CHALLENGES IN *TAKAFUL* APPLICATION WITHIN CONVENTIONAL INSURANCE FRAMEWORK IN NIGERIA – THE IMPERATIVE FOR LEGISLATIVE HARMONIZATION OF REGULATORY INSTRUMENTS

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ABSTRACT

The Nigerian insurance industry as a growth sector is struggling and stagnant despite its immense potential. The pervasive insurance gap induced by the lack of deepening insurance penetration has succeeded in financially excluding and underserving the greater Muslim majority of the populace. The *Takaful* Operational Guidelines, introduced in 2013 is adjudged an avenue for expanding into new geographies and client segments flavoured with a *Shari'ah*-compliant appeal in bridging the endemic insurance gap. However, the Guidelines, Insurance Act, and a host of other enabling regulatory instruments are enmeshed in a web of regulatory conflict and ambiguity - conditions inimical to the successful application of *Takaful*. The purpose of this research is to examine the effects of these conflicting regulatory provisions on *Takaful* application with a view to overcoming the inherent challenges by harmonizing the various enabling insurance instruments. The thesis scrutinises the legal framework of the government entrenched conventional insurance practice in Nigeria and how it breeds mistrust and apathy in the industry which has been responsible for low-level involvement by the populace. A contextual analysis of *Takaful's* legal sources and development precedes the discussion on its application in the Nigerian regulatory framework to illustrate how it differs from conventional insurance and how an efficient and effective *Takaful* regulatory framework can help bridge the endemic insurance gap in Nigeria. The study also highlights the analytical similarities and differences between the two types of insurance practices especially in their antecedents, structure of products and practices while subsequently elaborately discussing the general and regulatory challenges facing *Takaful*. The study examines the provisions of the Insurance Act especially the delineating section and the section conferring supremacy in the Act, among others, as those inimical to the efficient and effective application of *Takaful* within conventional insurance practice in Nigeria. This research is doctrinal, qualitative, and based purely on library study covering books, statutes, law reports, and internet sources from renowned databases and websites. Interviews are intercept, structured and semi-structured, and purposive to collect empirical data from targeted participants. Analyses of responses from interviews conducted suggest that ignorance, mistrust and apathy are largely responsible for the lack of participation and stunted growth of conventional insurance. Some respondents believe *Takaful* will boost insurance penetration if adequate regulatory framework and enforcement processes are put in place. While acknowledging the need for further empirical analysis in a future study, the thesis finds, among numerous other findings, the need for a wholesome *Takaful* legislation that will harmonize all the regulatory discrepancies, establish regulatory certainty and build trust in the struggling insurance industry. The study concludes that if the principal recommendation proposed by the thesis is adopted by enacting a wholesome *Takaful* Act like the current Islamic Financial Services Act (IFSA), 2013 of Malaysia, it will engender regulatory certainty that will positively influence the revival of trust in the insurance industry. This will further encourage patronage, product design and innovation that will lead to deepening insurance penetration and financial inclusion of the greater majority of the Nigerian underserved insurance populace.

ABSTRAK

Industri insurans di Nigeria, yang sepatutnya merupakan sebuah sektor yang berkembang, menghadapi kesusahan dan tidak berubah-ubah di sebalik mempunyai potensi yang luas di negara itu. Kekurangan yang jelas dan meluas dalam perkhidmatan insurans serta ketiadaan usaha memperdalam dan menembusi pasaran insurans telah berjaya, dari sudut kewangan, dalam mengecualikan dan mengurangkan perkhidmatan bagi populasi Muslim di Negara tersebut. Garispandu Operasi Takaful (Takaful Operational Guidelines) yang diperkenalkan dalam tahun 2013 telah diisytiharkan sebagai lebuh/jalan untuk meluaskan pasaran ke tempat-tempat dan segmen klien-klien yang baru bagi mengisi kekurangan dalam perkhidmatan insurans dengan menjadikan konsep patuh-Shariah sebagai tarikan. Walaubagaimanapun, Garispandu tersebut, Akta Insurans (Insurance Act), dan beberapa instrumen regulatori yang lain, adalah terperangkap di dalam percanggahan dan ketaksaan; perkara-perkara yang akan menghalang kejayaan pelaksanaan Takaful. Tesis ini memeriksa rangka kerja amalan insurans konvensional yang diasaskan oleh kerajaan di Nigeria dan bagaimana ia menghasilkan ketidakpercayaan dan sikap tidak peduli di dalam industri ini yang telah bertanggungjawab menyebabkan kurangnya kadar penyertaan di kalangan populasi setempat. Tesis ini didahului oleh satu analisis kontekstual terhadap sumber-sumber perundangan Takaful dan perkembangannya dalam aplikasinya dalam rangka kerja regulatori Nigeria untuk menampakkan bagaimana ia berbeza daripada insurans konvensional dan bagaimana suatu rangka kerja regulatori Takaful yang efisien dan berkesan boleh membantu mengisi kekurangan yang jelas dalam perkhidmatan industri di Nigeria. Kajian ini juga mempamerkan kesamaan dan perbezaan analitikal di antara kedua-dua jenis amalan insurans tersebut terutama sekali dari segi latar belakang, struktur produk-produk dan amalannya, dan seterusnya intipati tesis ini membincangkan secara terperinci cabaran-cabaran umum dan regulatori dalam pelaksanaan Takaful. Kajian ini mengenalpasti dan menekankan peruntukan peruntukan di dalam Akta Insurans terutama sekali seksyen penerangan (delienating section)dan seksyen yang memperuntukkan keagungan (supremacy) di dalam Akta, antara lain,sebagai seksyen-seksyen yang menghalang pelaksanaan Takaful yang efisien dan berkesan dalam insurans konvensional di Nigeria. Kajian ini berbentuk doktrinal, kualitatif, dan berasaskan sepenuhnya kepada kajian perpustakaan meliputi buku-buku, statut-statut, laporan undang-undang, dan sumber-sumber dari internet daripada pangkalan data dan laman web yang terkenal. Temubual yang digunakan adalah dengan cara 'intercept interview', dalam bentuk berstruktur dan separa-berstruktur, dengan menggunakan pensampelan purposif untuk mengutip data empirikal daripada peserta-peserta yang telah dikenalpasti. Analisa respons dari para peserta menunjukkan bahawa tiada pengetahuan, ketidakpercayaan, dan sikap tidak peduli merupakan sebahagian besar sebab kepada tiada penyertaan dan terbantutnya perkembangan dalam insurans konvensional. Sebahagian responden percaya bahawa Takaful akan meningkatkan peluang menembusi perkhidmatan insurans jika rangka kerja regulatori dan proses penguatkuasaan yang mencukupi diwujudkan. Di samping mengiktiraf keperluan terhadap analisis empirikal yang lebih lanjut dalam kajian akan datang, tesis ini mendapati, di samping banyak dapatan-dapatan lain, perlunya diwujudkan peruntukan Takaful yang lengkap yang akan mengharmonikan kesemua percanggahan-percanggahan regulatori, mewujudkan kepastian regulatori dan membina kepercayaan dalam industri insurans yang sedang menghadapi kepayahan. Kajian ini menyimpulkan jika pelbagai rekomendasi yang dicadangkan di dalam tesis ini dikuatkuasakan secara

efektif, Akta Takaful yang lengkap seperti Akta Perkhidmatan Kewangan Islam, 2013 (Islamic Financial Services Act (IFSA), 2013) yang wujud di Malaysia akan memberangsangkan kepastian regulatori yang akan memberikan impak positif dalam mengembalikan kepercayaan di dalam industri insurans tersebut, dan menggalakkan inovasi dan rekabentuk produk yang kemudiannya akan menjurus kepada usaha memperdalam dan menembusi pasaran insurans serta membawa masuk lebih ramai populasi Nigeria yang tidak mempunyai peluang mendapatkan insurans sebelum ini.

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LIST OF ABBREVIATIONS

AC	Appeal Cases
All Comm.	All Commercial
All E.R.	All English Reports
E.R.	English Reports
ATK	Atkins Reports Chancery
B and ALD	Barnwell and Alderson
Burr	Burrow
Ch. D	Chancery Division
Co.	Company
C.P.	Common Plea
DLR	Dominion Law Reports
E.C.S.L.R.	East Central State Law Report
F.N.L.R.	Federal Nigeria Law Report
Holt N.P.	Holt's Reports, Nisi Prius
Ins.	Insurance
K.B.	King's Bench
Lloyd's Rep.	Lloyd's List Law Reports
L.L.R.	Lagos High Court Reports
L.R.	Law Reports
Ltd.	Limited
MLR	Modern Law Report
N.M.L.R.	Nigeria Monthly Law Report
NWLR	Nigeria Weekly Law Report
Par.	Paragraph
QB	Queen's Bench

QBD	Queen's Bench Division
T.L.R.	Times Law Reports
Swan.	Swanston
UILR	University of Ife Law Reports

TERMINOLOGIES

Aqad: Contract

Aqilah: Blood money

Barakah: Blesssings

Darrurah: Permission due to unfavourable circumstances

Diyah : Blood money

Fatwa: Deliberations of Jurists

Fidyah: Ransom of prisoners of war

Fiqh: Jurisprudence

Gharar: Uncertainty

Haram: Forbidden

Halal: Permissible

Hudud: Islamic Capital Punishment

Husn: Beauty

Ijab: Offer

Ijtihad: Independent Reasoning

Ijma: Consensus Opinion of Jurists

Khatar: Peril/Danger

Khid'ah: Deceit/Fraud

Maysir: Gambling

Maslahah: Solutions

Mithl: Average

Mubah: Allowed

Mudharabah: Partnership

Qabul: Acceptance

Qard Hasan: Non-Interest Loan

Qiyas: Analogical Deductions

Quhb: Ugliness

Quraish: Prophet Muhammad's pbuh Tribe

Ribah: Interest

Sukuk: Islamic Bond

Ta'awun: Cooperation

Tabarru: Donation

Takwa: God Consciousness

Takaful: Joint Guarantee

Thawab: Reward

Tabakul-al-Qurud: Mutual Exchange of Loans

Wakalah: Agency

Waqf: Endowment

Yathrib: Former Name of Madinah

Latin

Ab Initio: From the very beginning

Causa Proxima: Proximate Cause

Corpus Juris: Body of Laws

Interesse Termini: Right of Entry

Locus Standi: Right to Institute an Action

Totidem Verbis: In So Many Words

Uberrimae Fidei: Utmost Good Faith

CHAPTER 1: INTRODUCTION

1.1 Background and Justification of Study

The Nigerian insurance industry[1] has a history of niggling endemic insurance gap brought about by the prevalence of several factors, especially the very nature and practice of conventional insurance itself in a predominantly Muslim environment.[2] The Islamic insurance (*Takaful*) Operational Guidelines introduced in March, 2013, as an alternative to conventional insurance, were meant to bridge this endemic gap by engendering deepening insurance penetration and financial inclusion of the hitherto underserved and uninsured huge Muslim clientele. However, the *Takaful* Operational Guidelines and a host of other enabling insurance instruments are caught up in a web of regulatory conflict and ambiguity.[3] The fragmentation of insurance policy-making, regulation and supervision amongst different regulating authorities encapsulated in regulatory ambiguities leaves gaps in *Takaful* application and its market development thereby creating an uneven playing field in the insurance industry. The legal effect of this is a huge regulatory vacuum that is bound to impact negatively on capital investment[4] in *Takaful*, breed mistrust and discourage active participation by the populace. This poses a serious threat to the much desired financial inclusion and deepening insurance drive of the National Insurance Commission (NAICOM), which is

[1] The Nigerian insurance industry can be divided into four groups: (a) those regulated by the National Insurance Commission (NAICOM), forming the largest group; (b) health insurance, which is regulated by the National Health Insurance Scheme (NHIS); (c) agricultural insurance, provided almost exclusively by the Nigerian Agricultural Insurance Corporation (NAIC); and the cooperative sector, which offers insurance to their members. See NAICOM's website, accessed on 6th April, 2016.

[2] Nigeria is the most populous country in Africa with approximately 186 million people. It is the 7th most populous in the world, and still growing by about 2.5% per year, according to CIA Nigeria Country Fact Book, 2017. The median age is 19.2 years and life expectancy of 52 years. Half of the population are in rural areas, most of them engaged in subsistence agriculture. Sixty-eight per cent of the population is literate, and the most widely spoken languages are English, Hausa, Yoruba, Igbo and Fulani. About 50% of the population is Muslim, 40% Christian and 10% engage in indigenous beliefs. The North and South of the country is mostly Muslim, while Christians concentrate in the East.

[3] It must be understood that there are remarkable differences between an Act and Guidelines as legal instruments. The Insurance Act, 2003 is an Act of Parliament while the 2013 *Takaful* Operational Guidelines is a delegated legislation which is meant to clarify and address the ambiguous and unresolved areas as they pertain to Islamic insurance. The Guideline is to be clear on all that is required to put *Takaful* into practice. But herein begins the peculiar problems of Islamic insurance in Nigeria. The absence of legislative mention of Islamic insurance or *Takaful* in Section 1 of the Insurance Act, 2003 is a serious and costly affront. This is bound to impact negatively on the application of *Takaful* in building confidence in the industry. The 2013 Operational Guidelines for *Takaful* Operators should have cleared the ambiguity concerning the absence of legislative mention of Islamic insurance in Section 1 of the Insurance Act, 2003. See Olayemi, A.M., *The Legality of Islamic Banking in Nigeria: A Critical Approach* at http://ssrn.com/abstract=1941010, accessed April 1, 2016. See also Garba, A., (2014), The Emergence of Islamic Banking in Nigeria: Constitutional and other Legal Issues, *Journal of International Banking Law and Regulation*, Issue no. 3, Thomson Reuters (professional), UK Limited and Contributors.

[4] Where regulations are unclear and ambiguous, this will not do well to attract foreign investments into the industry especially those from the wealthiest investors of the world who are located in the Gulf Cooperation Countries (GCC).

the chief regulator of the Nigerian insurance industry, and other stakeholders. The quest to attain expected levels and positively make significant impact on Nigeria's gross domestic product will remain a mirage if this absence of synergy between the enabling insurance regulatory instruments is allowed to fester. The harmonization of these instruments is bound to fill the legal void, establish regulatory certainty and build trust leading to the active participation of the populace and stakeholders alike in *Takaful* insurance. That is the premise this research is established on.

Historically, rudimentary form of insurance has been in existence long before the advent of English Common law in Nigeria which was occasioned by colonial conquest.[5] Age grade and tribal associations have been practicing some form of mutual assistance resembling a life insurance contract.[6] The members of the group raise funds through levies and donations from which a handsome amount will be presented to the next of kin of a deceased member on the occasion of the demise of such a member.[7]

Conventional insurance,[8] on the other hand, as explained by Lawrence, J in *Lucena v. Craufurd*, may be described as follows:

> "Insurance is a contract by which one party in consideration of a price paid to him adequate to the risk becomes security to the other that he shall not suffer loss, damage or prejudice by the happening of the perils specified to certain things which may be exposed to them."[9]

Flowing from the above, insurance by whatever name called exists in one form or another, though the form in which the contract is entered may differ, yet they all aim at

[5] Okany , M. C., (1992) *Nigerian Commercial Law*, Africana First Publishers Plc, p. 811.
[6] *Ibid.*
[7] Achike O., (1985) *Commercial Law in Nigeria*, University Press, p. 316.
[8] The concept of insurance is founded upon the law of contract. Like in any other case, therefore, all rules of contract will apply to an insurance contract. Accordingly, for example, parties to an insurance contract will have the right to determine their obligations under the contract, and the court will refrain from interfering with the rights of the parties except where the terms of such contract are manifestly unreasonable to the detriment of one of the parties or against the public interest. See Okany, M.C., *op cit.*
[9] (1806) 2 Bos. and P. N. R. 269 at p. 301.

achieving the same purpose and that is the indemnification of the insured from the peril insured against.

The Nigerian legal system recognizes three forms of insurances namely, conventional insurance, customary insurance and Islamic insurance, albeit by inference as indicated in the delineating Section 1 of the Insurance Act, 2003.

Conventional insurance has been the dominant insurance practice in Nigeria. This has been so because it is government entrenched as reflected in the various enabling laws of insurance practice in the country. Government has even gone further in making some aspects of insurance compulsory like the third party motor vehicle insurance contract. Conventional insurance is the most dominant form of insurance contract in Nigeria by virtue of lingering colonial heritage and active government patronage. It is better known as commercial insurance or insurance in exchange for fixed premium. Here, the insured is bound to pay fixed installments to the insurer. In return the insurer is responsible to compensate the insured for losses caused by events stipulated in the contract. If the stipulated events do not occur, the insured loses his right to the payments he made and they become property of the insurer.

This system of insurance has succeeded in creating an endemic gap in the Nigerian insurance industry due to low level patronage and financial exclusion of most of the populace. Most Nigerians do not understand it and abhor it because they see insurers as eager to collect premiums but are reluctant to settle genuine claims upon occurrence of peril insured against;[10] hence they do not buy into it except the compulsory third party/vehicle insurance. Religion has also been identified as a strong factor for the abhorrence of conventional insurance by Muslims because of the anti-*Shari'ah* features

[10] Most Nigerians hold insurance business with contempt. They see insurers as eager to collect premium from the insured at the beginning of the contract but unwilling to settle genuine claims when they arise. They have therefore chosen to avoid insurance except perhaps for the few insurance products that have been made compulsory. Even in the case of the compulsory insurances, many have found means of escaping the eyes of the law enforcement agents through patronizing fake insurance agents.

embedded in it. The average Nigerian suffers from lack of awareness about insurance process. He does not understand how he pays premium for an insured risk yet cannot recover his money when the event does not occur. Again many insurance companies have not been transparent in their dealings. There is a long standing mutual suspicion between the parties right from the niche days in the history of conventional insurance practice in Nigeria when many innocent insured were fleeced by rogue insurers. Scars of the enduring damage are yet still very much visible.[11]

Customary form of insurance[12] has been entrenched in cultural practices in almost all the known ethnic populations found in Nigeria since earlier known times. It is simple and rudimentary but serves the purpose very well which is to cushion the effects of devastating loss that may occur to a person or group of persons. It is a form of contribution of resources that is mutual and transparent devoid of the complexities embedded in conventional insurance practice. People come together to contribute money or produce to aid those who are in dire need. This form of contribution and assistance is a merry-go-round because no one is immune to disasters. It is to a great extent similar to *Takaful*. In spite of its attraction, this type of insurance practice is too rudimentary or banal to make any meaningful impact in the modern world of complex economic dealings.

The global economy is facing unprecedented distress and the Nigerian economy is no exception. Economies are continuously looking for ways and means to help cushion the rigors of economic difficulties thus attention is being focused on alternatives in sourcing for resources such as the huge premium deposits in Islamic insurance. Customary form

[11] Most Nigerians are wary of the concept of conventional insurance because of distrust in how businesses traditionally operate in Nigeria. Some believe insurance is a good thing, yet do not patronize it as they consider it too expensive. Culture and religion also influence attitudes towards insurance.

[12] Nigerians without access to or unable to use formal financial services use informal options for their savings and credit needs. Informal choices such as moneylenders and Asusus are dominant in rural areas, but exist in urban settings as well. Asusu is the oldest form of savings club in Nigeria. The majority operates with unwritten laws, based on oath of allegiance and mutual trust. Asusu associations contribute a fixed amount periodically and give all or part of the accumulated funds to one or more members in rotation until all members have benefited from the pool. It is estimated that 20-30% of Nigerians use Asusus and over 40% are in the rural areas. See http://www.microfinancenigeria.com/other-news/Asusu-expanding-nigeria%E2%80%99s-financial-services-frontier/.

of insurance is rudimentary and therefore, not attractive. Conventional insurance has not lived up to its billing. The most viable alternative is now Islamic insurance (*Takaful*) and other associated products. There is a significant shift in paradigm in the world economic order. Islamic finance has made remarkable inroads in world financial circles and Islamic insurance or (*Takaful*) which is a component of Islamic finance has found unprecedented acceptance in numerous economies of the world.

Takaful is the name given to the practice of insurance under the framework of Islamic finance. Technically, the concept of *Takaful* in the area of insurance means mutual assurance or guarantee amongst the members of a group between each other. It is basically the pooling of resources to assist brethren who are in need. It is also seen as a mutual agreement between two parties for a mutual cooperation in protecting one's life or property from any unprotectable and unavoidable risk, danger or tragedy.[13]

Islamic finance embodies the utilization of Islamic law by applying it to conventional financial and commercial transactions[14] including, as stated above, *Takaful*. Islamic insurance and conventional insurance are diametrically opposed to each other in both substance and form because the former operates in an atmosphere devoid of interest (*Riba*), uncertainty (*Gharar*) and gambling (*Maysir*), the latter has at the very core of its embodiment, the presence of these anti-*Shari'ah* features which are integral to the survival of its operations. However, in as much as the two are fundamentally different, they do share a common objective or goal which is the indemnification of the insured upon the happening of the peril he sought protection against. The two can and do exist side by side in spite of the differences.

