful* activities, departing from its original core roles of providing mutual guarantee, assistance and solidarity. This is most apparent when looking at family *takāful* where the participant's fund is segregated into two pools: the participant's risk fund (PRF) and the participant's investment fund (PIF). The offering of a number of investment-linked products in the market has led to making the *takāful* scheme more appealing and competitive. This evolution has been the result of a natural progression to ensure that *takāful* operations remain continuously viable and compatible in the current economic and social environment.

However, the investment role carried out by *takāful* operators has raised a number of questions. Some have argued that it is inappropriate for *takāful* to incorporate the investment feature in addition to its core focus of protection as it contradicts the social and charitable nature of *takāful*. Others are of the view that there is nothing wrong with the investment initiative undertaken by *takāful* operators as long as the investment activities are in compliance with Islamic law and the contractual mechanic requirements are satisfied.

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II. OBJECTIVES AND ORGANISATION OF RESEARCH

This research has the following three primary objectives:

1. To understand the Shari'ah perspective on the investment initiative carried out by the *takāful* industry.
2. To identify contentious Shari'ah issues, prevailing operational issues and legal issues surrounding the investment fund in the *takāful* industry.
3. To propose guidelines and parameters for the *takāful* industry in undertaking the investment role.

Employing a qualitative descriptive method, the paper will be organized as follows: Firstly, it will discuss the importance of investment in financial operations. Secondly, it will review the Shari'ah perspectives on the investment initiatives undertaken by *takāful* operators. The discussion will explore the concept of investment in the light of the Qur'ān, Sunnah and juristic views. The discussion will also examine the *fiqh* characterization (*takyīf fiqhī*) of *takāful* operators' investment activities. Thirdly, the paper will identify existing Shari'ah issues, operational issues and legal challenges experienced by *takāful* operators in carrying out the investment role. The paper will conclude by providing certain guidelines and parameters for investment activity in the *takāful* industry.

III. PRELIMINARY FINDINGS

The preliminary findings of the research reveal that the current Shari'ah contracts employed as a *takyīf fiqhī* for the participant's investment fund (PIF) are *muḍārabah*, *wakālah bil istithmār* or a combination of the two. The position of *takāful* operators in managing the PIF is either as investment agent (*wakīl*) or investment manager (*muḍārib*). The paper has also identified a number of contentious Shari'ah, legal and operational issues faced by *takāful* operators in undertaking the investment role. Some significant Shari'ah issues include: (i) the management fee in the hybrid model and the fee for the fund manager; (ii) sharing of investment profit in the modified *wakālah* model; (iii) commingling the fund; (iv) investment in mixed companies; and (v) income purification when Shari'ah-compliant companies or securities are ruled as non-Shari'ah compliant. The main legal and operational issues, among others, relate to participants' involvement in *takāful*,

such as in the Annual General Meeting (AGM), the limited avenues for investment, cross-border investments, asset-liability management, and structural as well as governance issues.

Some parameters are proposed, primarily to overcome the Sharī'ah issues, as follows:

1. The *takāful* operator should clearly disclose the Sharī'ah principle underlying the investment product to the participants. All expenses chargeable to the *takāful* fund shall also be clearly disclosed. The fund should also be invested in Sharī'ah-compliant businesses. Any income from non-Sharī'ah compliant investment activities shall be channelled to charity.
2. *Tabarru'* and investment contracts in *takāful* operations should be concluded independently and separately. In family *takāful*, the *takāful* operators should establish the investment of the PRF and the PIF separately to recognize their different purposes, ownership and associated risks, and the commingling of funds must be avoided. The signing of the contracts should also be segregated in different contract agreements, i.e. (i) the *tabarru'* agreement and (ii) the *wakālah* agreement.
3. Any loss in the *takāful* investment fund in *muḍārabah* and *wakālah* structures should be borne by the participants. However, should the loss be caused by the negligence of the *takāful* operator, it shall be covered by the shareholder's fund. Therefore, as the participants bear all investment risks, they should be made aware of all investment-related information, i.e. market movement and its implication on the PIF, potential risks and types of assets invested.
4. Under the *muḍārabah* or hybrid model, the *takāful* operator should not be allowed to impose a management fee for investing the fund as it will be rewarded from the profit-sharing agreement. However, if the fee charged is a part of other services executed in an independent contract, it would be allowed. Under the *wakālah* model, a fixed upfront fee should be charged on the contribution based on the contractual terms agreed during the signing of the contract to avoid uncertainty and ignorance. The fee can be based either on a percentage of the contribution or set at a fixed amount. It is not allowed to impose a fee based on the percentage of surplus or percentage of profit. It is also impermissible to share any investment return as the *takāful* operator has been compensated with the fixed upfront fee.

5. *Takāful* operators should have a clear mechanism for the participants' involvement. The mechanism can be created through various means. For instance, the Takāful Act 1984 can be amended to regulate the involvement of participants and the participants' election of one or more individuals to represent them in dealings with the operator. Reporting all investment-related information to the participants should be mandated.

IV. CONCLUSION

The study will provide literature on the *fiqh* characterization of the investment initiative in *takāful* operations as well as provide guidelines that govern the investment role of the *takāful* funds. This could serve as reference material for industry players to assist them in their continuous efforts of ensuring more standardized and transparent investment operations in line with Shari'ah principles and objectives.

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