The conventional insurance product as packaged today is un-Islamic in its entirety from the Muslim's perspective hence the introduction and embracing of *Takaful* which is in

[13] Ahmed, S., (2006) *Islamic Banking, Finance and Insurance.* A. S. Noordeen Publishers, Kuala Lumpur, p. 512.
[14] Bakar, M. D., and Ali, E. R. A., (eds.) (2008), *Essential Readings in Islamic Finance,* Kuala Lumpur, CERT Publications Sdn Bhd, p. 38.

tandem with *Shari'ah* rules and obligations. Muslims account for about 2 billion in the total world population and most Muslims have been reluctant in participating in conventional insurance schemes because of the usury obstacle. *Takaful* remedies that drawback.

It is an established fact that Islamic banking, finance and insurance have grown in stature and importance in the last two or more decades. This progress needs to be sustained by further exploring areas of mutual interest and cooperation between conventional and Islamic insurance practices. It is without doubt that conventional insurance and Islamic insurance can co-exist side by side as *Takaful* is not meant for Muslims only. It is a product that is meant to cushion the effects of devastating loss no matter the creed or conviction of the insured.[15]

It is worth noting that Islamic finance, banking and insurance are actually Islamized conventional finance, banking and insurance. The products are products of conventional banking, finance and insurance but "Islamized" by removing the features prohibited by *Shari'ah* and applying *Shar'iah* principles to achieve the same or similar effects. This has been the developmental pattern of Islamic finance over the decades. The expertise of conventional banking, finance and insurance experts is still very much critical to the continued development of Islamic finance.[16]

The Nigerian Muslim population is the largest in Sub-Saharan Africa,[17] and it has the potential of becoming the African power house for Islamic finance just like Malaysia is to the world.[18] The emergence of *Takaful* as a global insurance institution is something that is relatively new. The same fact also applies to the Nigerian situation. At the same time it is to be noted that Nigeria is a country that is made up of about 250 ethnic tribes

[15] Alabadan, S., *NAICOM with Guidelines for Islamic Insurance*, Daily Independent Newspaper site, 24th August, 2012.
[16] Bakar, M. D., and Ali, E. R. A., (eds.) (2008), *op cit*.
[17] *The Emerging Islamic Finance Market Outline and Challenges*, posted by Detail Solicitors, 14th Floor, 38/39 Conoil Building, Marina, Lagos, available at www.google.com, accessed on 24th August, 2012, Aliyu, S. U. R., *Islamic Banking and Finance in Nigeria: Issues, Challenges and Opportunities*, http://mpra.ub/uni-muchen.de/425573, accessed on 8th May, 2013, pp. 1-3.
[18] *Ibid.*

and languages and Muslims constitute more than 50% of the total population of 186 Million. This entails a huge market for the *Takaful* industry.

The Nigerian society thrives on mutual suspicion emanating from the fear of religious dominance.[19] The Nigerian government faced a lot of pressure and criticisms in the course of introducing Islamic banking. The introduction of *Takaful* also faced similar resistance. However, it has been shown that both *Takaful* and conventional insurance are compatible and that they share some common traits and that the whole thing is not about religious dominance. This has gone some way in alleviating those fears.[20] This much was admitted by the former Chairman of the National Insurance Commission of Nigeria (NAICOM), Mr. Fola Daniel, a Christian, prior to the introduction of *Takaful* Guidelines in 2013, when he said,

> "……..rather than allowing people to see Islamic insurance as being designed only for the Muslim population, Christians and any other person would patronize *Takaful* insurance products by the time they understand what *Takaful* is all about and that it has a prospect of returning part of their premium at the end of the year, many people will buy into it, it is not about religion, it is about a way of sharing risks."[21]

[19] The controversies generated by the approval of the non-interest banking institution among Nigerians especially the stakeholders and legal luminaries is hinged primarily on the interpretation of S.10 of the 1999 Nigerian Constitution regarding the adoption of a State religion. The section provides that: ''The Government of the Federation or a state shall not adopt any religion or state religion''. Based on this, the opponents for the establishment or promotion of Islamic finance perceive same as contravening the constitutional provisions. They have always interpreted the section as declaring Nigeria as a secular state. It is difficult to see how this assertion by the opponents of Islamic finance can hold water because of its irrationality. To them, promoting Islamic finance amounts to promoting or adopting Islam as a state religion. It is humbly submitted that this is manifestly erroneous. Nigeria is not even a secular state because secular by definition means an ideology or attitude of life that rejects spiritual values outlook. Rather, Nigeria is a pluralistic society and multi-religious state. This explains why both Federal and State governments sponsor and fund religious activities like Muslim and Christian Pilgrims Welfare Boards, establish mosques and churches in State Houses etc. They also give statutory recognition to the observance of Saturday and Sunday as work-free days in conformity with Christian and Sabbath injunctions. Friday was made half work-free day to allow for Friday congregational prayers for Muslims and public holidays are declared to mark religious festivals. With all these no state can claim to be secular. This is more particular so as there is no place in the constitution where such provision is contained. See Garba, A., (2014), *The Emergence of Islamic Banking in Nigeria: Constitutional and other Legal Issues*, J.I.B.L.R. Issue 3, Thompson Reuters (Professional) UK Limited and Contributors. See also Abdul Qadir, A.I., (2003), Constitutional Impediments to the Total Enthronement of *Shariah* in Nigeria, in Oseni, Z.I., (ed), *A Digest of Islamic Law and Jurisprudence in Nigeria* (Auchi: Dar Al Nur), p. 169.

[20] Alabadan, S., *op cit.*

[21] *Ibid.*

The Nigerian insurance industry is facing a myriad of problems, chief among which is low level patronage and lack of insurance deepening which has resulted in financial exclusion of the majority of the populace.[22] The problems are endemic and defy solutions. *Takaful* then appears to be the panacea[23] if properly implemented with the help of adequate legislative backing[24]. In an effort to make *Takaful* take its rightful place, the National Insurance Commission of Nigeria (NAICOM) introduced *Takaful* Insurance Operational Guidelines effective March 2013, to pave the way for the full implementation of *Takaful* insurance. With this introduction, comes a plethora of challenges that have naturally ensued. This thesis is premised on the examination of these challenges in the *Takaful* legal framework and other insurance enabling instruments.

The crowning effort of this research is a case being made for the enactment of a wholesome *Takaful* legislation in the form of an Act by the National Assembly that will harmonize all the discrepancies in the various enabling insurance instruments in order to engrain and safeguard the effective application of *Takaful* insurance in Nigeria. The introduction of the Operational Guidelines on *Takaful*[25] is without doubt a promising development but an enactment by the National Assembly will further consolidate all the gains made in attempting to bridge the endemic gap existing in the Nigerian insurance industry that was brought about by the shortcomings of conventional insurance practice.

[22] Financial exclusion is high and the gap between rural and urban adults is wide. Around 30% of total adults have an account at a formal financial institution (banks and others). According to the World Bank, 52% of the adult population is completely financially excluded. Intermediation is highly skewed toward the public sector and while 59% of urban adults have an account at formal institutions, only 23% have one in the rural areas. Eighty-sic per cent of the unbanked population are rural dwellers. According to Cenfri 2014 Opportunities for insurance inclusion in Nigeria, ''Informal associations seem to be effective and trusted: nearly a quarter of those who save belong to an informal/savings club, while 13% indicated they save with a village association. Furthermore, 45% of savers save at home''. See the World Bank (Financial Inclusion Global Index, 2014 survey).

[23] Alabadan, S., *op cit.*

[24] These are some of the views expressed by a Deputy Director in NAICOM, Barrister Ahmed Ibrahim Adamu when interviwed by the researcher in NAICOM Headquarters, Abuja. Please refer to Appendix 1.1 for complete set of interview questions asked. These comments are in complete alignment with the objectives of this study.

[25] *Takaful* Operational Guidelines 2013 issued for *Takaful* Operators by the national Insurance Commission of Nigeria (NAICOM).

The Malaysian *Takaful* Act of 1984 which has been repealed and replaced by Islamic Financial Services Act, 2013, is an example of such an enactment.[26]

Based on the reasons adduced above, it is safe to conclude that the harmonization of the existing enabling insurance legislations to expressly include *Takaful* will enhance regulatory clarity and consolidate the dual system of insurance operating side by side in Nigeria as is the practice in the banking industry. In the same vein, conventional insurance companies should be encouraged to have a counter in their existing operations which offers *Takaful* insurance. Under the dual system of insurance, not only do the two systems work in parallel, they also utilize essentially the same infrastructure. This, undoubtedly, will have significant implications in terms of cost and speed in the effective application of Islamic insurance in Nigeria.[27]

This research seeks to solve a monumental problem that has been plaguing the Nigerian insurance industry namely: the persistent endemic gap in the industry brought about by lack of deepening insurance penetration, lack of standardization of Nigerian insurance legislations and the chronic suspicion among the populace of conventional insurance practices as a result of lack of transparency and non-payment of proven claims by insurers, among others.

The research examines the challenges of conventional insurance operations from the Islamic perspective and the development and challenges in the application of *Takaful* as an alternative. The thesis specifically investigates the statutory and regulatory insurance frameworks contained in the Insurance Act, 2003 amongst others and the newly released *Takaful* Operational Guidelines with a view to harmonizing and standardizing the inherent regulatory discrepancies. A good regulatory environment is critical to building trust and confidence in any undertaking. Therefore, the imperative of having

[26] The Central Bank of Malaysia which is the chief regulator of all financial institutions in Malaysia has repealed both the Banking Act, 1983 and *Takaful* Act, 1984 and replaced them with a consolidated Act known as Islamic Financial Services Act (IFSA), 2013.
[27] Bakar, M. D., and Ali, E. R. A., (eds.), *op cit*, Foreword.

the treasures of *Takaful* permanently engrained legislatively cannot be overemphasized. For the Muslim, the issues of interest, uncertainty, speculation and gambling which are central to the operations of conventional insurance are unattractive and have largely contributed to the avoidance of insurance, thus the resultant financial exclusion. To those who may not be Muslims, the equity factor in which premium is returned at the end of the transaction, is not only attractive but a fair business deal.

1.2 STATEMENT OF THE PROBLEM/HYPOTHESIS

Despite its immense potential in contributing to Nigeria's economy[28] through deepening insurance penetration and financial inclusion of the majority of the underserved Nigerians, the introduction of Islamic insurance (*Takaful*) is facing some significant and peculiar regulatory challenges especially in a multi-religious society such as Nigeria. The challenges for the successful implementation and sustenance of Islamic insurance are based on the following:

a. The challenges of legislative enactment.

b. The challenges of the enabling regulatory instruments.

c. The issue of regulators powers and circumscriptions.

d. Fragmentation of policy making and laws.

For the Muslim, conventional insurance system as practiced in Nigeria and elsewhere in the world is against the teachings of Islamic principles because of its association with interest (*Riba*) and uncertainty (*Gharar*).[29] This has had serious negative effects on the

[28] The importance of economic growth and development cannot be overstated. Income growth is essential for achieving economic, social and even political development. Countries that grow strongly and for sustained periods of time are able to reduce their poverty levels significantly, strengthen democratic and political stability, improve the quality of their natural environment and even diminish the incidence of crime and violence. See also Barro, R.G., (1996), Democracy and Growth, *Journal of Economic Growth*, 1(1), pp. 1-27. See also Easterly, W., (1999), Life During Growth, *Journal of Economic Growth*, 4(3), pp. 239-276. Also Dollar, D. & Kraay, (20020, Growth is Good for the Poor, *Journal of Economic Growth*, 7(3), pp. 195-225.

[29] Mallam Ali Goni, a devout Muslim from Maiduguri, Borno State was interviewed by this researcher where he stated that he and his people will never patronize conventional insurance because it is completely haram (prohibited by Shari'ah. As an ordinary citizen, it was a surprise how he categorically castigated conventional insurance practice. He said he would rather be struck by

industry as it has contributed in no small measure to low level patronage and financial exclusion. Considering the huge Muslim population in Nigeria, *Takaful* was introduced in Nigeria in March 2013 to cater for the needs of both Muslim and non-Muslim members of the society[30]. While it has been observed that, some insurance companies in Nigeria currently provide Islamic insurance product as a window, the fact remains that, the foremost Nigerian legislation on insurance activities which is the Insurance Act of 2003 has not explicitly made provisions for the operation of *Takaful* business and until recently there was no regulatory framework for the operation of *Takaful*. This may constitute serious challenge to the application of Islamic finance products generally, and in particular Islamic insurance (*Takaful*) because its application is by inference.

Furthermore, a case for a legislative enactment becomes all the more imperative because of the inherent challenges and discrepancies embedded in the enabling insurance instruments in Nigeria. This may be the reason why the alternative insurance system has not yet become popular even though, it has been in practice for about three decades. Nigerians are yet to enjoy its bountiful gains despite remarkable development and progress in that area across the world.

1.2.1 Hypothesis

A legislative enactment[31] to harmonize the discrepancies in the enabling insurance instruments on *Takaful* in Nigeria will boost regulatory certainty and trust thus

adversity than to partake in such insurance scheme. However, it was disappointing to note that he was totally ignorant of *Takaful*.He believes anything insurance is haram and a Muslim should not go near it. See Appendix 1.4 for interview structure.

[30] For Nigeria, the motive for effective application of *Takaful* and how it can contribute to the goal of economic growth and development of Nigeria and Nigerians is borne out of several factors; some of which are (1) the pervasive poverty trend that abounds in the Nigerian populace; (2) stack lack of awareness of the workings of insurance among most of the elite class; (3) image deficit of most conventional insurers; (4) growing awareness of Islamic alternative among the Muslim populace who constitute the majority in the country; and (5) the ethical contents of the Islamic alternative. The above stated factors no doubt can attract substantial funds hitherto, left dormant in the informal sector, thereby stimulating insurance and economic activities. See Yusuf, T.O., (2014), Prospects of *Takaful*'s Contributions to the Nigerian Economy, Journal of p. 218.

[31] Nigerian legislation consists of statutes and subsidiary legislation. Statutes are laws enacted by the legislature – the legislative arm of government. Subsidiary legislation is law enacted in the exercise of powers given by a statute just like the Insurance Act, 2003 and the subsidiary legislation on *Takaful* Guidelines, 2013 by NAICOM, which is the chief insurance regulator in Nigeria. Subsidiary legislation is also known as subsidiary instrument or delegated legislation. It consists of rules, orders, regulations, bye-laws and other instruments made under the authority of statutes. A statute is usually referred to as the principal law in a later statute amending it. A statute under which subsidiary legislation is made is referred to as an enabling statute. Legislation is the most important instrument of legal development. It has a tremendous effect on all the other sources of law. It can readily alter their

engendering deepening insurance penetration and financial inclusion of Muslims and non-Muslims alike.

1.3 AIM/OBJECTIVES OF THE STUDY

The major aim of this research is to examine the challenges that are inherent in the application of *Takaful* insurance within the practice of conventional insurance in Nigeria with a view to harmonizing the discrepancies in the various enabling insurance instruments through a legislative enactment.

1.3.1 Objectives of the Study

1. To establish a theoretical foundation and framework for this research through an inclusive literature study.
2. To investigate the factors responsible for the stunted development in the application of conventional insurance in Nigeria.
3. To examine the perception of the Nigerian populace particularly the Muslim population towards conventional insurance practice.
4. To gauge the attitude of the Nigerian populace towards the legal application of *Takaful* insurance in Nigeria.
5. To identify the key challenges likely to impede the development and legal application of *Takaful* insurance in Nigeria.
6. To examine the prospects and challenges of a legislative enactment on *Takaful* insurance in Nigeria.

content. It is also a useful tool for the social, economic and technological development of the country. See Obilade, A.O., (2007), *The Nigerian Legal System*, Spectrum Books Ltd, Ibadan, Nigeria, p. 64.

1.3.2 Objectives that Influenced the Research

(a) The Nigerian population is made up of 70% Muslims who are reluctant to patronize conventional insurance products because of the anti-*Shari'ah* features that are central to its operations.[32] Once *Takaful* is efficiently and effectively implemented to the satisfaction of Muslims and non-Muslims alike, the level of insurance penetration would be very much enhanced. There is a vast untapped clientele for the *Takaful* Insurance industry waiting to be harnessed.

(b) The global financial market is in turmoil and the capitalist West is shifting its attention to Islamic financial models for solutions. This research is a contribution towards pinpointing the pervading challenges of conventional insurance in Nigeria and highlighting the treasures of Islamic insurance (*Takaful*) as a panacea with a view to easing the rigors of economic constraints currently being experienced[33].

(c) The Nigerian insurance industry has been in dire straits due to lack of direction. The regulatory bodies are at a loss as to what to do about the lack of patronage. In a country of over 186 million people[34], it is appalling that only about 800,000[35] individuals bought into insurance. The quest to attain deep levels of insurance penetration by the regulatory bodies and impact significantly on Nigeria's economy and gross domestic product still remains a mirage because of endemic problems like lack of awareness, mistrust and the activities of fake insurance institutions. Furthermore, the less than optimal financial literacy in Nigeria today is at the roots of apathy and disinterest in financial services and

[32] This position was amply reflected in all interviews conducted by the researcher with some respondents that include lawyers, NAICOM officials, law lecturers, insurance and *Takaful* operators. All of the respondents were unanimous in their views that that the problems of the Nigerian insurance industry have to do with religion. See Appendices at the end of the thesis.

[33] As the second largest economy in Africa, Nigeria aspires to be an important player in the international context. This aspiration is reflected in nearly all the government's policy documents, most notably the Vision 2020 package. Nigeria is rich in natural resources, particularly natural gas, petroleum, tin, and iron. Its economy is primarily based on exports of oil and gas, which provides 80% of budgetary revenues and 40% of the GDP. However, the majority (over 70% of the workforce is employed in the agricultural sector (See African Economic Outlook, 2014). The key drivers in the non-oil sector, in terms of growth, are telecommunications, commerce, manufacturing, agriculture and services. The growth of the telecommunications sector is particularly impressive, having averaged over 30% annually lately, with an increase of over 200% in the stock of Foreign Direct Investment (FDI) between 2005 and 2013. See Dias, D. et al, (2013), Access to Insurance Initiative, *Towards Inclusive Insurance in Nigeria: An Analysis of the Market and Regulations*, Eschborn, p. 14.

[34] See CIA World Fact Book Nigeria, 2017.

[35] NAICOM/Access to Insurance Initiative Report, *Towards inclusive Insurance in Nigeria*, Eschborn, 2013, p. 27.

insurance unwittingly bears the heaviest brunt in that sector. Now that the Operational Guidelines for *Takaful* have been issued by NAICOM[36], the endemic gap looks to be filled. However, a lacuna still exists in the absence of an Act of National Assembly to harmonize all the regulatory discrepancies in the enabling insurance instruments and have *Takaful* insurance engrained. This research hopes to come up with an inquisition into the challenges of the regulatory framework and to make a case for legislative safeguard.

(e) This research aims to contribute to existing knowledge by being an important reference for all those interested in *Takaful* business, teachers, researchers, students, policy and lawmakers etc.

1.4 RESEARCH QUESTIONS

This study is designed to espouse the general and regulatory challenges in the application of *Takaful* within conventional insurance practice in Nigeria.

Thus the research questions the study intends to address are as follows:

i) What are the key factors likely to impede the legal application and development of *Takaful* insurance within conventional insurance framework in Nigeria?

There are substantial degrees of statutory and regulatory ambiguities in the enabling insurance instruments that make the application of *Takaful* fraught with challenges.

ii) Would the harmonization of the enabling insurance instruments provide some regulatory clarity and what effects (if any) could such an enactment have on *Takaful* application and development in Nigeria?

[36] The National Insurance Commission (NAICOM) issued the Guidelines for *Takaful* insurance pursuant to Section 7 of the NAICOM Act, 1997.

iii) What are the factors responsible for the stunted development of the Nigerian insurance industry?

iv) What is the perception of the Nigerian populace especially the Muslim population towards conventional insurance practice?[37]

1.5 SIGNIFICANCE OF THE STUDY

It is submitted that this thesis serves an important purpose because to the best of the author's knowledge, there has been no single comprehensive study on the statutory and regulatory challenges in the application of *Takaful* under conventional insurance practice and the effects of synergizing the conflicting enabling laws. This study is unique because the *Takaful* Operational Guidelines were just released in 2013 and not much study has been undertaken on the regulatory aspects of *Takaful* within conventional insurance application. There is general recognition that positive outcome could ensue from a legislative enactment that has *Takaful* regulation clarified and engrained whereby deepening insurance penetration and financial inclusion is achieved. This is a reflection of the hypothesis.

This study is of paramount significance because of the impact insurance has in contributing to the gross domestic product of Nigeria's economy.[38] Nigeria is missing out on this massive contribution to its economy because there are only about 800,000 policy holders in a population of 150 million. The quest of this study is to unravel the

[37] The Nigerian Muslim population is highly enlightened about basic *Shari'ah* tenets embedded in Islam and as such would not hesitate to avoid anything that glaringly contravenes religious rules. Prohibitive acts like eating pork, drinking alcohol, fornication, taking interest on loans and other transactions, and all other major disallowed acts are shunned with impunity. That is why the issue of interest in conventional banking and conventional insurance became stumbling blocks in the growth of the financial industry. Most Muslims who managed to take their savings to the banks expressly instructed the banks not to add interest rates to their capital. The situation is not the same as is found under conventional insurance and that is one of the major reasons why the industry stagnated due to lack of patronage.

[38] The importance of the insurance growth nexus is growing due to the increasing share of the insurance sector in the aggregate financial sector in almost every developing and developed country. Insurance companies, together with mutual pension and funds, are one of the biggest institutional investors into stock, bonds and real estate markets and their possible impact on the economic development will rather grow than decline due to issues such as ageing societies, widening economic disparity and globalization. This trend is likely to be accelerated with the new foray of Islamic insurance into the new economic space by essentially targeting a sizeable mass of low-income earners. This is the opportunity *Takaful* must seize in order to make a difference in the Nigerian insurance landscape. The growing links between the insurance and other financial sectors also emphasize the possible role of insurance companies in economic growth. See Yusuf, T.O., (2012), Prospects of *Takaful*'s (Islamic insurance) Contributions to the Nigerian Economy, *Journal of Finance and Investment Analysis,* vol. 1 no. 3, Science Press Ltd, p. 221.

mystery behind this dismal patronage in order to chart the way forward. The Nigerian insurance industry has suffered adverse effects due to lack of understanding and patronage of conventional insurance practices. Not enough trust has been created in the insurance business due to non-settling of claims and most Nigerians are not used to paying premiums to alleviate the risks. There is a near total absence of deepening penetration and awareness. This, in turn, has greatly affected the economy because the turnover from the insurance industry is nothing to write home about. In an ever changing and fast growing economic terrain, insurance plays a cardinal role in underwriting the risks associated with rapid economic growth and development which if not adequately covered could facilitate the collapse of an economy.[39] The study proposes the specific option of *Takaful* to help stem this unsavoury situation. With adequate legislative enactment, the development and application of Islamic insurance (*Takaful*) within conventional insurance will be engrained and will positively aid the growth and diversification of the Nigerian economy.

The provision of the most needed insurance cover for all categories of people through its various models of conceptual and operational techniques makes *Takaful* a front runner. It needs to be reiterated that this type of insurance policy is open to both Muslims and non-Muslims alike.

Furthermore, the development of Islamic insurance has evolved into a rapidly growing industry. *Takaful* has therefore assumed a strategic position in the financial sector of many countries, Nigeria inclusive, and serves as a key component of Islamic finance considering its potential in mobilising funds for investment in a pattern similar to that of

[39] ''Researchers have often been concerned about the role of insurance in economic development. This accounts for why considerable attention has been devoted to evaluating the relationship between economic growth and financial market deepening. Most of what we have had relate to banking systems and securities markets – with insurance receiving only a passing mention. Yet, while insurance, banking and securities markets are closely related; insurance fulfils somewhat different economic functions than do other financial services, and in turn requires particular conditions to flourish and to make full economic contributions. The insurance sector worldwide remains the only industry that exists to ensure the continuity of other sectors by restoring individuals and corporate bodies to their former positions each time they suffer losses through claims settlement''. – per Bates, I. & Atkins, D., (2008), *Insurance*, Global Professional Publishing, London, p. 8.
See also Outreville, J.F., (1997), Theory and Practice of Insurance, Massachusetts, USA, Kluwer Academic Publishers, p. 26.

conventional insurance, hence the need for adequate legislative backing to safeguard its huge potential.

Most significantly, the thesis explores the challenges and impact of the recently released *Takaful* Operational Guidelines issued by the regulator to the insurance industry, a position that has not been considered and researched previously.

1.6 SCOPE AND LIMITATIONS OF THE STUDY

The study is limited in scope to the application of *Takaful* under conventional insurance in Nigeria and the inherent statutory and regulatory discrepancies that abound in the enabling insurance instruments. The Operational Guidelines issued by NAICOM[40] and other enabling insurance instruments are critical to the scope and limitations of the study. Most importantly, the thesis dwells on the general and regulatory challenges in the application of *Takaful* within conventional insurance in Nigeria with a push for legislative enactment to harmonize the regulatory discrepancies.[41]

However, to be able to do that, a descriptive developmental analysis of the history of conventional insurance and *Takaful* will be made for purposes of establishing a nexus between our past experiences and the present and future projections of insurance dealings.

The study will also draw from the experiences of the number one *Takaful* nation in the world (Malaysia)[42] and from other notable jurisdictions in overcoming general and regulatory challenges in the application of *Takaful*.

[40] *Takaful* Guidelines for *Takaful* Operators 2013 issued by NAICOM.

[41] *Takaful* in Nigeria is relatively a new area of academic interest. While a number of international texts, journals and writings on *Takaful* are available, none have been considered with specific emphasis on the Nigerian regulatory challenges. This is a unique set of circumstances. To the best of this writer's knowledge and at the time of publication there is no dedicated Nigerian legal text written on this area of interest (although a number of articles have been written peripherally on the area of study. This explains some of the limitations encountered.

[42] Malaysia has a new *Takaful* legislation effectively repealing the Malaysian *Takaful* Act of 1984. The new Act, released by the Central Bank of Malaysia which is the chief regulatory body just like NAICOM in Nigeria, has now been bundled together with the Banking and Financial Institutions Act and is collectively referred to as Islamic Financial Services Act, 2013. The provisions containing *Takaful* are more or less the same with the repealed *Takaful* Act, 1984.

1.7 RESEARCH METHODOLOGY

The methodology of study or research design shall be both doctrinal and qualitative methodologies employing non-random sampling technique. There will be extensive use of both primary and secondary sources of information and interviews where appropriate, consulting textbooks, journals, periodicals, newspapers and magazines, world wide web, unpublished articles, theses, seminar papers etc.[43] Quantitative instead of qualitative methodology could have been used but this would not achieve the desired results because statistics is not of essence to this particular research. If the study employs statistical evaluation methodology, there is apprehension that that the conclusion, although arithmetically precise, may fail to describe or capture the reality of the research.

1.7.1 Explanation of Methodology Used in Study

The research work invariably has to have recourse to library research which will involve consulting textbooks connected to the research topic, examining and analyzing them with a view to either agreeing or disagreeing with their contents or making constructive remarks on the opinions of the authors.

Historical documentaries will be invaluable materials to this research as events chronicling the emergence of Islamic Finance in the global stage will be referred to.

Interface interviews[44] where appropriate will be conducted. The sample size selection of respondents will be purposive and this will include law makers, professional employees of insurance companies, insurance brokers, religious clerics, law teachers and the ordinary citizens. Since the respondents have a heterogeneous background, the sample

[43] The main sources of materials were local and international texts. The sources were derived mostly from the holdings of the Faculty of Law library of the University of Malaya, the main library of the university, the Faculty library of the University of Maiduguri, Borno State, Nigeria and the National Archives in Abuja, Nigeria, where necessary materials were not available from Malaysian and Nigerian libraries and the internet. The writer sourced and bought some materials from overseas publishers.

[44] Dikko, M., (2016). Establishing Construct Validity and Reliability: Pilot Testing of a Qualitative Interview for Research in *Takaful* (Islamic Insurance)''. *The Qualitative Report* 21.3 (2016): 521-528.

size will be 5 respondents drawn across geo-political zones of Nigeria. Their ages, levels of education or literacy, occupation, marital status and gender bias will be important determinants towards eliciting the desired response.

Data collection process is divided into two stages. The first stage will involve recourse being had to library materials, statutory legislation, case laws, textbooks, newspapers, journals, articles, theses, web pages and other relevant data based materials. The second stage which is the qualitative methodology[45] part will be conducted through interviews. The qualitative methodology data collection procedure is going to be through structured and semi-structured interviews in order to accommodate the different educational and socio-cultural backgrounds of the respondents. The research will equally employ both the intercept method of interviewing respondents as well as the door to door format where expedient. The medium of reading interview questions to the selected respondents will greatly ease the difficulties of the less educated ones. Cooperation is highly envisaged here because of the interface interaction. Radio recordings of interviews will also be employed where it is deemed necessary in addition to telephone interviews. The collection of data will invariably be in the form of words and narrations. All information collected will subsequently be transcribed and analyzed to lend credence to the research.

Whatever data collated will be evaluated and analyzed with a view to arriving at logical conclusions.

[45] Although this thesis is premised on theoretical hypothesis that is at present largely academic, the idea of a qualitative mix in the form of interviews was considered a very good option for adding empirical value to this very important study. Nonetheless, frustrations were encountered by the researcher due to ignorance and suspicion. However, the greater percentage of the interviews conducted were highly successful and enriching.

1.8 LITERATURE REVIEW

On literature review, the researcher acknowledges with gratitude the labour of those who have written and researched books, articles, comments and reports on conventional insurance and *Takaful* issues that have opened the way for further research into this particular and unique aspect of *Takaful* law in Nigeria.

There are no comprehensive books available on the specific regulatory challenges of *Takaful* and conventional insurance in Nigeria. The researcher has not come across a single article or commentary on the regulatory conflicts replete in the newly introduced *Takaful* Guidelines. There are very limited number of texts and materials written on Nigerian *Takaful* practice specifically. On the contrary, conventional insurance literature is blessed with so much texts, articles, commentaries and reports.

A great number of textbooks on *Takaful* and conventional insurance were referred to in the course of the study but none specifically on the challenges of the statutory and regulatory insurance frameworks in Nigeria. This makes this research unique and a pacesetter in this area. There is a serious dearth of academic writing or critical analysis of *Takaful* regulations in Nigeria. International journals written generally on this idea were available. However, no extensive writings have been made from the local or national perspective.

Literature review entails a critical assessment of relevant works that have been done in the area of inquiry to indicate their strengths and weaknesses.[46] This affords the researcher the opportunity of knowing what areas have been covered and what gaps are left uncovered which the researcher intends to cover.[47]

[46] Taiwo, A.,(2011) *Basic Concepts in Legal Research Methodology, A Practical Guide on Writing Excellent Master and Doctoral Thesis.* (St. Paul's Publishing House Ibadan) P 36

[47] Ahmed, A. B., (2010) *Techniques of Writing a Research Proposal in Law*, in Ahmed A. B., (ed) *Issues in Research Methodology in Law*, Ahmadu Bello University Press, Zaria, p. 21.

Islamic insurance (*Takaful*) is an adjunct of conventional insurance practice hence the appropriateness of commencing the review of literature from the precincts of conventional insurance.

Despite the high level of unawareness of insurance policies in the Nigerian society, a few Nigerian authors have, however, helped in publishing some very useful literature on Insurance law. Notable writers include J. O. Irukwu on *Insurance Law and Practice in Nigeria*; Olusegun Yerokun on *Insurance Law in Nigeria* and Funmi Adeyemi on *Nigerian Insurance Law*.

Olusegun Yerokun,[48] talked about insurance contracts generally and states that insurance contracts are administered within the ambit of the general law of contract. The Nigerian insurance industry is bedecked with so many challenges that have resulted in its stunted growth. Examples include the issue of utmost good faith which should be applicable to both parties. Sadly, though, the author did not dwell on such major drawbacks as practiced in Nigeria. He instead chose to place the burden of utmost good faith on the shoulders of the insured alone. Several other negative practices are simply just brushed aside. He laid so much emphasis on the basic laws of insurance without recourse being had to critical issues plaguing the practical application of those insurance principles.

Most Nigerian authors who wrote on the laws of insurance are no different from the approach taken by Yerokun in discussing basic insurance principles.

[48]Olusegun Y., (1992) *Insurance Law in Nigeria* (3rd Ed) (Nigeria Revenue Projects Publisher, Lagos).
The writer posits that there is a serious dearth of academic writing or critical analyses of regulations on insurance in general and *Takaful* in particular. The issue of *Takaful* is understandable since it has just been introduced to the insurance industry. However, what remains particularly disturbing is the nonchalance of Nigerian writers on regulatory insurance practice which is partly responsible for crippling the industry. A good example is the issue of enforcement under the Insurance Act. The laws are good on paper but applying them practically is a problem because of the circumscription of the powers of the regulator, NAICOM. These things are hardly mentioned in textbooks. There fines and jail terms in the provisions of the Act for violators but NAICOM has no power of arrest and as such enforcement process is compromised. These are proactive issues that need tackling by erudite Nigerian scholars.

Irukwu,[49] concentrates mainly on the basic doctrines of insurance law as administered in Nigeria. The striking thing about his work which predated the Insurance Act 2003 is that the principles he discusses remain in conformity with the requirements of the Act. However, for purposes of this research, a lot of shortcomings plaguing the Nigerian insurance industry remain largely ignored. Even at case law level, not much was done by Irukwu and his colleagues in bringing to the fore the maladies of the industry and why it has simply refused to grow. On fairness of insurance contract, he states that the knowledge as regards the nature of the risk proposed for insurance is almost always exclusively possessed by one side. In order to make insurance contracts fair to all parties, the law has elevated insurance contracts to the status of contracts *uberrimae fidei* but this can hardly be true of such position because one of the main drawbacks of conventional insurance is the lack of level playing field. The insured is almost always at a disadvantage. This makes conventional insurance policies unattractive.

Funmi Adeyemi[50] also discusses the fundamental principles of insurance but then fails like her colleagues in addressing issues dogging the industry. One striking feature of Funmi's position which is in tandem with *Takaful* stance is that insurable interest must be an interest that can be enforced or secured by legal procedure. The interest must be apparent and subsisting. The expectation of an interest that is hoped to be acquired in the future, however probable, cannot be insured. In other words the proposed can only take out a policy in respect of a risk which is capable of being determined. This is in agreement with principles of *Takaful*.

On the latitude of insurance company's recovery under the doctrine of subrogation, Funmi said that if the loss incurred by the insured exceeds the proceed of insurance, the client can claim the indemnity in addition to reimbursement from other sources up to

[49]Irukwu J. O., (1991) *Insurance Law and Practice in Nigeria.* (Heinemann, Ibadan)
[50] Funmi, A., (1992) *Nigerian Insurance Law* (Dalson Publications Limited)

the maximum allowable for his loss.[51] An insurer is not allowed to profit through subrogation by recovering more than the amount of claim paid to the insured.[52]

There are also foreign authors whose works are peripherally analysed.

Chai[53] writes on general insurance law as applicable to Singapore and Malaysia. He also incorporated decisions pronounced in UK as well as the relevant statutory provisions that are applicable. On the nature of insurance contracts, Chai says an insurance policy is basically a contract established between insured and insurer and many of the rules governing contracts in general are also applicable to an insurance contract. He further opines that one basic feature governing an insurance contract is that the contract exists in reference to the occurrence of an uncertain event specified in the contract.

Chai in a different work[54] says insurance plays an important role both in commerce as well as our modern way of life. The need for insurance coverage has permeated deeply into every sector of our economy. The average layman is familiar with the fact that he is not entitled to ply his vehicle on a road unless he is adequately insured against third party risks. Motor insurance coverage against third party risks is compulsory by law for anyone who uses a motor vehicle on a road. Similarly, an employer is also under a statutory duty to insure against his liability for workmen's compensation claims. Trade, indeed, will come to a standstill if it is not possible to insure against the risks of doing business. Recent events have shown that an airline with not be able to operate if it is unable to obtain cover against the risks of terrorism. He also falls short in discussing the major drawbacks of conventional insurance.

In spite of the critical role that insurance plays in our modern economy, an insurance cover is essentially a contract and is only useful to an insured if it is enforceable. There

[51] Funmi, A., (1992) *Nigerian Insurance Law* (Dalson Publications Limited) at p.250
[52] *Yorkshire Insurance Co. v. Nisbet Shipping Co*. (1961) All ER 408, as cited by Funmi, *Ibid*, at p.202
[53] Chai, P. C., (2009) *General Insurance Law,* Utopia Press Pte Ltd.
[54] Chai, P. C., (2005) *Principles of Insurance Law,* Lexis Nexis, Utopia Press Pte Ltd.

are many factors which determine whether a contract of insurance is enforceable. Most contracts of insurance are subject to the statutory requirements that a person taking out an insurance policy must be interested in the risk insured.

The crux of this discourse is a legal examination in the area of Islamic insurance within the conventional laws that regulate the operations of Nigerian insurance industry. The topic of the research appears *nouveau,* in the sense that, it may be doubtful if any comprehensive research work of this nature has been done after the release of various guidelines by the regulators. Thus, there may not be much to review in respect of the new Nigerian regulatory regime. However, there are lots of literature in respect of other jurisdictions which, indeed, shall enrich the research. It is pertinent to look into these literature and legal opinions and put them on the review scale to see whether or not they lay any foundation for the purpose of this research.

Billah,[55] states that the basic aim of *Takaful* application is to spread the risk among the members of a group or a community. In an applied sense, *Takaful* can be envisaged as a scheme of mutual protection among participants against peril or damage that may be visited upon any one of them. The participants pledge to mutually cooperate that should any of them be afflicted by misfortune, he is entitled to the indemnity of a certain amount of money to cushion the effects of the catastrophe. The objective of Islam is the establishment of a pacific community through brotherhood. Pacificity in the community can be guaranteed only when there is safeguard against 'risk' (subsistence) for members partaking in the scheme. Where this safeguard is absent, the society will be awash with worries and anxieties.[56]

[55] Billah, M., (2003) *Islamic and Modern Insurance Principles and Practices,* Kuala Lumpur, Malaysia, Ilmiah Publishers.
[56] *Ibid.*

According to Rahman,[57] insurance warranty is likened to Keynesian prophylactic motive of claim for money. The continued subsistence of such a pledge is only realisable when equity, justice and economic balance prevail in the society. Capitalism and conventional insurance are at variance with this postulation. Islam encourages that we should have recourse to mutual guarantee and co-operative insurance to solve our problems instead of resorting to the quick-fix measures and grabbing the first thing that comes across our way as escape route. The writer fails to discuss the main challenges inherent in this guarantee scheme and how these challenges are inimical to the continued development and expansion of *Takaful.*

In pre-Islamic period, the Arabs practiced different kinds of insurance schemes. Taylor,[58] writes that in the first constitution in Medina of 622 BC, there were codified allusions to social insurance schemes which were hinged upon practices such as *al-Diyah* and *al-Aqilah* (wergild or blood-money to ransom an accused tribesman who innocently killed a man), *Fidyah* (indemnity of war prisoners) and cooperative arrangements in aid of the disadvantaged, sick and indigent. Still, Islamic thinkers fail to agree about the permissibility of insurance. There is a prevalence of different kinds of insurance products in the Muslim world that are known by different names. This smacks of disunity. Moreover, different schools of thought have construed them with different appellations and different functions. However, Muslim jurists concur that the basis of pooled obligation in the scheme of *al-Aqilah* as practiced between Muslims of Mecca and Medina laid the underpinning of Islamic insurance or *Takaful*.[59]

Manjoo,[60] states that *Takaful* emanated from the *Aqilah* and *Diyah* systems whereby, members of a particular community would come to the fiscal rescue of one of their tribesmen should he be faced with an unexpected liability such as indemnity for blood

[57] Rahman, I., (1979) *Islamic Interest-free Banking*, IMF Staff Papers, March 27, 1979, p. 217
[58] Taylor, (2000) *Some Theoretical Aspects of an Islamic Takaful System,* Paper presented at a Conference on Islamic Banking, Sponsored by the Central of the Islamic Republic of Iran, Tehran.
[59] *Ibid.*
[60] Manjoo, (2007) *Islam and Financial Intermediation*, Documented Papers in Malaysia, March 29, (1): 108 - 42

money (*Diyah).* The practice of insurance originated from the ancient pre-Islamic Arab tribes in the form of *Al-Aqilah,* which was endorsed by the Prophet (SAW) in his life time.

The Noble Qur'an contains five hundred verses that specifically deal with legal sanctions.[61] A number of Divine injunctions in the Noble Qur'an do categorically justify the validity of Islamic insurance contract. Islamic insurance contracts contain elements of joint co-operation as provided for by the Noble Quran in the following; ''Help one another in furthering virtue and God consciousness (*Taqwa*), and do not help one another in furthering evil and enmity'' (Q5:V2).

Sheikh Abu Zahra, an erudite jurist of 20th century has reflected upon the subject of Islamic insurance in detail and established that a cooperative and shared insurance arrangement is in principle valid and that non-cooperative insurance is objectionable because of the presence of gambling, lure and usury that nullify the contract.[62] The *Fiqh* Council of the Organization of Islamic Countries (OIC) sanctioned *Takaful* system based on joint collaboration as substitute to the conventional insurance practice in 1985.[63]

Throughout the history of Islamic law, there have been disagreements among the scholars as to whether the conventional insurance contract is prohibited or not. The centre of the disagreements is mainly on two grounds, that is, whether it pertains to the kind of contracts involving *Gharar*, or it involves *Ribah*. Generally, these views can be classified into three groups namely; those who view the contract as prohibited; those

[61] See Al Hidayah, (1965), Cairo, v.3, p. 281. See also Jaziri, (1938), Kitabal Fiqh 'ala al Madhahib al Arba'ah, Cairo, v.2, p. 349.
[62] Ali, K., (2004) *Islamic Insurance: A Modern Approach to Islamic Banking,* London: Routledge Curzon, Taylor and Francis Group.
[63] Islamic *Fiqh* Academy Report (1985), Resolution 9, Jeddah/KSA.

who view it as permitted; and those who express the view that some types of contracts are permitted while some are prohibited.[64]

The first group mainly consists of the traditional scholars of Islamic law, among who are distinguished contemporary scholars like Musleh-ud-Din who also holds the same view.[65] The second view came about as early as late 19th and early 20th centuries. Among them are Siddiqi[66] who argues that the contemporary insurance business is founded on *Shari'ah*'s valid concept and is distinct from *Maysir* and *Gharar*. The involvement of interest in it also is not inherent to its concept. The last view contends that not all insurance contracts can be said to be prohibited. Some of these contracts are permitted especially those that are beneficial to the public at large for instance, mutual and cooperative insurance. Among the advocates are Muhammad 'Abduh, Muhammad Abu Zahrah and Muhammad Yusof Musa.[67]

Other works on *Gharar* mainly discuss the effects of *Gharar* and the extent of the effects on contracts in general as espoused in the works of Ahmad Hidayat who holds the opinion that the effect of *Gharar* on insurance contracts has produced different views on the permissibility of insurance as well as different contending views on *Gharar* in the contract over time. He contends that the modernist view tends to be more liberal in the sense that the prohibition of *Gharar* is qualified according to current circumstances and conditions than the traditionalist view, which is a distillation of the classical jurisprudence on the subject.[68]

Other works that bring out new forms of discussion on *Gharar* in insurance among others include Siddiqi who maintains that the uncertainty involved in the contract tends

[64] Ahmad, H., (2000) *Evolution of Islamic Banking and Insurance as a System Rooted in Ethics*, New York: *Takaful* Forum, April, 26.
[65] Muslehuddin, M., (1982) *op cit*.
[66] Siddiqi, M. N., (1985) *Insurance in an Islamic Economy*, United Kingdom: The Islamic Foundation.
[67] Ahmad, H., (2000) *Evolution of Islamic Banking and Insurance as a System Rooted in Ethics*, New York: *Takaful* Forum, April, 26.
[68] Ahmad, H., *op cit*.

to disappear when large numbers are involved.[69] Ma'sum also points out that the possibility of *Gharar* being involved in the subject matter of the transaction is only through the 'happening of the risk' and this uncertainty will forever be known by Allah only. The uncertainty comes in the form of pure risk which is implicated with fear of risk, for example the death of the policyholder or the incident insured is not vague and is identified before the commencement of a policy.[70]

Rosly,[71] in the meantime questioned the address of the *Gharar* pinpointed by the *Fatwa* from the perspective of risks, which is dealt by a commercial insurance contract. He suspected that the issue of *Gharar* contended by the *Fatwa*[72] is misplaced in certain parts that is in the uncertainty of the event, for example the occurring of death or injury. These uncertainties are pure risks that are transferred to the insurer companies by the insured through the payments of premiums and are beyond human control.

Looking back at the literature, we notice that the permissibility of insurance from *Gharar* perspective depends on the extent of its existence in the contract. On the other hand, the scale of its existence depends on the accepted subject matter as well as consideration of pure risk as an internal or external factor of the contract. Thus, by trying to determine the precise subject matter as well as resolving the issue of pure risk, the discourse might give a new insight on the true extent of *Gharar* existence in an insurance contract.

The above doctrine suggests that *Takaful* as an alternative to conventional insurance seeks to provide the same or better services that are obtainable in conventional insurance practice. The *Takaful* model is aimed at protecting the participants against

[69] Sadiq, C. M., (2001) *op cit*.
[70] Ma'sum, B. M., (2001) *Principles and Practices of Takaful and Insurance Compared*, Malaysia, International Islamic University of Malaysia.
[71] Rosly, S. A., (1997) *Economic Principles in Islam*, International Islamic University of Malaysia (IIUM), Journal of Economics and Management.
[72] Fatwa by the *Fiqh* Council in 1985 prohibiting Muslims from partaking in conventional insurance scheme because of the *Shari'ah* prohibitive features embedded in it.

incapability to overcome uncertainties and difficult times. This noble aim of the concept dubbed ‘’insurance with a human face’’ is realized on the foundation of different supportive features altogether.

Aiman Fazeer Yap[73] looks at application of Islamic Insurance (*Takaful*) from the point of view of Marketing and Sales. He opines that within the context of *Takaful* business, marketing is essential because *Takaful* is new and therefore needs good marketing to achieve market penetration. *Takaful* agents have to have that selling skill to get people to finally adopt *Takaful* products. As market grows, the potential for the agents business also grows. That opens up opportunities for the agent to expand business as an entrepreneurial venture.

Rusni Hassan[74] in his introductory book says so much literature has been written on Islamic Finance, particularly the subject of Islamic Banking and *Takaful* from a general point of view. However, there are many who study the subject without an adequate knowledge of the basic *Shari'ah* concept, mechanism and legal framework in which it operates. He posits that many of the literature on the products of Islamic banking and *Takaful* provided are too concise an explanation on the concept or are too technical for beginners to understand its concept and operation. Further, the materials are scattered in journals, online publications and published works. His book fills in the gap by providing the necessary background material.

Zuriah and Hendon[75]state that it is common knowledge that *Takaful* or Islamic insurance is not a new conception, rather a doctrine in practice from the age mankind started trading with one another. They maintain that *Takaful* is a form of financial loss transfer designed to offset losses due to the ever present hazards associated or found in any business venture. The book discusses risk followed by description of the reported

[73] Aiman, F. Y., (2009) *Takaful Effective Marketing and Sales Practices IBFIM,* Parcetakan Mesbah Sdn Bhd (819193 – K).
[74] Rusni, H., (2011) *Islamic Banking and Takaful,* Pearson Malaysia Sdn Bhd.
[75] Zuriah, A., and Hendon R., (2009) *Takaful: The 21st Century Insurance Innovation,* McGraw – Hill (Malaysia) Sdn Bhd.

insurance-like or cooperative scheme in the older days, tracing its beginnings and the conventional practice in different parts of the realm. They further highlighted the reasons for the acceptance of *Takaful* and its role for the future. The authors also focused on the experience of Malaysia in *Takaful* implementation and also those of other parts of the world. They stated further, that the impressive growth and impending expansion into new economies are strong indications for would be *Takaful* Operators to equip and fortify themselves with innovative *Takaful* packages that are tailored to the needs of the participants in order to match the service eminence of the conventional insurance market.

Sudin Haron and Wan Nursofiza Wan Azimi[76] write extensively on the theoretical, conceptual and operational aspects, laws and regulations of Islamic Banking, Islamic Financial markets and *Takaful* system. They posit that the integration of Islamic finance into the global economic stage is a reflection of the growing cognizance of and demand for investments in line with *Shari'ah* principles, progress in developing Islamic regulatory framework and enhanced global connexions. They maintain that the recent financial crisis that has emerged due to global credit woes has broadened the appeal for Islamic finance. The vibrant and thriving *Takaful* Industry and Islamic capital market are explored extensively.

Rosly[77] examines in great details the principles and practices of Islamic Banking and financial markets, particularly from the Malaysian experience. He says the main objective of Islamic financial system is to govern the flow of funds from the surplus sector to the deficit sector and it does so to promote balance and justice in accordance with the tenets of Islam. That is, by adhering to *Shari'ah* principles and adeptness, public and private interests can both be equally secured. By so doing the legal and

[76] Sudin, H., and Wan Nursofiza W. A., (2009) *Islamic Finance and Banking System: Philosophies, Principles and Practices,* McGraw – Hill, Malaysia Sdn. Bhd

[77] Rosly, S. A., (2005) *Critical Issues on: Islamic Banking and Financial Markets, Islamic Economics, Banking and Finance, Investment, Takaful and Financial Planning,* Dinamag Publishing, 600000, Kuala Lumpur, Malaysia.

moral proportions of product enterprise are accorded equal importance. The book further demonstrates the interlinking network of values derived from revelation and reason-senses in resources allocation, particularly capital. It deals with variant issues invoking philosophy and ethics, history, economics, banking and the capital market. Islamic economics and finance are discussed by way of examples and problems faced by Islamic financial institutions, particularly in Malaysia.

Venardos[78] discusses the foundations of Islamic banking, developments and issues. The book provides essential insights on the development of Islamic finance in South-East Asia. It also analyses Islamic finance and portrays the importance of Islamic finance that transcends cultural and religious diversities within the region. A projection for the future is also made along this line.

Frenz and Soualhi[79] discussed *Takaful* and Re*Takaful* in depth in their work. They provided an insight into the doctrines and trending practices of Islamic insurance (*Takaful*) and reinsurance (Re*Takaful*). Their approach is a balanced mix of general background information, technical knowledge and examples from the current key *Takaful* knowledge, complimented by a primer on the Islamic banking and capital market as well as Islamic contract law.

CONCLUSION

The chapter laid the foundation of the study by briefly introducing the background and historical antecedents of the Nigerian insurance industry and the attendant practice which has led to the emergence of a niggling endemic insurance gap. *Takaful* as a panacea was touted as a veritable proposition in engendering deepening insurance penetration and financial inclusion of the hitherto underserved huge Muslim clientele. However, what remains critical is that the *Takaful* Operational Guidelines 2013 are

[78] Venardos, A. M., (2005) *Islamic Banking and Finance in South-East Asia its Development and Future,* B & Jo Enterprise Pte ltd.
[79] Frenz, T. and Soualhi, Y., (2010) *Takaful and Retakaful IBFIM,* Munich Re Percetakan Mesbah Sdn. Bhd

caught in a web of regulatory ambiguities and uncertainties with other enabling insurance instruments – conditions which could be inimical to the smooth take off and sustenance of *Takaful* practice in Nigeria. The problem of the research was stated while highlights were made of the aims and objectives bothering on research questions and hypothesis. The significance and scope of the study formed veritable building blocks while the methodology which comprised doctrinal and qualitative tools were employed in carrying out the objectives of the study. Literature review was stated to be of paramount significance but the limitations within the context of this particular study were evident due to the dearth of literature on the statutory and regulatory challenges on *Takaful* application in Nigeria.

CHAPTER 2: THE LEGAL FRAMEWORK OF CONVENTIONAL INSURANCE UNDER NIGERIAN LEGAL SYSTEM

2.0. INTRODUCTION

The importance of institutionalized insurance businesses in modern commerce cannot be overemphasized.[80] Their emergence and existence in Nigerian commercial practice is relatively recent. The development of insurance legal framework and practice in Nigeria is traceable to the British pattern which was introduced into Nigeria by the British colonial administrators. The British insurance companies first operated in Nigeria through their accredited agents[81] but later these agents were gradually displaced by the establishment of branch offices. A good example is Royal Exchange Assurance which established its branch office in Nigeria in 1921.[82]

The practice of some form of insurance in Nigeria has been known in traditional Nigerian society even before the advent of British colonial administrators. Age grade and tribal associations as well as social clubs[83] have for more than a century, and even today, evolved a rudimentary form of insurance scheme for their members. Under this scheme, the members of the association through levies and donations may raise funds from which a handsome amount of money will be presented to the next of kin of a deceased member, on the occasion of the demise of such a member. Such a donation will go a long way in settling both the funeral expenses of the deceased member as well as the immediate financial burdens of the deceased's family and dependants. Some social clubs have even, in special deserving occasions, awarded educational

[80] The insurance sector worldwide remains the only industry that exists to ensure the continuity of other sectors by restoring individuals and corporate bodies to their former positions each time they suffer losses through claims' settlement. See Outreville, J.F., (1998) *Theory and Practice of Insurance*, Massachusetts, USA, Kluwer Academic Publishers, p. 10. That insurance gives impetus to economic growth and development cannot be overstated. Income growth, which is guaranteed by insurance, is essential for achieving economic and social development. In this context, insurance fulfils somewhat different economic function than do other financial services put together, and in turn, insurance requires particular conditions to flourish and to make full economic contributions. That is its unique attribute.

[81] These were educated Nigerians who schooled in Britain and later came back home and became attached to the British colonial administration. They were later to spearhead the Independence movement, e.g. late Dr. Nnamdi Azikiwe, first president of The Federal Republic of Nigeria.

[82] Okay, A., (1985), *Commercial Law in Nigeria*, p. 316.

[83] Examples are Igbo Progressive Union and the Egbe Omo Oduduwa Organisation.

scholarships to the children of their deceased member, depending, of course, on the financial resources of the club. Although the efforts of these traditional, *quasi*-insurance schemes[84] are commendable, it is doubtful whether they can cope with the intricacies and demands of modern insurance. Surely, in order to co-exist as adjuncts of modern insurance companies, they require some modifications and improvements in their operations, in order to check embezzlement, excesses and abuses by their leaders or officials.[85]

There was a proliferation of mushroom insurance companies that sprang up in Nigeria in the sixties and seventies in the lucrative conventional insurance business. They were established and operated by persons of doubtful integrity, although a few of these insurance companies operated impeccably. Widespread public outcry against the nefarious activities of some of these 'mushroom' companies, prompted the then Federal Military Government to promulgate the Insurance Decree (now Act)[86] on 1st December 1976 to bridle their excesses. This was a revolutionary Act, for it provided new and stringent rules and regulations,[87] whose principal aim was to liquidate all mushroom insurance companies and replace them with strong dependable and financially viable ones. The existing insurance companies were given six months, expiring on 3rd May 1977 to comply with the new regulations otherwise they would forfeit their licenses. On the expiry date, only 56 out of well over 200 companies satisfied the provisions of the new law and were duly registered. In addition, four more companies were registered between September and October, 1977.[88]

[84] Nigerians without access to or unable to use formal financial services use informal options for their savings and credit needs. Informal choices like moneylenders and Asusus are dominant in rural areas, but exist in the urban settings as well. Asusu is the oldest form of savings and local insurance club in Nigeria. The majority operates with unwritten laws, based on oath of allegiance and mutual trust. Asusu associations contribute a fixed amount periodically and give all or part of the accumulated funds to one or more members in rotation until all members have benefitted from the pool. See http://www.miccrofinancenigeria.com/other-news/Asusu-expanding-nigeria%E2%80%99s-financial-services-frontier/.
[85] Okay, *op cit* p. 316.
[86] Decree (Act) No. 59 of 1976.
[87] Insurance Regulations 1977; it came into force on 17th January 1977.
[88] Okay, *op cit*, p. 317.

The law regulating conventional form of insurance in Nigeria can be broadly classified into two. The first part is the law of insurance contract itself which deals with legal relationship between the insurance company and the person taking out the insurance policy referred to as the insured or the policy holder.[89] The applicable law in this regard is sourced from English Common law. This applicable legal framework is derived from the English Common law itself, the doctrines of equity and statutes of general application in force in England before the 1st of January, 1900.

The second part of the regulatory framework is the body of laws that regulate the conduct of the business of insurance and the entire regulatory machinery through which the insurance industry is controlled and supervised.[90] This is also referred to as subsidiary legislation and derives its authority from the various statutes that have been enacted to regulate the insurance industry. Although insurance principles and legislative instruments are so closely connected and collectively constitute the body of laws that regulate affairs of the industry, the two are distinct in their features, effects and historical sources.[91]

On a broader scale, the whole legal framework of insurance under Nigerian law may, therefore, be viewed from a number of perspectives namely; - statutes of general application, doctrines of equity, English common law, Nigerian subsidiary legislation or regulatory framework, Islamic law and customary law. Customary law and Islamic law are included here because they form part of the sources of Nigerian laws. The sixth source is judge-made-law or case law.[92]

[89] The insured is any person who is capable of entering into a contract of insurance. It includes a minor if the contract is for his benefit, but insane persons and drunken persons may lack such capacity. Contracts of insurance made by such persons are voidable.
[90] The development of financial markets and the insurance sector in particular depends to a great extent on the existence of an enabling policy, regulatory and supervisory environment. Policies are important as they define the priorities, the roles and responsibilities of significant stakeholders, and influence where the bulk of financial, political and human resources, from both private and public actors, are invested. Regulation above all sets the rule for entry, operation and market conduct. Supervision ensures compliance with the rules and penalizes violations, being therefore an important factor to increase public confidence. See Dias, D., et al (2013), Towards Inclusive Insurance in Nigeria: An Analysis of the Markets and Regulations, Eschborn, p. 50.
[91] Irukwu, J. O.,(1993) *Fundamental Principles of Insurance Law*, p. 3.
[92] Irukwu, J.O., *op cit*, p. 12.

As far as antecedents and application of insurance is concerned in Nigeria, customary insurance[93] is rudimentary and still inchoate while not much is known about Islamic law of insurance (*Takaful*) until recently, despite the fact that Islamic law is part of the Nigerian legal system.[94] This chapter primarily deliberates on the concept of conventional insurance as it is generally known worldwide with particular reference to some notable differences in its application in Nigeria. The chapter also discusses the historical origins of the received English laws and their legislative limitations in the scope of their application in Nigeria. It also analytically dwells on the regulatory laws that shape the business of insurance conduct and the entire regulatory machinery through which the Nigerian insurance industry is controlled and supervised. The chapter concludes with an examination of the major challenges faced by the Nigerian insurance industry resulting in the emergence of an endemic gap that has stunted its growth and trivialized its impact and contributions to the Nigerian economy. It is submitted that it is the prevalence of this endemic insurance gap that has paved the way for recourse being had to Islamic insurance (*Takaful*) in order to facilitate rapid deepening insurance penetration and financial inclusion of the majority of Nigerians who remain generally underserved.

2.1 APPLICATION OF RECEIVED ENGLISH COMMON LAW AND HISTORICAL BACKGROUND OF CONVENTIONAL INSURANCE IN NIGERIA

As earlier pointed out, Nigeria was colonised by the British and with that colonisation came the receipt of all their laws and practices as were applicable to the United

[93] The existence of customary insurance is inferred from the delineating provisions of Section 1 of the Insurance Act, 2003, in its recognition of some forms of insurance other than those to be regulated by the Act. The implication of the provision is that those forms of insurance exempted from the Act will also be out of the regulatory purview of the National Insurance Commission (NAICOM). In as much as traditional or customary insurance exists and is so recognized, the fact still remains that it is rudimentary and unviable on a large scale. The intricacies of modern insurance practice are simply too overwhelming for customary form of insurance to be put on a comparative scale.

[94] Islamic law was administered in Nigeria as if it was one of the variant customary laws and was therefore subject to the repugnancy doctrine test applicable to customary laws. See Section 14 of the *Shari'ah* Court of Appeal Law (N.N. Laws 1963, Cap 22) which empowers the *Shari'ah* Court of Appeal of each of the northern states to administer Muslim law of the Maliki School as customarily interpreted at the place where the trial at first instance took place. This had negative impact on early evolution and integration of the *Shari'ah* based financial systems into Nigerian legal framework. See also Adamu, A.I., *op cit*, p. 61.

Kingdom. The Nigerian legal system is comprised mainly of the English Common law, doctrines of equity and the statutes of general application that were in force in England before 1st January 1900. Other foundations of Nigerian *corpus juris* include the various customary laws which do not offend natural justice, equity and good conscience, Islamic law and case law or judge made law.

2.1.1 The Received English Law

The received English Law as a foundation of Nigerian body of laws[95] has its origins in ''common law, doctrines of equity'', statutes and subsidiary legislation. It has been introduced into Nigerian law by Nigerian legislation. The chronology of the reception dates began in 1863 when Ordinance No. 3 of that year ushered in English law into the Lagos colony. Usually, where a court is empowered to administer the received law, provisions relating to its application by the court are contained in the enactment which created the court and subsidiary legislation made under the enactment. For instance, various High Court enactments, the Magistrates Courts regulations operational in southern States and the District Courts legislation applicable in the northern States contain such provisions. The reception provisions applicable in each jurisdiction are substantially the same in wordings as the reception provisions in force in other jurisdictions except that the Law of England (Application) Act does not receive English statutes.[96] An example of a current Nigerian enactment that has received English law is the Law (Miscellaneous Provisions) Act[97] in force as federal law throughout the country.

Section 2 (Miscellaneous Provisions) Law[98] provides as follows:

[95] The received English law as a source of Nigerian law excludes English law received by being enacted or re-enacted as Nigerian legislation. The latter type of received English law is not a source of Nigerian law. It is the resulting Nigerian legislation that is a source of the law. See e.g. the Defamation Act 1952 (15 & 16 Geo. 6 & 1 Eliz. 2, c. 66) whose provisions were re-enacted as part of the Defamation Law (W.R.N. Laws 1959, Cap 33).
[96] Obilade, A.O., (2007), *The Nigerian Legal System*, Spectrum Books Limited, Ibadan, Nigeria, p. 69.
[97] See Interpretations Act 1964 (No. 1 of 1964), s. 28.
[98] Lagos Laws 1973, Cap. 65.

''2 (1) Subject to the provisions of this section and except in so far as other provision is made by any Federal or State enactment, the common law of England and the doctrines of equity, together with the statutes of general application that were in force in England on the first day of January, 1900, shall be in force in Lagos State.

(2) The statutes of general application referred to in subsection (1) together with any other Act of Parliament with respect to a matter within the legislative competence of the Lagos State which has been extended or applied to the Lagos State shall be in force so far only as the limits of local jurisdiction and local circumstances shall permit and subject to any Federal or State law.

(3) For the purpose of facilitating the application of the said imperial laws they shall be read with such formal verbal alterations not affecting the substance as to names, localities, courts, officers, persons, moneys, penalties and otherwise as may be necessary to render the same applicable to the circumstances.''

With respect to the date January 1, 1900, it is clear from Section 2 of (Miscellaneous Provisions) Law that the date applies to the statutes only and not to the ''common law'' or ''equity'' both of which are separated from the ''statutes'' by the use of the words ''together with.''[99]

Another point which should be mentioned in relation to the application of English common law and equity in the Nigerian legal framework is that in the event of a discrepancy between a rule of the common law and a doctrine of equity on the same matter the doctrine of equity prevails, generally.[100]

[99] Obilade, A.O., *op cit*, p. 70.
[100] See, e.g. the High Court Law (N.N. Laws 1963, Cap. 49), s. 31.

It should also be stated that in determining any applicable rule of the common law of England or any applicable English doctrine of equity, the decisions of the courts of England are a mere guide to the Nigerian courts.[101] The Nigerian courts are free to hold that what is accepted by the English courts including the highest court of England (then House of Lords but now known as the Supreme Court) as the common law rule or equitable doctrine on a particular matter is not in fact the English rule or doctrine on the matter.[102]

The case law on this subject, however, appears to support the view expressed in the test in *Attorney-General v. John Holt & Co.*[103] that an English statute which applied to all classes of the community in England on January 1, 1900 would very likely be held to be a statute of general application. For instance, in *Lawal v. Younan,*[104] the Federal Supreme Court held that the Fatal Accidents Act, 1846[105] and the Fatal Accidents Act, 1864[106] both of which applied to all classes of the community in England were statutes of general application that are applicable in England. Similarly, in *Braithwaite v. Folarin*[107] the West African Court of Appeal in holding that the Fraudulent Conveyances Act 1571[108] was a statute of general application said, Transfer Act 1897:[109]

> ''The Land Transfer Act of 1897 applied quite generally to all estates in England of persons dying after 1st January1898. It is difficult to see how a statute could be of more 'general application' in England than that, and it was in force in England on 1st January, 1900.''[110]

[101] See *Alli v. Okulaya* (1970) 2 All N.L.R. 35; Jill Cottrell, ''An End to Slavishness? A Note on *Alli v. Okulaya''* J.A.L. 247.
[102] *Ibid*. Compare A.E.W. Park, *The Sources of Nigerian Law* (1963), pp. 62-64.
[103] (1910) 2 N. L. R. 1 at p. 21.
[104] (1961) 1 All N. L. R. 245.
[105] 9 & 10 Vict. c. 93.
[106] 27 & 28 Vict. c. 95.
[107] (1938) 4 W.A.C.A. 76.
[108] 13 Eliz. 1, c. 5.
[109] 60 & 61 Vict. c. 65.
[110] See also *Olanguno v. Ogunsanya* (1970) 1 All N. L. R. 223 at pp. 226-227; *Ajuo v. Sonola* (1973) 5 S.C. 119 at pp. 122-124.

In fact, the statute applied to the estate of persons who died after 1897 holding legal interests in land. It has, however, been argued that because persons dying after a particular date holding legal interests in land were not ‘’all classes of the community’’ the court was wrong in stating that it was difficult to see how a statute could be of more general application.[111] It is submitted that this ingenious argument takes a narrow view of the extent of the application of statutes. Every statute deals with a particular subject matter. With respect to its subject matter – holding legal interests in land at the time of death – the Act applied to all classes of persons without any distinction with effect from its date of commencement. Every person was a potential owner of a legal interest in land to whom the Act could apply. However, if at the point of his demise a person did not hold a legal interest in land the Act would not in fact apply to him. It is submitted that a statute applies to all classes of the community if, in relation to its subject matter, all classes of persons are potentially within the ambit of the statute even if it is unlikely that the statute will ever be applied to a specific individual or a specific class of individuals. It is only on this broad view of the extent of application of statutes that any statute can be said to apply to all classes of the community.[112]

In the light of the decisions of the courts, therefore, a statute would probably be held to be a statute that is generally applicable in England if it was applicable on January 1, 1900, where the following conditions are satisfied:

(a) That the statute was in force in England on January I, 1900; and

(b) That in respect of its subject matter, it applied to all classes of the community in England on that date.

It would have been observed that statutes of general application are received in general terms, without reference to their subject matter. However, there is another class of

[111] A. E. W. Park, *op cit* (n. 19, above). P. 28.
[112] See e.g. the Infants Relief Act 1874 (37 & 38 Vict. c. 62. See also Obilade, A. O., *op cit* p. 74.

received English statutes which consists of statutes received by reference to their subject matter. For instance the received English law of probate consists of the common law, equity, statutes and subsidiary legislation. Thus, Section 33, High Court Law[113] of the northern States provides:

> '' The jurisdiction of the High Court in probate cases and proceedings may subject to the provisions of the Law and especially section 34[114] and to rules of court be exercised by the court in conformity with the law and practice[115] for the time being in force in England.''

The received English law applies subject to Nigerian legislation. Thus section 2 of (Miscellaneous Provisions) Law states that the ''common law, the doctrines of equity and the statutes of general application'' are applicable subject to the requirements of the section ''and except in so far as other provision is made by any Federal or State enactment.''[116] Accordingly, to the extent that the subject matter of a rule of the received law is dealt with by a local enactment, the local enactment and not the received law is the applicable law. Moreover, where there is a conflict between the received law and a local enactment, the local enactment prevails. As a result of the reception statutes, therefore, the received English law applies to the application of customary law in appropriate cases.[117] Nigerian legislation is gradually reducing the content of the received English law as a foundation of Nigerian body of laws. For instance, the common law doctrine of *interesse termini*[118] was abolished by section 163 of the

[113] N. N. Laws 1963 Cap. 49.
[114] Section 34 deals with the application of customary law.
[115] Provisions of Nigerian legislation introducing the common law and equity into Nigeria in general terms are subject to reception provisions introducing the rules of the common law and equity on specified matters into Nigeria. See e.g. High Court Law (N.N. Laws Cap. 1969, Cap 49), s. 28 where the rules of the common law and equity on a specified matter are received together with the English statutory law on the matter the statutory law prevails in case of conflict between it and a rule of common law or equity. Of course, where there is a conflict between the received common law and the received equity on the same matter equity prevails, generally.
[116] See also High Court Law (Lagos Laws 1973 Cap. 52), s. 16.
[117] See e.g. High Court Law (N. N. Laws 1963, Cap 49, ss. 28, 29 and 33, *Contra Adesubokan v. Yunusa,* (1971) N. N. L. R. 71.
[118] An *interesse termini* was an interest – a right of entry – which a lessee of land acquired in the land by virtue of the lease before he was actually in possession of the land.

Property and Conveyancing Law[119] and the Defamation Act 1961[120] modified the common law.[121] Similarly, some statutes of general application were repealed impliedly or expressly. Thus, section 7 (1) of the Obscene Publications Act 1961[122] as affected by section 4(1) of the Lagos State (Applicable Laws) Edict 1968[123] provided as follows:

> ''To the extent that the Obscene Publications Act, 1857[124] is in force in the Lagos State as a statute of general application that Act shall cease to have effect and is hereby repealed.''[125]

An example of implied repeal is found in section 2 of the Criminal Justice (Miscellaneous Provisions) Decree 1966.[126] By creating the offence of obtaining credit by fraud, the Decree impliedly repealed section 13(1) of the Debtors Act 1860[127] in its application to Lagos.

Local circumstances constitute another limitation to the application of the received English statutes. Thus, with respect to Lagos State section 2(2) of (Miscellaneous Provisions) Law[128] provides that

> ''statutes of general application…shall be in force so far only as the limits of local jurisdiction and local circumstances shall permit and subject to any Federal or State law.''[129]

No doubt, some English statutes are unsuitable for application in Nigeria by reason of the difference between the circumstances prevailing in England and those prevailing in

[119] W. R. N. Laws 1959, Cap. 100. See *Adeponle v. Saidi* (1956) 1. F. S. C. 79.
[120] No. 66 of 1961.
[121] The Act was based on the Defamation Act 1952 (15 & 16 Geo 6 and 1 Eliz. 2, c. 66). See also Law Reform (Contracts) Act 1961 9No. 64 of 1961) which modified the common law by re-enacting provisions of the Law Reform (Frustrated Contracts) Act 1943 (6 & 7 Geo 6, c. 40).
[122] No. 51 of 1961. See now Criminal Code (Lagos Laws 1973, Cap. 31), ss. 233B-233F.
[123] No. 2 of 1969.
[124] 20 & 21 Vict. c. 83.
[125] See also s. 5(6) of the Law Reform Contracts Act 1961 (No. 64 of 1961) which expressly repealed s. 4 of the Statute of Frauds Act 1677 (29 Car. 2, c. 3).
[126] No. 84 of 1966.
[127] 32 & 33 Vict, c. 62. See P. E. O. Bassey, ''Obtaining Credit by Fraud in Nigerian Law'', *Nigerian Bar Journal*, Vol. IV, No. 2 (1963), p. 21.
[128] Lagos Laws 1973, Cap. 65.
[129] *Ibid.*

Nigeria. Where a particular factor essential to the application of an English statute is not present in Nigeria, the courts would hold local circumstances have not permitted its application. For example, the Bankruptcy Act 1883[130] is not in force in Nigeria because the machinery for its application is not available in the country. Brett F. J., in *Lawal v. Younan*[131] expressed the view that

> ''the court would be free to hold that local circumstances did not permit a statute to be in force if it produced results which were manifestly unreasonable or contrary to the intention of the statute.''[132]

It should be stressed, however, that the fact that some difficulties are encountered in applying an English statute in Nigeria does not mean that local circumstances do not permit its application.[133] Obviously, difficulties do arise in some cases because the statutes were made for England in the light of circumstances which are in some cases much different from circumstances prevailing in Nigeria. If a statute of general application is otherwise applicable, it is the court's duty to solve problems concerning its application in Nigeria in so far as the application would not defeat the purpose of the statute.[134]

The received English statutes apply ''so far only as the limits of the local jurisdiction…permit.'' That the words ''limits of the local jurisdiction'' do not refer to legislative competence appears clear from section 29 of the High Court Law[135] of each of the northern States which expressly provides that the application of the ''imperial laws'' within the legislative competence of the State is subject to the parameters of the local jurisdiction. Thus, the words ''limits of the local jurisdiction'' are not to be

[130] 46 & 47 Vict. c. 52.
[131] (1961) 1 All N. L. R. 245 at p. 257.
[132] See *Jex v. Mckinney* (1889) 14 App. Cas. 77 where the Judicial Committee of the Privy Council in holding that the Mortmain Act 1735 (9 Geo. 2, c. 36), a statute of general application, was not in force in British Honduras said that it ''was framed for reason affecting the land of society of England, and not for reasons applying to a new colony''. The application of the statute would have resulted in a declaration that the gift of land to certain churches was invalid.
[133] *Lawal v. Younan* (1961) 1 All N. L. R. 245 at p. 250.
[134] Obilade, A. O., (2007), *op cit*, p. 79.
[135] N. N. Laws 1963, Cap. 49.

construed to mean legislative competence. The words appear superfluous. They may be construed as reference to the rule against extra-territorial legislation applicable to dependent territories but retained in error after the attainment of independence by the country.[136]

It is noteworthy that the provisions relating to local circumstances in relation to the application of statutes of general application do not apply to the common law or to equity.[137]

2.1.2 English Law Extending to Nigeria

English legislation that is directly introduced in Nigeria is referred to as extended English Law. This genre of English law is to be clearly differentiated from the received English law. The latter is brought into Nigeria directly by Nigerian legislation. Extended English law into Nigeria consists of statutes[138] and subsidiary legislation[139] enacted on or before October 1, 1960 that were not yet abrogated by any appropriate Nigerian authority.[140] Some particular English laws extending to Nigeria that have been abrogated from the time of independence include the Copyright Act 1911,[141] the Nigerian Independence Act 1960[142] and the Nigerian (Constitution) Order in Council 1960[143]. Similar to the received English statutes, English enactments that extend to Nigeria are subject to Nigerian legislation, parameters of local jurisdiction, local

[136] A. E. W. Park, *op cit*, p 30.
[137] *Contra* Robert B. Seidman '' A Note on the Construction of the Gold Coast Reception Statute'' (1969) J. A. L. 45 at p. 50.
[138] The statutes consisted of Acts of the U. K. Parliament and prerogative Orders in Council. Prerogative Orders in Council are not subsidiary legislation. They are original laws made by the Crown as a legislature and are, therefore, statutes. Such Orders were made for the colony of Lagos. Dee S. G. G. Edgar (ed.)
. *Craies on Statute Law* (17th ed., 1971), p. 289.
[139] The subsidiary legislation includes Orders in Council made under Acts of the U. K. Parliament.
[140] Nigeria Independence Act 1960 (8 & 8 Eliz. 2, c. 55); Nigeria (Constitution) Order in Council, 1960 (S.I. 1960 No. 1652), s. 1.
[141] 1 & 2 Geo. 5, c. 46. The Act was applied to Nigeria by Order in Council No. 912 of 1912 (Fed. and Lagos Laws 1958, Vol. XI, p. 222). It was repealed by s. 18 of the Copyright Decree 1970 (no. 61 of 1970).
[142] 8 & 9 Eliz. 2, c. 55.
[143] S.I. 1960 No. 1652 (L. N. 159 of 1960). See also s. 21(3) of the Extradition Decree 1966 (No. 87 of 1966 which repealed *inter alia*: (a) the West African (Fugitive Offenders) Order in Council 1923 (No. 596 of 1924); (b) the Extradition Act 1870 (33 & 34 Vict. c.52); (c) the Extradition Act 1873 (36-37 Vict. c. 60); (d) the Extradition Act 1895 (58 & 59 Vict. c. 33); (e) the Extradition Act 1906 (6 Edw. 7, c. 15) and (f) the Fugitive Offenders Act 1881 (44 & 45 Vict. c. 69).

statuses and formal oral alterations.[144] Furthermore, since there is no English law enacted that was enacted in England after October 1, 1960 that now applies on its own authority in Nigeria, any enactment that now extends to Nigeria continues to be applicable in Nigeria, notwithstanding its abrogation in England after that date, until it is equally abrogated by an appropriate Nigerian authority.[145]

One prominent characteristic of the content of English enactments as bases of Nigerian law is that many English regulations which, have been considered obsolete and unsuitable in England, long ago and have been abrogated or replaced there by new rules remain applicable in Nigeria. For instance, the abrogated English law in 1925 forms a large part of the land law that is still in force in many southern states of Nigeria.[146] It should also be mentioned that as a result of the reception of English statutes by reference the exact content of the statutory law in force in Nigeria cannot be readily ascertained. In 1959, the Legislature of the Western Region of Nigeria re-enacted as local legislation selected provisions of English statutes and made the Law of England (Application) Law[147] by virtue of which no statute of the United Kingdom Parliament within the limits of the Region's legislative competence was to be in force in the Region. Such a step, rather than the piecemeal method of replacing English statutes with Nigerian enactments is recommended to all the jurisdictions in the country.[148] In receiving English or other foreign ideas in law-making the social values of the local community should be carefully considered. Suitability in the locality should be one of

[144] See e.g. law (Miscellaneous Provisions) Law (Lagos Laws 1973, Cap 65). ss. 2(2) and 3; Interpretations Law (E. N. Laws 1963, Cap 66), s. 15; Interpretation Law (N.N. Laws 1963, Cap. 52), s. 13; Interpretation Law (W. R. N. Laws 1959, Cap. 51), s. 13; Law (Miscellaneous Provisions) Act, s. 15 (see Interpretation Act 1964, s. 28).
[145] See e.g. s. 6 of the Civil Liability (Miscellaneous Provisions) Act 1961 (No.33 of 1961) in relation to the continued application in the city of Lagos of the Carriage by Air Act 1932 (22 & 23 Geo. 5 c. 36) after the repeal, in England, of the 1932 Act by the Carriage by Air Act 1961 (9 & 10 Eliz. 2, c. 27). The provisions of the 1961 Act have now been incorporated in section 21 of the Law Reform (Torts) Law (Lagos Laws 1973. Cap. 67).
[146] Obilade, A. O. *op cit*, p. 82.
[147] W. R. N. Laws 1959, Cap. 60.
[148] Obilade, A. O., *op cit*, p. 82.

the conditions to be satisfied before an English statute, repealed or current in England, is re-enacted as Nigerian legislation.[149]

2.1.3. Insurance Contract Law in Nigeria

The law relating to insurance is an example of specific or particular contracts. It is thus overseen by the common law of contract, except that the doctrine of frustration is inapplicable to a contract of insurance. The rule of law here is that once the premium is paid and risk assumed by the insurer, there shall be no apportionment or return of premium afterwards, even though the subject-matter of the risk may vanish before the period of cover has elapsed.[150]

An insurance contract arises between an insurer and an insured whereby the former undertakes to provide against a risk apprehended by the insured. In other words it arises where a person pays money as consideration to another person to indemnify him upon the happening of an uncertain event or upon the occurrence of an event indeterminate as to time.[151]

Lawrence, J., defined insurance in the case of *Lucena v. Craufurd*[152], as follows:

> '' Insurance is a contract by which one party in consideration of a price paid to him adequate to the risk becomes security to the other that he shall not suffer loss, damage or prejudice by the happening of the perils specified to certain things which may be exposed to them.[153]

In Chitty on Contracts[154] another comprehensive definition was attempted thus;

[149] Obilade, A. O., *op cit*, p. 82.
[150] Cheshire, G.C., and Fifoot, C.H.S., (1964), *The Law of Contract*, London, p. 497.
[151] Okany, M. C., (1992), *Nigerian Commercial Law*, Africana First Publishers PLC, p. 812.
[152] (1806) 2 Bos. And P.N.R. 269 at p. 301
[153] *Ibid* at p. 301.
[154] Chitty on Contracts Specific Contracts (24th Edition) Para 3901.

‘’ a contract of insurance is one whereby one party (the insurer) undertakes for a consideration to pay money or to provide services to or for benefit of the other party (the assured) upon the happening of an event which is uncertain, either as to whether it has or will provide against loss or to compensate for prejudice caused by the event or for his old age (where the event is the reaching of a certain age by the assured) or (where the event is the death of the assured) for the benefit of other upon his death.’’[155]

At Nigerian case law level, in *Mark Kayode v. Royal Exchange Assurance*,[156] insurance contract was defined as;

‘’ a contract whereby one person called the insurer undertakes in return for the agreed consideration called premium to pay another person called the assured , a sum of money on the happening of a specified event.’’[157]

Adeyemi[158] on the other hand says of insurance as;

‘’ a scheme whereby one person called the insurer in consideration of a price known as premium , agrees to indemnify or pay a sum of money to another known as the insured upon happening of a loss or misfortune.’’[159]

In the case of *Charles Chime v. United Nigeria Insurance Company Ltd*[160] Agbakoba, J., defined insurance as:-

‘’ a contract whereby a person called the insurer in consideration of money paid to him the premium by another person called the assured, agrees to indemnify the latter against loss resulting to him on happening of certain events.’’[161]

[155] Chitty On Specific Contracts, *op cit*, para. 3901.
[156] (1955) W. T. L. T. 154 at 154.
[157] *Ibid.*
[158] Funmi, A., (2007), *Nigerian Insurance Law*, 2nd Edition, p. 3.
[159] *Ibid.*
[160] (1972) 2 E.C.S.L.R. 808 at 811.

Considering the approach taken in Nigerian cases cited above in attempts at defining insurance, it becomes clearly evident that the Nigerian legal system is heavily influenced by the received English laws and statutes thus basically underlining the pattern of conventional insurance practice in the country.

As discussed earlier, the legal basis for the application of English enactments in the Nigerian *corpus juris* is traceable to the Reception Statutes which conferred on Nigerian courts the jurisdiction to enforce principles of English common law, the doctrines of equity and the statutes of general application.[162] As stated earlier on, English Common law encompasses those principles developed by the courts from the norms and customs of the English people otherwise known as the Residual Laws of the land. Consequently, the reception of English common law brought into the Nigerian legal system the concept of insurance in the conventional form from the inception of the contract in addition to the basic principles and other requirements of the insurance contract. The doctrine of equity is well known to have evolved to mitigate the injustices resulting from the strict application of common law principles. The principles of equity were judicial discretions often invoked by the courts to cushion the unpalatable impact of strict application of common law rules. The right of subrogation in an insurance contract, for example, was developed on equitable principles.[163]

Statutes of general application applicable in England prior to 1st January 1900 form the cornerstones of insurance framework. Some examples of these statutes that were integrated into the insurance legal framework in Nigeria are the Life Assurance Act of 1774, Policies of Assurance Act, 1867, etc. In as much as most of these statutes have been substituted with local legislations on insurance, they, however, still remain relevant because Nigerian legal draftsmen normally draw heavily from those English

[161] (1972) 2 E.C.S.L.R. 808 at 811.
[162] Section 32 Interpretation Act Cap 192 Laws of the Federation of Nigeria 1990, Laws of England (Application) Law, Cap 60; High Court Laws No. 8 of 1955 (Northern States).
[163] Funmi, A. *op cit.*

statutes while the statutes still serve as persuasive precedents especially in areas of commercial litigation.

However, in spite of the domestication of the country's legal system by local legislation, the principles of common law have continuously shaped the modern insurance business in Nigeria as well as many other common law countries.

The main purpose of insurance is that an assured protects himself against a risk in the sense that in payment of the premium by him as consideration, he will be paid money as indemnity by the insurer in the event of the happening of the underwritten risk. In other words, the assured by taking out a policy attempts to provide a means of indemnifying himself from some unforeseen hazards.[164]

Under Nigerian legal framework, for a contract of insurance to come into existence, certain essential requirements must be satisfied which are in tandem with the general common law principles of insurance contracts. However, since these common law principles are now domesticated by virtue of the Insurance Act 2003,[165] a brief descriptive analysis of these principles will certainly help elucidate the nature of insurance practice in Nigeria.

It is pertinent to ask the rhetorical question: why will an insurer voluntarily offer to undertake the burden upon himself to provide for the insured on the happening of the event contemplated, by the mere payment of a premium? The answer is that time has now shown that the risk is worth taking, as the appearance of many insurance

[164] See Muslehuddin, M., (2012), *Insurance and Islamic Law*, Adam Publishers and Distributors, New Delhi-2, India, p. 3. ''The aim of all insurance is, to make provision against the dangers which beset human life and dealings. It is, in fact, the danger of loss which makes men to think seriously of some safety devices to avoid it. These devices vary according to the degree of the losses. If the loss is foreseeable it may be avoided by adopting preventive measures, and in case it is small the individual may assume it himself, but the difficulty arises when it is unforeseen and large as it can neither be prevented nor assumed. Hence 'loss prevention' or 'loss assumption' has a very limited application and cannot cope with the losses that are heavy, ruinous and unforeseen. On such occasions the individual is completely destroyed if the assistance of the community or group is not forthcoming. Foe the community as a whole such a loss will be negligible but the individual will be totally ruined if exposed to it singly. This is the theoretical background of insurance which has been devised to meet a loss unknown in time and in amount''.
Still on the purpose of insurance, the Court of Appeal in *I.G.I. Co. Ltd v. Adogu* (2010) 1. NWLR (Pt. 1175), p. 337. CA., held that the fundamental purpose of an insurance contract is to give cover to an insurance risk. In other words, a contract of insurance is meant for unforeseen future occurrence and not for an accident that has occurred.

[165] Laws of the Federation of Nigeria.

companies reveals that what has been regarded as a risk is now been transformed into a very profitable commercial venture.[166]

The core substance of insurance contract may be any movable or immovable property, and in practice is always amply described in the insurance policy. One may for example, insure against the theft of his property or against the property being damaged or destroyed by fire.[167] Apart from physical objects, the subject matter of insurance may consist of an event, whose occurrence may expose the assured to liability against another person.

A contract of insurance, as already stated, operates within the general framework of law of contract, subject to such peculiar rules and principles which govern insurance business. Thus with the exception of marine insurance, a contract of insurance may be made orally,[168] since there is no special form prescribed in law for making a contract of insurance. But nowadays it is customary to embody the terms of an underwriting agreement in a written document because of the complexities of insurance contracts.[169]

Since an insurance contract entails simple contract, it must satisfy the fundamental requirements for the making such a contract. These include the mutuality of consent between the parties;[170] the parties must have contractual capacity; the agreement must be supported by a consideration in order to ensure its enforceability; the insured and the insurer must have proposed to create a legally binding contract, and the object of the contract must not give rise to illegality.[171]

[166] Okany, M.C., *op cit*, p. 12.
[167] *Ibid*, p. 812.
[168] The only exception is that marine insurance must be in writing.
[169] Okany, M. C., *op cit*, p. 813
[170] In life insurance, there may be three parties to the contract, for example, when a creditor takes out a life policy on the life of his debtor or when a wife takes a policy on the life of her husband, In these cases, the parties to the contract would be (a) the insurer (b) the person whose life is insured and (c) the insured or beneficiary under the policy, in this example, the creditor or the wife.
[171] See Okay, A., *op cit*, pp. 317-318; Adesanya and Oloyede(1983) *Business Law in Nigeria*, p. 189; Merritt and Claton(1966), *Business Law*, p. 199.

Generally speaking, there are two main types of insurance as operate in Nigeria, namely:

(a) Indemnity insurance which affords a cover against loss, for example a fire policy on a house or a marine insurance on a ship or vessel. Within the parameters of the underwriting cover, the quantum of the loss is the quantum of the indemnity: and

(b) Contingency insurance which does not provide an indemnity but recompense on a contingent risk, for example a life assurance policy or personal injury cover. The amount to be settled is not quantified by the loss but is amply stated in the insurance policy. And the contractual pecuniary amount is satisfied if the insured dies or the limbs are lost, the value of the life or limb being immaterial.[172]

2.1.4. Elements in a Contract of Insurance

There are three focal elements in a contract of insurance, namely;[173]

(1) For some consideration, usually but not necessarily by way of periodic payments called premiums, the contract gives the insured a right to be recompensed with money or money's worth, upon the occurrence of some uncertain event specific to the contract.[174]

(2) The risk must be one which encompasses some measure of improbability. There must be either improbability or uncertainty whether or not the event will ever occur, or if the occasion is one which is bound to occur at some point in time, there must be uncertainty as to the timing of its occurrence.[175]

(3) The uncertainty of the risk which is essential making the contract that of insurance, rather than a wagering agreement, must be a risk which is *prima facie* adversative to the

[172] See Schmitthoff and Sarre(1984) Charlesworth's Mercantile Law, 14th Edition, p. 499.
[173] Popoola, N., (2015), Taking Insurance Industry Beyond Current Growth Rate, *Punch Newspaper* (online), 20th June, p. 28.
[174] *Ibid.*
[175] Popoola, N., (2015), Taking Insurance Industry Beyond Current Growth Rate, *Punch Newspaper* (online), 20th June, p. 28.

interest of the insured. That requirement is expressed by the law stipulating that the insured must have insurable interest during the conclusion the contractual agreement.[176] Thus, in *Department Of Trade v. St. Christopher Motorists Association Ltd*[177] ‘’each member of an association paid an annual sum so that if an event occurred which prevented the member from driving due to disqualification or injury, the member had a right to be provided with a chauffeur, and if necessary a car and a chauffeur, for up to 40 hours a week, for a maximum of 12 months. The Department of Trade contended that the association was carrying on an insurance business and was an insurance company to which the Insurance Companies Act 1958 (then in force) applied.’’[178]

‘’It was held that, there was no difference in substance between the association paying for a chauffeur for a member and its agreeing to pay him the cost of providing himself with a chauffeur; accordingly, the contracts between the members and the association were contracts of insurance; insurance business was being carried on.’’[179]

On the other hand, in *Medical Defence Union v. Department Of Trade*[180] where the right of a member of the Medical Defence Union, on a claim being made against him, was to have his application for help with that claim properly considered by the Union, but not the right to money or money’s worth, it was held that, ‘’the contract between him and the Union was not a contract of insurance.’’[181]

The contract of insurance as we have seen, as is applicable in Nigeria, is overseen by the universal principles of contract laws, and it is contrary to public policy for a court to enforce a contract of insurance in respect of goods imported into the country in breach of the law. Thus in *Geismar v. Sun Alliance And London Insurance Ltd,*[182] where an

[176] Popoola, N., (2015), Taking Insurance Industry Beyond Current Growth Rate, *Punch Newspaper* (online), 20th June, p. 28.
[177] (1976) 1 W. L. R. 99.
[178] *Ibid.*
[179] (1976) 1. WLR 99.
[180] (1980) Ch. 82.
[181] *Ibid.*
[182] (1978) Q. B. 383.

insurance against theft covers jewellery which had been imported into the country with the intention of evading customs duty, it was held that, ‘’the insured could not claim indemnity from the insurer when the jewellery was stolen because, if he could, he would profit from his illegal act.’’[183]

2.1.5 The General Principles of Insurance Law in Nigeria

The fundamental Common Law doctrines of insurance are cardinal to the validity of any insurance contract. These principles are of the same efficacy worldwide, however, in Nigeria, some of these principles have been slightly modified by domestic legislation to accommodate our peculiar circumstances under the Nigerian legal framework. The Common Law principles are discussed followed by a deliberation on the local legislation of the same principles.

Contracts of insurance, as we have seen, are overseen by the universal doctrines of contract regulations[184]. However, because of their peculiar attributes, all contracts of insurance are in addition administered by distinct fundamental principles[185]. These basic principles can broadly be categorized as follows;

(a) The doctrine of *uberrimae fidei* - utmost good faith

(b) The requirement of an insurable interest.

(c) The principle of indemnity and subrogation.

[183] See Schmitthoff and Sarre, *op cit*, pp. 499-500, 513.
[184] In Nigeria there is no specific legislation like an Act governing the application of law of contract, like what obtains in Malaysia where you have the Law of Contract Act, 1950. Instead the applicable laws are those found in the Received English Laws embodied in Common law, doctrines of equity and statutes of general application that were in force in England before the 1st of January, 1900.
[185] Insurance companies are established to provide financial security to their policyholders through the pooling of premiums, out of which those who suffer losses are indemnified. The relationship between the insured and the insurer is contractual. It is, however, a contract with unique characteristics in that all the material information and circumstances of the subject matter are almost invariably within the knowledge of the insured. Since the insurer is required to bear a risk, the nature and scope which are unknown to him, he has to rely on certain developed principles that guide the parties in the insurance contract. See Banjo, B.O., (1999), *Modus International Law & Business Quarterly*, June, vol. 4, p. 73.

2.1.6 Utmost Good Faith (*Uberrimae Fidei*)

The first basic principle which lies at the root of insurance contract is the doctrine of *uberrimae fidei*, the utmost good faith. Under the general principles of contract, the basic caution is that of *caveat emptor* i.e. (buyer beware). Under this rule, the seller is not bound to make any representations to the buyer with respect to the quality of the goods, the subject matter of the transaction. Consequently, within certain limits, the contract of sale may be concluded in silence and without much exchange of information between the parties. But in contracts of insurance and a limited number of other contracts, the law insists that the assured is bound to voluntarily make disclosures of material facts of the contract within his knowledge which he is aware or ought to be aware may influence the judgement of a prudent insurer in fixing or deciding whether to take the risk, or whether to demand for a higher premium as a condition for bearing the risk. This basic doctrine of transparency and non-concealment of material facts which entails exhibiting attributes of utmost good faith *(uberrimae fidei)* by the insured is the trademark of all contracts classified *uberrimae fidei.* Nonetheless, the responsibility on the insured to make candid declarations and to make total disclosures must also be mirrored by the insurers in like manner. Correspondingly, a mutual duty on both parties to divulge all material particulars is a cardinal requirement. Concealment by either side of material particulars amounts to fraud and the aggrieved party has the option to either carry on with the insurance contract or to repudiate it. An insurance contract is rendered voidable where material facts are deliberately concealed. Since the responsibility to disclose material facts is not basically an implied condition of the contract, non-disclosure does not by itself give rise to a claim in damages; the remedy lies in the avoidance of the contract.[186]

[186] Okany, M. C., *op cit*, p. 822.

What fact is material is the same in the ordinary contract of insurance as in marine insurance. Every contextual circumstance in an insurance contract is of material importance if it would influence the judgement of a prudent insurer in fixing his premium or deciding if he will assume the risk or not.[187] What fact is material depends on what a reasonable man will consider material. If any prudent insurer will attach importance to such facts to enable him fix the premium, then those facts will be material. In contracts of life insurance, if a person has more than one insurance policy on his life, there is a duty to disclose the fact to subsequent insurers.

The insured need not disclose the following facts unless he is questioned as to such facts:

1. Facts he does not know, unless his ignorance is due to negligence[188]

2. Facts which might diminish the risk.

3. Facts within the knowledge of the insurers or facts which are waived by the insurers.

It follows, therefore, that the general responsibility to divulge all material particulars is limited to facts actually known or ought to be reasonably within the knowledge of the insured, or the insurers. It is immaterial that either party had not the intention to conceal the facts. Thus, in *Akpata and Anor. v. African Alliance Insurance Co. Ltd*,[189] the plaintiffs who were the administratrix and administrator respectively of the estate of the deceased, Dr. Richard I. Akpata, claimed from the defendant insurance company the sum of £3,000 being the amount the deceased was insured in 1965. The defendant sought to avoid payment on the insurance contract on two grounds, namely;

[187] Marine Insurance Act No. 54 of 1961. S. 20. The following are examples of the concealment of facts which have been held to be material: The fact that the ship had grounded and sprung a leak before the insurance was effected(*Russell v. Thornton(1859) 20 L.J. Ex 9);* a merchant ship on hearing that a vessel similar to his own had been captured, effected an insurance without disclosing this information(*De Costa v. Scandret (1723) 2 P. Wms.170);* the nationality of the assured concealed at a time when his nationality was important (*Associated Oil Carriers Ltd v. Union Insurance Society of Canton Ltd(1917) 2 K.B. 184);* in an insurance on a ship, the fact that the goods carried insured at value greatly exceeding their real value (*Ionides v. Pender (1874) L.R.9 Q.B. 531.*

[188] See *Joel v. Law and Crown Insurance Co.*(1908) 2 K.B. 863

[189] Suit No. LD/340/67 of 16th October 1967.

It is cases like this that have served to erode the confidence of most Nigerians about insurance. As an institution that is governed by fiduciary principles and utmost good faith. Nigerians do not understand how they can pay premium, even if it is with different insurance companies and at the end of the day end up with nothing because of technicalities. There is a serious lack of understanding about insurance and how it works. The regulators have done virtually nothing towards addressing this serious issue. The apathy bred as a result of this turns round to haunt the insurance industry.

1. The non-disclosure by the deceased that he was suffering from the ailments from which he died.

2. The deceased in answer to one of the questions in the proposal form, denied ever having previously taken out a life insurance policy with another company. However, it was later discovered that he had a policy of life insurance with the National Employers Life Assurance Company Limited in 1962 as a result of which a sum of £2,000 had since been paid.

The declaration made in the latter proposal was to be the basis of the contract of insurance contained in the policy. The defendants contended that in view of the untrue statement made by the deceased in the proposal form, the insurance contract was null and void consequently they were not under any obligation to pay any money to the estate of the deceased. In other words, the failure by the deceased to make disclosure that he had taken out a policy previously with another insurance company was material enough to avoid the contract of life insurance.

With regard to the first point, it was held that, neither the deceased nor the doctor treating him knew until after the policy had been executed that the assured was suffering or had suffered from any infirmities complained about; therefore, the contention that the deceased concealed the fact he was suffering from an ailment was not tenable.

But with regard to the second issue, the court held that non-disclosure that the deceased was previously insured with another company was fatal to the claim. According to Taylor, C.J,

> ‘’The deceased having warranted the truth of the statements in the proposal form and having agreed that they form the basis of the contract, and that all sums paid should be forfeited and the contract declared null and void if any of the statements are untrue, cannot now be heard to claim on the policy because of the

uncontested fact that the answer to one of the questions is untrue to the knowledge of the deceased.''[190]

The proposed insured, as we have seen, must make full disclosure of all material facts. It is pertinent for him, therefore, for his own good, to augment the facts specifically solicited by the insurer, if he is of the opinion there are no other relevant particulars which he needs to make available. Failure to disclose or amplify any material facts may portend that, should the insurer accept the offer and the peril insured against actually ensues, the insurance company can escape liability in the contract and are not obliged to satisfy the insured's claim.[191]

Disclosures relating to the integrity or morality of the insured can affect the risk and ultimately culminate in the evasion of the insurance contract by the insurer. Therefore, the person making the proposal is also under a duty of disclosing to the insurers all relevant particulars connected to the peril which are likely to affect the insurer's judgement, whether or not any questions are asked on the point in question.[192]

A proposal may necessitate the proposer to append his signature to a declaration in which he guarantees that the avowals he has made are sincere, and agrees that they be integrated into the contract of insurance. In other words, it is sometimes stated in the policy that the facts contained in the policy proposal form shall be the foundation of the insurance contract. In such a case, if any of the statements are untrue, whether in a

[190] See Okay, A., *op cit*, p. 322; The Marine Insurance Act, 1961 contains an up to date statement of the law on material facts as it applies to Nigeria, and it is submitted that the Nigerian courts would apply the provisions of the Act to all classes of insurance. Section 20(2) of the Act provides a description of material facts thus: ''every circumstance is material which would influence the judgement of a prudent insurer in fixing the premium, or determining whether he will take the risk''. The duty of disclosure does not extend to every fact and circumstance, but only to such facts that are material in the particular case. See *Ionides v. Pender* (1874) 10 QB 531.
Adesanya and Oloyede, *op cit*, pp. 200-201;
Schmitthoff and Sarre, *op cit*, p. 503.

[191] The duty to disclose imposed by the law is confined to facts actually known to the party on whom the duty falls. Being a duty to disclose, that is to do a positive act, no one can be expected to disclose what he does not know. Therefore, if insurers wish to avoid the policy on the ground that there has been a non-disclosure of a material fact by the insured, they must show that the insured knew or ought to have known about the existence of the material fact. See *Joel v. Law Union and Crown Insurance Company* (1908) 2 KB 863.

[192] Okany, M.C. *op cit*, p. 824.

material particular or not, the policy may be avoided by the insurers.[193] It follows, therefore, that the responses contained in a proposal form are deemed to be terms of the contract and unless they can be treated as a description of the risk, these answers are warranties the accuracy of which is of the same effect as a condition precedent to the liability of the insurance company, whether the answers are relevant to the peril or not warranties, as already stated, are thus equivalent in effect to conditions in any other type of contract.[194]

It is possible that a term of the contract may be treated by the courts not as a contractual warranty but merely as a description of the risk being covered. By implication, it means that if the statement in the proposal form is only a description of the risk, the policy can be avoided.

If there is any indistinctness in the policy or in the application form, since these documents are devised by the insurers, the courts will construe them *Contra Preferentem.* This means, in the event of any ambiguity, since it is the insurer's clause, the ambiguity will be resolved in favour of the insured.

Problems have arisen with regards to previous refusals of some insurance companies to accept the proposal of a particular individual. The law on this point is not clear as there have been various decisions by the courts for and against failure to disclose previous refusals.

Generally, a material fact is deemed to be crucial if it will influence the decision of the insurers in accepting to insure the insured and is useful in assessing the premium payable to him.[195] And the question of materiality of a fact must relate to the date which the particulars ought to have been made known to the insurers. Whether the omission to

[193] Okany, M.C. *op cit*, p. 824.
[194] See Schmitthoff and Sarre, *op cit*, p. 504, 508-509, 512-513.
[195] Section 20(2) Marine Insurance Act, 1961.

disclose any particular circumstance is material as to render the contract voidable is a matter of fact in each case.[196] The duty of the insured to disclose all material facts of which he knows continues up to the time the contract is made. Therefore, if between the period of the offer and the actual coming into effect of the contract there is a significant change of the subject of insurance, full disclosure of this change must be disclosed to the insurers else the contract becomes voidable. The duty of disclosure cannot be avoided by appointing an agent, and the insured is bound to disclose to his agent every material circumstance, unless he became aware of it belatedly for him to relay it. It is incumbent on the agent to disclose to the insurer every material context within his knowledge,[197] and he is deemed to be conversant of every contextual situation which, in the conventional circumstances of business ought to be known by or to have been relayed to him.[198]

It may be noted that many facts by their nature are deemed to be material. Such facts for example, include all facts which indicate that the liability of the insurers may be higher than in ordinary circumstances, such as previous fire incidents in the area, explosives and volatile liquids or facts which show 'moral hazards' in the sense that the insured should be given a special consideration either because of his bad habits or because he has been refused insurance on ground of his moral hazards. Most of the questions in the proposal are material and should be answered fully and not left blank. The proposal form is not exhaustive, therefore, to ensure that all material facts are disclosed, insurers have evolved a new technique whereby they incorporate a clause in the policy effectively stating that the proposed insured not only warrants the statements contained

[196] The obligation to disclose necessarily depends on the knowledge a person possesses. This summarizes the principle in its true and equitable sense. Where a person possesses no knowledge that was incumbent on him to disclose, he cannot be expected to do more. This is an indication that there is a clear limitation to the duty of the insured. See *Akpata and Anor v. African Alliance Insurance Co. Ltd*, (1969) FNLR 111.

[197] See *Woolcott v. Sun Alliance and London Alliance Ltd* (1978) 1 W.L.R. 493.

[198] The question whether an insurer is bound a disclosure made to his agent can be said to be a controversial issue, should one consider the case of *Bawden v. London Edinburgh and Glasgow Assurance Co* (1892) 2 QB 534 where information known to an insurer's agent was held to be information known to the insurer and in *Northern Assurance Co. Ltd v. Idugbo* (1966) 1 All N.C.L.R. 88., where information which came to the notice of the insurer's agent was said to be binding on the insurer. However, Section 54(3) of Insurance Act, 2003, formerly Section 1(3) of the Insurance (Special Provisions) Decree 1988 and Insurance Decree 1999, provides that a disclosure or representation made by the insured to the insurance agent shall be deemed to be a disclosure or representation to the insurer provided the agent is acting within his authority.

in the proposal to be true but that he has not withheld any information which ought to have been communicated to the insurers.[199]

This provision seems to be too wide, as it indirectly seeks to require the insured to disclose material facts which may not ordinarily be deemed by him to be necessary nor requested for by the insurers. Furthermore, failure to make such disclosure may expose the insured to the repudiation of the policy even though he was honest and acted in good faith at the time he filled the proposal form. It follows, therefore, that where there are circumstances not expressly referred to in the proposal form which may have a bearing on the decision of the insurers to undertake the risk under the policy, the insured is bound to furnish such information. However, it is consoling to state that in all classes of insurance except marine insurance, if it is made clear that what the proposer was asked to state is no more than what he believes to be the situation, then the assured will be exonerated if he believes on reasonable grounds that his statement is true.[200]

The Nigerian insurance legal framework approach to the application of doctrine of utmost good faith takes a slightly modified stance. In modifying the common law principle of utmost good faith to suit the local environment, **Section 54(1) of the Insurance Act**[201] shifted the burden of materiality of information from the insured or proposer to the insurer by requiring that all proposal forms should elicit such information considered by the insurer to be relevant. The section provides:

> ''(1) where an insurer requires an insured to complete a proposal form or other application form for insurance, the form shall be drawn up in such a manner as to elicit such information as the insurer considers material in accepting the

[199] Okany, M. C., *op cit*, p. 829.
[200] See *Century Insurance Co Ltd v. Atunanya* (1966) 2 A.U.N.L.R. 317.
[201] Section 54(1) Insurance Act, 2003. ''Where an insurer requires an insured to complete a proposal form or other application form for insurance, the form shall be drawn up inn such manner as to elicit such information as the insurer considers material in accepting the application for insurance of the risk and any information not specifically requested shall be deemed not to be material''.

application for insurance of the risk and any information not specifically requested shall be deemed not to be material

(2) The proposal form or other application form for insurance shall be printed in easily readable letters and shall state, as a note in a conspicuous place on the front page, that ‘’an insurance agent who assists an applicant to complete an application form or proposal form for insurance shall be deemed to have done so as the agent of the applicant.

(3) A disclosure or representation made by the insured to the insurance agent shall be deemed to be a disclosure or representation to the insurer provided the agent is acting within his authority.

(4) In this section, the expression ‘’insured’’ includes an applicant for insurance.’’[202]

The Nigerian insurance law requirement of the insurer to elicit such information that is deemed material to the insurance contract totally contrasts with the provisions of standard common law insurance practice. One can understand the reason for deviation by the Nigerian insurance legal framework, because the courts have been inundated with cases of insurance companies taking advantage of unsuspecting insurance clients innocently seeking legal cover only to end up being short changed by the antics of dubious insurance companies who always capitalize on technical requirements to fleece unwary clients. The level of education in Nigeria is quite low and insurance is such a technical field that even some trained lawyers find it a bit difficult to comprehend. Such sharp practices by dubious insurance underwriters have contributed in no small measure

[202] Section 54 (1)(2)(3)(4) Insurance Act 2003. These provisions are a novelty and literacy challenged countries could do well in adoption such measures to protect innocent citizens who are not literate so that rogue insurance companies do not take advantage of their educational challenges. Such dubious acts by insurance companies of relying on technicalities of non-disclosure of material facts by the insured greatly contributed to the problem of mistrust which the insurance industry is currently grappled with. As a fiduciary contract, both parties must be honest and transparent in effecting the contract. The issue of trust and transparency is not a one-sided requirement but applicable to both parties based on equity.

towards the low level patronage and stunted growth that the Nigerian insurance industry is currently enmeshed in. As a result of these unwarranted antics, most Nigerians view insurance as whole with so much derision and contempt. They don't understand it and as such do not buy into it.

2.1.7 Insurable Interest

It is normally expected that there should be the presence of insurable interest as the core subject of a contract of insurance. But it has been stated by Roche, J., in *Williams v. Baltic Insurance Association of London*[203] that ''there is nothing in the common law of England which prohibits insurance even if no interest exists.'' However, such an interest may be required by statute, or it may be demanded by the policy itself. Although its absence in the former will the render the contract null and void, its absence in the later will render it unenforceable only. The Life Assurance Act, 1774, a statute that generally applies in Nigeria, prohibits insurance made by an individual on the life of some other individual or other event, wherein the individual for whose benefit such policy is taken out has no corresponding interest. Gaming and wagering insurance contracts are also sanctioned by way of prohibition. Such insurance contracts are null and void.[204]

It is trite principle of insurance law that contracts of insurance must indicate the presence of insurable interest in the subject matter of the insurance contract otherwise the contract is of no effect whatsoever. Alternatively, insurable interest is deemed not to exist where the insured cannot positively establish the fact that he is bound to suffer adversity where the subject matter of the insurance contract is destroyed; consequently, the supposed contract of insurance is rendered invalid.[205] An insurable interest, therefore, presupposes that the insured will sustain some pecuniary loss on the demise

[203] (1942) 2 K.B.282 at 288.
[204] Section 1 of Life Assurance Act, 1774, which is a statute of general application in Nigeria.
[205] Okany, M.C., *op cit*, p. 830.

of the individual whose life a policy was taken out on.[206] Thus, in *University of Nigeria, Nsukka v. Edward Turner & Sons (W.A.) Ltd and Anor*,[207] the plaintiffs, in 1962, sought to invest a sinking fund assurance policy for an assured sum of £3 million over 50 years and requested the first defendant to make inquiries and obtain quotations from insurance companies. This, the first defendant did. After further correspondence and telephone conversations between the plaintiffs and the first defendant as to the suitability of the second defendants to undertake such a venture, the first defendant acting as plaintiff's agent secured the sinking fund policy from the second defendants as requested by the plaintiffs. After paying the first premium of £25,830 and completing the proposal form, the plaintiffs subsequently discovered that the second defendants had merely £25,000 paid up capital and £100,000 authorized capital and concluded that the second defendants could not with such negligible assets meet the assured sum when the policy ripened and therefore repudiated the policy on advice of their solicitor. They contended that the first defendant, as an expert in insurance matters, negligently or deliberately failed to disclose material information and they were subsequently induced to take out the policy. The plaintiffs, therefore, claimed:

1. The return of the deposit of £25,830 with interest thereon at 5%,

2. Damages for not disclosing material facts; and

3. Damages against the first defendants for professional negligence and for breach of undertaking.

[206] Insurable Interest gives the insured the *locus standi* (See *Adefuye v. Royal Exchange Assurance* (1962) LLR 43.) to sue as any one can only sue in respect of his own interest unless if by a special provision, the law allows it, the policy is made for the sake of another – per Phillimore, J., in *Hebdon v. West* (1803) B & 579. An insurable interest *simpliciter* is the financial interest of the insured in the event or things insured. See *Accident and Motor Insurance in West Africa* (Law and practice) Heinemann, 1991.
Strictly speaking, the definition of insurable interest as contained in the Marine Insurance Act, 1961 refers to what constitutes an insurable interest in marine adventure, but the definition does not indicate what would constitute an insurable interest in other insurance transactions. The requirement of insurable interest applies to all classes of insurance, whether the insurance is in respect of property, life, liability or contingency. See Irukwu, J., *op cit*, p. 41. See also *Lucena v. Craufurd, op cit*, p. 269, *Cooperative and Commerce Bank Ltd v. Nwokocha* (1998) 9 NWLR (pt. 564) 98 CA., *Law Union and Rock Insurance Ltd v. Livinus Onuoha* (1998) NWLR 576.

[207] (1965) L.L.R. 33.

It was held, *inter alia,* that, the contract between the plaintiff and the second defendants did not fall under a contract regarded as *uberrimae fidei* but was merely an investment without an insurance risk or insurable interest, and accordingly, the second defendants were not bound to make any disclosures to the plaintiffs as to their capital structure or assets or financial commitments.[208]

Insurance law in Nigeria, as outlined in **Section 56(1) of the Insurance Act**[209] renders a contract of insurance becomes invalidated where the insured fails to establish the presence of insurable interest in the policy of the insurance. Lawrence, J., described insurable interest as:

> ''interest in a thing to which advantage may arise or prejudice happen from the circumstances which may affect it.''[210]

The legal requirement as to when an insurable interest must exist for the contract to be valid in the eyes of the law varies with different classes of insurance. **Section 56(1) of the Insurance Act** renders a life policy void where the proposer lacks insurable interest in the life of the other party. The Section defines insurable interest in the life of another as:

> ''where he stands in any legal relationship to that person or other event in consequence of which he may benefit by the safety of that person or event or be prejudiced by the death of that person or loss from the occurrence of the event.''[211]

[208] (1965) L.L.R.33. per the court, ''the doctrine of utmost good faith has become a fundamental characteristic of insurance contracts and distinguishes insurance contracts from other contracts. In the general law of contract, the parties are bound by the common law doctrine of caveat emptor, that is, 'let the buyer beware'. Insurance contract is an exception to the doctrine. It is generally believed that the principle of utmost good faith is the distinguishing factor of insurance contracts. See Yerokun, O., (1992), Insurance Law in Nigeria, 3rd edition, Nigeria Revenue Projects Publishers, Lagos, p. 160. See also *McKenzie v. Coulson* (1869) L.R. 8 Eq. 368., London General Omnibus Co. Ltd v. Holloway (1912) 2 K.B. 72.
[209] Section 56(1) insurance Act, 2003.
[210] *Lucena v. Craufurd* (1806) 2 B & PNR 269.
[211] Section 56(2), Insurance Act, 2003.

In the Nigerian context, the definition of insurable interest as contained in the Marine Insurance Act is a good guide for understanding what constitutes insurable interest in other branches of the law even though that definition is limited to marine insurance. It is stated, thus;

> ''….every person has an insurable interest who is interested in a marine adventure. In particular, a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure or any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss or damage thereto, or by the detention thereof, or may incur liability in respect thereof.''[212]

The Marine Insurance Act[213] further requires that the insured must have interest in the subject matter that was insured at the time of the loss, though he may not have been interested when the insurance took effect.

Instructive examples of insurable interest may be found in contracts of life insurance, and it is normal in the case of life assurance that the assured has an insurable interest in his own life. Where an individual effects insurance in the life of any other individual, the name of such a beneficiary must be insured in the policy or else it will be void.[214] The value of the insurance must not be greater than the amount of the interest assured.[215]

Unquestionably, an individual has an insurable interest in his or her own life, and one spouse has insurable interest in the life of the other spouse. However, a parent has no insurable interest on his or her child except it originates from a legal pecuniary loss

[212] Section 7, Marine Insurance Act, 1961.
[213] *Ibid,* Section 8(1).
[214] Section 2 Life Assurance Act, 1774.
[215] *Ibid,* Section 3. For an interest to be insurable, it must be a pecuniary one. Sentiment cannot be the basis of an insurable interest. The interest must be one which can be enforced by legal process (See *Macaura v. Northern Assurance Co.* (1925) AC 619. The interest may be legal or equitable (See *Harse v. Pearl Assurance Co.* (1925) 1KB 588. An interest founded on moral duty is not enforceable. The interest must be real and subsisting. The hope of an interest expected to be acquired in the future, however probable, is not insurable.

which he will bear in consequence of the child's death. Similarly, a child has no insurable interest in the life of his parents, unless the parents are supporting the child.[216]

Sisters have no insurable interest in each other's lives.[217] A wife has an insurable interest in her husband's life.[218] A creditor has insurable interest in the life of his debtor for the amount of the debt, or in any of the debtor's properties over which he has a lien or, where there is a mortgage transaction he is the mortgagee of the property. The creditor or the mortgagee needs to prove the existence of an insurable interest at the time he takes out the insurance.

For the interest to constitute an insurable one, it must be such that can be enforced or protected by the law.[219] A duty founded on morality is not insurable.

An agent, without any semblance of interest, may, however, enter into a valid and enforceable contract on behalf of his principal in respect of a property on which the latter has an insurable interest. Either the principal or the agent can sue on such a contract.

A seller who remains in possession of goods after the property in the goods has passed to the purchaser has no interest but may make an insurance covering the buyer's interest. He thereby becomes an agent by implication or necessity of the buyer.[220]

2.1.8 The Principle of Indemnity

The principle of indemnity lies at the root of the law of insurance, except in the case of life and personal accident. As stated earlier in the chapter, there are two types of insurance, namely:

[216] See *Howard v. Refuge Friendly Society*(1886) 54 L.T. 264
[217] See *Evanson v. Crooks*(1911) 106 L.T. 264.
[218] *Reed v. Royal Exchange* (1795) p. Add Cas. 70. See also Married Women Property Act, 1882, Married Women's Property law, Cap. 76 of Western Region of Nigeria. See also *Griffiths v. Fleming* (1909) 1KB 805, where it was held that it is now settled law that a husband has an insurable interest in the life of his wife. But a fiancé has no insurable interest in the life of his intended bride.
[219] Per Edozie, JCA, in *Law Union & Rock Insurance Co. Ltd v. Onuoha* (1998) 6NWLR Part 555, p. 576 at p. 590.
[220] Okany, M.C., *op cit*, p. 834.

1. Indemnity insurance; and

2. Contingency insurance, i.e. insurance contracts in respect of life and personal accident.[221]

With regard to contracts of insurance of life and accident, the insurers simply undertake to pay a certain stipulated sum of money in the event of death or personal accident. Life assurance, therefore, presupposes a payment of a sum certain on the occurrence of the risk insured against, and the amount for which a life policy is taken or valued is at the option of the assured.[222]

In contracts of indemnity, on the other hand, such as fire or marine insurance, it is a fundamental principle that where the insured risk occurs, the assured cannot be indemnified more than the actual loss he suffered within the limits of his policy. This is referred to as the principle of indemnity. Under this principle, it is illegal for the insured to be indemnified in excess of the value of his actual financial loss because the dictates of public policy frown on the insured making a profit over and above the amount of his actual loss. In other words, indemnity claims entail a claim for unliquidated damages. This presupposes that the claim cannot surpass the value of the sum insured. Therefore, the assured is not allowed to benefit excessively and unfairly out of the contract of insurance.[223] The principle of indemnity, within reasonable bounds, helps to check the malpractices of under insuring properties and of making fantastic profits from the transaction. If, for example, the insured has by some contractual arrangement reduced the actual loss to be recovered from the insurers, the amount of this reduction will be taken into consideration in determining the extent of the loss payable by the insurers.

[221] *Dalby v. India and London Assurance Co.* (1854) 15 CB. 365; of course, it is virtually impossible to restore the assured back to life in life assurances or to restore the insured's blinded eye back to normal in personal accident insurances. In these instances, the principle of indemnity does not apply. There can only be a claim for the insurance money on the happening of these events by the insured.
[222] Okany, M.C., *op cit*, p. 835.
[223] *Ibid.*

Thus in *Castellain v. Preston,*[224] ‘’a vendor contracted with a purchaser for the sale of a house, which he had insured against fire, although the policy was not assigned to the purchaser. After arranging for the contract of sale but before the contract of sale was actually completed, which contained no reference to the insurance, the house was damaged by fire. The insurance company paid the insured the amount of the loss occasioned by the fire. The insurance company claimed a refund of the amount they had paid in respect of the fire’’.

It was held that, the insurance company was entitled to recover, for since the insured had been fully paid by the purchaser without any deduction with regard to fire, he had suffered no loss as a result of the fire.’’[225]

The decision in the above case emphasizes the foundation of contract of indemnity which is that the insured under a contract is entitled to be indemnified only for the loss suffered. If the insured is permitted to receive any amount in excess of his actual loss, that would defeat the fundamental principle of insurance law.[226]

On general principles, an insured is entitled to claim the full cost of repairs in the case of partial loss, provided it comes within the total amount covered by the policy, so that the insured may feel adequately protected although the policy is under insured, since total loss is rare.[227] If, however, the policy contains a ‘subject to average’ clause, and the property is under insured, the insurers are liable only for the proportion of the actual loss which the amount insured reflects to the value of the subject matter. The phrase

[224] (1883) Q.B.D. 380.
[225](1883) Q.B.D. 380..
[226] Okany, M.C., *op cit*, p. 836. It is in the overall interest of the public that an insured should be forbidden from making a profit from what is, essentially, a misfortune. If the insured was allowed to gain by the loss or destruction of his insured property, he would be tempted to destroy it, and if the temptation to destroy is succumbed to, this would be injurious to the interest of the public generally. See Irukwu, J.O., (1971), *Insurance Law and Practice in Nigeria*, Sweet & Maxwell, London, p. 54.
[227] See *Fifth Liverpool Starr Bowkett Building Society v. Travellers Accident Insurance Co Ltd.* (1883) 9 T.L.R. 221.

'subject to average' is a stratagem to curtail the liability of the insurer and to discourage the insured from making an unfair gain out of the insurance policy.[228]

In the Nigerian legal system, this fundamental principle of indemnity has been re-enacted by local insurance legislation.[229] It states that in the event of a loss arising from the insured's peril, the insured shall be returned to the exact financial position that he was prior to the occurrence of the peril insured against. The Nigerian law equally hinges the principle of indemnity on the proverbial interest stance that the insured should not make profit from his misfortune. It is also assumed that if the insured were to profit from the loss or damage of the subject matter, he would be tempted to destroy the property and if the temptation to do so is condoned, it would be injurious to the public interest, generally.

Furthermore, on breach of material terms, Section 55(3) of the Insurance Act provides that;

> ''Where there is a breach of a material term of a contract of insurance and the insured makes a claim against the insurer and the insurer is not entitled to repudiate the whole or any part of the contract, the insurer shall be liable to indemnify the insured only to the extent of the loss which would have been suffered if there was no breach of the term.''[230]

2.1.9 Subrogation

Subrogation principle is closely tied to that of indemnity. The rule is that the insured cannot unfairly profit in excess out of the insurance. However, for the purpose of furthering the principle of indemnity that the insured should recover no more than his actual loss, the courts have adopted the doctrine of subrogation. Under the principle of

[228] Okany, M.C. *op cit*, p. 836.
[229] Section 55(3) Insurance Act, 2003.
[230] *Ibid.*

subrogation, the insurers who have paid the insured his entitlements under a contract of indemnity will be placed in the position of the insured; consequently, the insurers will be entitled to maintain actions in the name of the insured for recovering any money payable to the insured under the risk they had undertaken. Thus, as expressed by Brett, L. J., in *Castellain v. Preston,*[231] the effect of the doctrine is that:

> ''…between the underwriters and the assured the underwriter is entitled to the advantage of every right of the assured, whether such right consists in contract, fulfilled or unfulfilled, or in remedy for tort capable of being insisted on or already insisted on, or in any other right, whether by way of condition or otherwise, legal or equitable, which can be, or has been exercised or has accrued, and whether such right could or could not be enforced by the insurer in the name of the assured by the exercise or acquiring of which right or condition the loss against which the assured is insured, can be, or has been, diminished.''[232]

It is evident that the doctrine of subrogation was put in place to enable insurance to remain purely a contract of indemnity. By the application of the doctrine of subrogation, a court of equity will inhibit the assured from profiting unfairly from his misfortune. Also, if the assured deliberately refuses to pursue his entitlement against the third party, then the insurance company can sue the third party to recover, after satisfying the assured, thus stepping into the insured's shoes.

[231] (1893) 11 Q.B.D., 380 at p. 387. See also *Meacock v. Bryant and Co.* (1942) 2 All E.R. 661. The doctrine of subrogation comes into operation if after, the satisfaction of the claim out of the insurance money, the insured obtains additional compensation from a third party, he must hold such money as a trust for his insurers. The doctrine of subrogation arises in all policies which are contracts of indemnity including marine insurance. See also *John Edwards & Co. v. Motor Union Insurance Co. Ltd.* (1922) K.B. 249. See also *Chellarams and Sons (Nig.) Ltd v. The Nigeria National Shipping Line Ltd* (1974) E.C.H.C.J/3/74. See also *Yorkshire Insurance Co. Ltd v. Nisbet Shipping Co. Ltd.* (1962) 2 Q.B.D. 330. See BOAG v. Standard Marine Insurance Co. Ltd (1971) 2 K.B. 113. See St Johns 101Fed. R. 469 (1900). The Livingstone 130.R. (1904). The right of subrogation may be claimed even where the insured has no right of action, especially where it is incidental to the subject, such as gift, or for the recovery of salvage. See *Sun Insurance v. Hadden* (1884) 13 Q.B.D. 706.

[232] *Ibid.*

It should be noted that the doctrine of subrogation applies to those insurance contracts which are classified as contracts of indemnity, for example, fire, motor and contingency insurance covering non-payment of money, but not life or personal accident insurance. Subrogation applies to rights both in contract and in tort, and if the assured renounces any benefits or rights of action against third parties, the insurer is discharged to that extent.[233]

2.1.10 Proximate Cause

The *Causa Proxima* rule is part of the fundamental principles of insurance applicable in Common Law. It presupposes that the insurer would only be liable in an insurance contract if the insured peril is the proximate cause of the loss or damage occasioned. The principle of *causa proxima non remota spectatur* entails that the proximate cause should not necessarily be the latest cause, but the direct, dominant, effective and efficient cause of the loss or damage. The rule is that only loss or damage which has been proximately caused by an underwritten risk is recoverable under the relevant policy. It is therefore not enough for the insured to establish that loss falls within the cover provided by the policy.[234]

[233] Okay, M.C., *op cit* p. 840. Though subrogation is vested in the insurers after they have paid the claims made against them, by the insured not before, however, in recent times, a practice has developed whereby a clause or condition embodied in all non-marine policies provides that the insurer may exercise his subrogation right before payment has been made. The effect of this clause is to modify the common law doctrine of subrogation to the extent that the insurers may be subrogated to the insured's rights and remedies before payment is made. This in effect prevents the insured from waiving or compromising his rights against third parties having been indemnified by the insurers. This clause is however against the provision of the Marine Insurance Act, 1961 on subrogation as it provides that the insurer's subrogation right arises only after indemnifying the insured.

[234] Adamu, A.I., (2013) *Challenges of Integrating Takaful (Islamic Insurance) Within Legal and Regulatory Framework of Insurance in Nigeria (*Unpublished LL.M Thesis), p. 50. Thus, a loss may be as a result of some combination of a number of causes, but for the purpose of insurance law, the direct or dominant cause must be identified as the cause. In effect, the proximate cause may not be the first, the last or the sole cause of the loss; it must be the dominant, effective or operative cause of the loss. See *Samuel v. Pumas* (1923) 1Ks, 592; (1924) A.C. 431. See also *Leyland Shipping Co. v. Norwich Union Fire Insurance Society* (1918) A.C. 350; *Yorkshire Dale S.S. Co. v. Minister of War Transport* (1942) A.C. 691. In insurance policies, as in all commercial documents of similar nature, the proximate rule depends on the presumed intention of the parties. See *Becker Gray v. London Assurance* (1918) A.C. 101, 112, per Lord Sumner. See also *Samuel v. Pumas* (*supra*). See *Pawsey v. Scottish Union & National Insurance Co.* (1908) reported in 'The Times'' of October the 17th, 1908. See *Smith v. Cornhill Insurance Co. Ltd.* (1936) 54 T.L.R. 869. See also *Marsden v. City Country Assurance Co.* (1886) L.R. 1CP 282. See also the Nigerian case of *Phoenix Assurance Ltd v. Olabode* (1968) 2 All Comm. 7. See *Salmon Contractors v. Monksfield* (1970) 1 Lloyd's Rep. 387.

2.1.11. Conditions and Warranties

The insurance policy is the document that embodies the terms and conditions of a particular insurance contract. It is the written evidence of the contract and contains several terms, conditions and warranties which define obligations as well as description of the risk covered. The contract, evidenced by the policy, contains different types of terms and conditions.

The conditions contained in every policy may be express or implied. However, the nature of these conditions will be dictated by the type of insurance involved. The express conditions will include provisions for immediate report of accidents (or loss as the case may be) to the insurers or police, duty and precautionary measures to be adopted by the insured, the procedure for making claims and reference of disputes under the policy to arbitration.

The implied conditions comprise what may be described as the fundamental principles of insurance, which would always be implied in every contract of insurance, whether or not the parties spelt it out. These include the principles of *Uberrimae Fidei*, insurable interest, indemnity and subrogation.

Non-compliance with any term which is stated in the policy to be a condition precedent to liability will prevent the assured from recovering under the policy.[235]

As earlier on stated, policies of insurance contain the terms of the contract and it is always a matter of construction whether the terms are conditions or warranties. However, with regard to insurance contracts, the legal effects of both conditions and warranties are the same, because in a contract of insurance, a warranty corresponds to a condition, so that the breach of either, entitles the aggrieved party to avoid the

[235] See Okay, A., *op cit*, p. 320, Schmitthoff and Sarre, *op cit*, p. 285.

contract.[236] Thus, in *Jia Enterprises (Electrical) Ltd v. British Commonwealth Insurance Company Ltd,*[237] the plaintiff who was a manufacturer of accumulator batteries, plastic records and electrical goods, claimed the sum of £22,450 from the defendants, a firm of insurers, on properties which were destroyed or damaged by fire in 1958. The defendants refused to accept responsibility on the ground that the plaintiff was in breach of the terms of the policy in failing to provide on the premises the number of fire extinguishers required by the policy and in not keeping the records of the company in a fire-proof safe.

It was held that, the failure to observe the terms of the policy was a breach of condition, the effect of which relieved the insurers from liability.

Similarly, in *Malik Matar v. Norwich Union Fire Insurance & Others*[238], ''the appellant took out a policy for a sum of £4,000 against loss by theft following upon actual forcible and violent entry or damage by thieves in respect of goods and other property in a shop at 73, Broad Street, Lagos, Nigeria. Attached to the policy was a 'Documentary Evidence Warranty' which warranted that during the subsistence of this insurance contract, the assured must keep a complete set of books of accounts and stock sheets showing a true and accurate record of all business transactions and stock in hand, and that the stock books must be locked in a fire-proof safe or removed to another building at night. These warranties were breached by the appellant. Thieves broke in and stole a quantity of goods valued at £3,000 and covered by the insurance.

It was held by the Supreme Court of Nigeria that, failure to keep the books as had been undertaken was a breach of warranty and therefore the appellant could not recover.''[239]

[236] Okany, M.C., *op it*, p. 821.
[237] (1965) N.M.L.R. 147.
[238] Suit No. FSC.217/63/19 of 1963.
[239] Suit No. FSC.217/63/19 of 1963.

However, if there is no breach of condition or warranty by the assured, he will be eligible to recover from the insurance company according to the terms of the policy. Thus, in *Nicholas Brothers Co. v. Lion Of Africa Insurance Co. Ltd*,[240] the defendants undertook to insure the plaintiffs' car in consideration of a premium. The policy of insurance contained a clause giving the defendants the option-

1. To repair and reinstate;

2. To replace the motor car;

3. To pay in cash the amount of the loss or damage up to the value of the insured car. The car was damaged and the defendants elected to exercise their option to repair and reinstate it. The plaintiffs were dissatisfied with the condition of the car which, after the repairs, was valued at $300 less than its pre-accident value. The defendants sought to rely on the clause giving them an option to repair and reinstate.

It was held that, by failing to restore the car to its pre-accident state and condition, the defendants had not discharged their obligations, and the plaintiffs were eligible to recoup the insured worth of the car.[241]

In the current Nigerian context, the Insurance Act,[242] provides

> ''where an insurer requires an insured to complete a proposal form or other application forms for insurance, the form shall be drawn up in such manner as to elicit such information as the insurer considers material in accepting the application of the risk and any information not specifically requested shall be deemed not to be material.''[243]

[240] (1961) L.L.R. 86.
[241] See Adesanya and Oloyede, *op cit*, pp. 193-194.
[242] Section 54, Insurance Act, 2003. LFN.
[243] Section 54, Insurance Act, 2003. LFN..

However, Section 55[244] narrows the effect of any term whether referred to as a condition or warranty:-

> ''in a contract of insurance, a breach of a term called warranty or a condition shall not give rise to any right by or afford a defence to the insurer against insured unless the term is material and relevant to the risk insured against.''[245]

2.2 NIGERIAN INSURANCE LEGISLATION

The practice of insurance in Nigeria is not shaped by the principles of Common Law only. In addition to these fundamental principles of insurance as encased in Common law doctrines, the insurance legal framework in Nigeria has developed a plethora of statutes and legislations to compliment the Common law principles of insurance. These statutes and legislations, no doubt, have contributed in no small measure towards the evolution and growth of the insurance industry in Nigeria. Nigerian legislation comprises of statutes and subordinate regulation. Statutes are laws legislated by the legislature – the legislative arm of government. Subordinate legislation is law promulgated in the application of powers granted by a statute. It is also known as subsidiary instrument or delegated legislation. It consists of rules, orders, regulations, bye-laws and other instruments made under the authority of statutes. Examples of subordinate legislation are rules, orders, and guidelines made by Ministers, Commissioners and Chief Justices. A statute is usually referred to as the principal law in a later statute amending it. A statute under which subsidiary legislation is made is referred to as an enabling statute.[246] Legislation is the most important instrument of legal development. It has a tremendous effect on all the other sources of law. It can

[244] Section 54, Insurance Act, 2003. LFN..
[245] *Ibid.* The provisions of Sections 54 and 55 of the Insurance Act, 2003 are novel and commendable having taken into consideration the peculiar circumstances of the background of Nigerian insurers who have poor literacy and awareness culture. The onus lies more with the insurers to elicit material information that will help them arrive at acceptable proportions for them to accept to insure the risk. The hitherto dishonest reliance on technicalities to avoid settling genuine claims has been considerably narrowed by the proactive provisions of those two sections in the Insurance Act.
[246] Obilade, A. O., *op cit*, p. 64.

readily alter their content. It is also a useful tool for the social, economic and technological development of the country.[247] Some of the most pertinent statutes on insurance in Nigeria are discussed below.

2.2.1 The Insurance Act 2003[248]

Insurance is an element on the exclusive jurisdictive list in the Constitution of the Federal Republic of Nigeria.[249] This means, it is only the Federal legislative authority or the National Assembly that can make laws on the subject.[250] Thus, where the provisions in a legislation appear to be inconsistent with those of the Constitution, such legislation will be rendered void to the extent of the inconsistency. It is instructive to note that these legislations derive their origins from the Constitution which is the grundnorm.[251]

The Insurance Act, 2003, is the current subsisting legislation regulating all the operations of the Nigerian insurance industry today. The Act repealed all previous legislations made on insurance like the 1961 Insurance Act and the subsequent Decrees that were promulgated by the erstwhile military rulers. All the previous legislations have now been streamlined and coded into the new Insurance Act, 2003. This new Act introduced radical provisions to improve market discipline and viability of insurance institutions. It repealed some contentious provisions[252] in previous legislation contained in the 1997 Decree while some of those previous legislations were simply re-enacted, especially those of the pioneering Insurance Act, 1961.

[247] Obilade, A. O., *op cit*, p. 64.
[248] Laws of the Federation of Nigeria (LFN). The Act is the single most important piece of legislation determining if and how the bulk of insurance can be conducted in Nigeria. The Insurance Act 2003 is the evolution of Decree No. 59 of 1976, which constituted the first all-embracing insurance legislation in Nigeria by putting together the provisions of the various previous laws. The Act covers a great deal of detail from specific licensing requirements such as minimum capital, to supervisory reporting and corrective measures. By establishing such requirements in law, it gives little flexibility for NAICOM to create supplementary legislation. Hence NAICOM has issued very limited number of Guidelines. It should be noted that Guidelines are not the same as regulations although the words are sometimes used interchangeably. Regulations are a prerogative of the Federal Ministry of Finance, the parent Ministry of NAICOM.
[249] 1999 Constitution.
[250] Second schedule (legislative powers) Constitution of the Federal Republic of Nigeria 1999.
[251] According to Hans Kelson, the Law from which all other laws get their source or origin.
[252] See Section 99 of the Insurance Act, 2003 which repealed Section 4 of NICON Act, 1969 and the Nigerian Reinsurance Corporation Act, 1997, which placed the responsibility of insuring government's assets in NICON Insurance Plc and Nigerian Re.

The Act, as the primary legislation for regulating insurance business in Nigeria, is meant to among other things provide enhanced supervision and regulation of the insurance industry.[253] However, in spite of all the commendable giant steps taken in the provisions of the Act to bring Nigerian insurance practice at par with world standards, this thesis submits that certain pitfalls or gaps have been identified which need to be harmonized with other insurance regulatory instruments like the recently released *Takaful* Operational Guidelines. It is noticed that in the delineating section of its scope, the application of the Act is ‘’restricted to insurance business and insurers, other than the insurance business carried on by friendly society or company or persons established outside Nigeria to engage solely in reinsurance business.’’[254] Similarly, the Act does not expressly cater for the business of Islamic insurance or *Takaful* in the entirety of its provisions. Considering the recent trending of Islamic finance and its global acceptance as an adjunct of conventional insurance, the study posits that the Act should have expressly catered for this new phenomenon, instead it chose to allude to it by inference. This regulatory ambiguity is bound to pose some considerable challenges in the course of implementing the newly introduced guidelines on *Takaful* insurance by NAICOM. That is the premise of the study.

Some key provisions of the insurance Act, 2003 are discussed below:[255]

In pursuance of the provisions of the current Insurance Act, ‘’every company wishing establish an insurance business in Nigeria must first be incorporated as a limited

[253] Insurance Act, 2003.
[254] See Section 1 of the Insurance Act, 2003.
[255] The key provisions of the Insurance Act, 2003 discussed here are meant to highlight the evolution of conventional insurance legislation and the subsequent attempt to sanitize the Nigerian insurance industry. The provisions are self-evident and their meanings unambiguous. Some of the provisions were novel because they showed how legislation in the insurance industry had metamorphosed in the quest to provide a level playing field and build trust and confidence in the industry. The main thrust of the provisions was for ample customer and insurance players protection. Yet the challenges persisted.

liability company,''[256] ''or a body duly established by or pursuant to any other enactment to transact the business of insurance or reinsurance.''[257]

The Insurance Act makes it mandatory that ''no insurer shall commence business unless the insurer is registered by the Commission under this Act.''[258] ''The application for registration as an insurer is made to the Commission in the prescribed form and be accompanied by a business plan and other such documents or information as the Commission may from time to time direct or require.''[259]

Before an applicant is registered as an insurer by the Commission, the Commissioner must be satisfied as to all of the following matters namely:-

1. ''the class or category of insurance business shall be conducted in accordance with sound insurance principles;''[260]

2. ''the applicant being one of the persons referred to under Section 3 of the Act is duly established under the applicable law and has a paid up share capital and statutory deposit as specified in Section 9 of this Act for the relevant class of insurance business.''[261]

3. ''the arrangements relating to reinsurance treaties in respect of the class or category of insurance business to be transacted are adequate and valid;''[262]

4. ''the proposal forms, terms and conditions of policies are in order and acceptable;''[263]

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[256] The issue of incorporation under the Companies and Allied Matters Act, 1990 before an insurance company is considered for registration has generated so much controversy by virtue of the provisions of Section 100 of the Insurance 2003. The Section affirms supremacy in any matter in this regard which is inconsistent with the provisions of the Act in relation to insurance. The supremacy is extended to any other enactment not consistent with the Insurance Act. This is bound to come into conflict with the provisions of *Takaful* Guidelines 2013 because *Takaful* is quite different from conventional insurance in form and substance. In some other jurisdictions like Malaysia, the *Takaful* provisions completely insulate its application from those of the Financial Services Act, 2013, thus, guaranteeing regulatory certainty in *Takaful* application. This is the line Nigeria must toe. Details are elaborately discussed in the fifth chapter of this study.

[257] Section 3 of the Insurance Act, 2003 provides that: No person shall commence business or carry on any class of insurance business in Nigeria except:-
(a) a company duly incorporated as a limited liability company under the Companies and Allied Matters Act, 1990; or
(b) a body duly established by or pursuant to any other enactment to transact the business of insurance or reinsurance.

[258] Section 4(1) Insurance Act, 2003.

[259] Section 5(1) Insurance Act, 2003.

[260] Section 6(1)(a) *Ibid.*

[261] Section 6(1)(b) Insurance Act 2003.

[262] Section 6(1)(c) Insurance Act 2003..

5. ‘’there shall be such competent and professionally qualified persons as may be determined from time to time by the Commission to manage the company;’’[264]

6. ‘’the applicant does not have in its employment a person disqualified from being appointed by an insurer under Section 12 of this Act;’’[265]

7. ‘’the directors have attended the promoters’ interview and are persons who have not been involved in or found guilty of fraud;’’[266]

8. ‘’the name of the applicant is not likely to be mistaken for the name of any other insurer who is or has been an insurer or so nearly resembling that name, as to be calculated to deceive;’’[267]

9. ‘’the applicant has paid the fee prescribed for registration;’’[268]

10. ‘’it is in the interest of public policy that the applicant be registered;’’[269]

11. ‘’where the class of insurance is other than life insurance business, the applicant is for the purposes of transacting not less than three classes of insurance business;’’[270]

12. ‘’the applicant has a satisfactory business plan and feasibility study of the insurance business to be transacted within the next five succeeding years from the date of the application;’’[271] and

13. ‘’in the case of reinsurance business, that in addition to the matters referred to in this section, it has complied with Section 9(1)(d) of this Act and any other conditions which may be specified from time to time by the Commission;’’[272]

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[263] Section 6(1)(d) *Ibid.*
[264] Section 6(1)(e) *Ibid.* This is one area the Nigerian insurance industry has been suffering from-the dearth of technical expertise. This problem is even more pronounced in relation to *Takaful* application because the industry is just growing and most experts are drawn from conventional insurance practice.
[265] Section 6(1)(f) Insurance Act 2003.
[266] Section 6(1)(g) *Ibid.*
[267] Section 6(1)(h) *Ibid.*
[268] Section 6(1)(i) *Ibid.*
[269] Section 6(1)(j) *Ibid.*
[270] Section 6(1)(k) Insurance Act, 2003.
[271] Section 6(1)(l) Insurance Act 2003

‘’The Commission shall if satisfied, register the applicant as an insurer and issue to the applicant a certificate of registration.’’[273]

‘’Notice of the registration of an applicant as an insurer and under Section 7(6) of this Act be published in the Gazette or in such other manner.’’[274]

‘’Where the Commission is not satisfied, it shall give notice in writing to the applicant within sixty days of the submission of the application of the Commission’s intention to reject the application.’’[275]

‘’Any applicant aggrieved by the intention of the Commission to reject an application for registration as an insurer may within thirty days after the notice of the Commission’s intention to reject application, appeal to the Minister of Finance.’’[276]

2.2.2 Cancellation of Registration

The Insurance Act provides that:-

(1) ‘’If, in the case of a registered insurer, the Commission is satisfied that –

(a) ‘’the class of insurance business of the insurer is not being conducted in accordance with sound insurance principles;’’[277]

(b) ‘’the insurer has failed to satisfy the margin of solvency as contained in Section 24 of the Act;’’[278]

(c) ‘’the insurer has ceased to carry on business of the class or category assigned to it for at least one year in Nigeria;’’[279]

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[272] Section 6(1)(m) *Ibid.*
[273] Section 6(2) Insurance Act 2003.
[274] Section 6(3) Insurance Act 2003.
[275] Section 7(1) *Ibid*.
[276] Section 7(2) *Ibid*.
[277] Section 8(1)(a) *Ibid.*
[278] Section 8(1)(b) *Ibid.*
[279] Section 8(1)(c) *Ibid.*

(d) ‘’the insurer has applied in writing for the cancellation of its registration as an insurer;’’[280]

(e) ‘’a judgement obtained from a court of competent jurisdiction in Nigeria against the insurer remains unsatisfied for ninety days and there is no appeal pending against the judgement;’’[281]

(f) ‘’the insurer is carrying on simultaneously the insurance business and any other business which is detrimental to the insurance business of the insurer;’’[282]

(g) ‘’subject to Part V of this Act, the insurer has transferred to or amalgamated with the business of any other insurer;’’[283]

(h) ‘’the insurer has refused to submit to an examination of its books as provided for in the Act;’’[284]

(i) ‘’the insurer has failed to comply with the provisions of Section 26 of this Act;’’[285]

(j) ‘’the insurer has failed to maintain adequate reinsurance arrangements and treaties in respect of the classes or category of insurance business the insurer is authorized to transact;’’[286]

(k) ‘’subject to subsection 5 of this Section, the insurer lacks the necessary expertise by virtue of a substantial reduction in the number of qualified employees;’’[287]

(l) ‘’the net asset of the insurer is below the minimum paid-up capital and the capital injections have not been made within the time stipulated by the Commission;’’[288]

[280] Section 8(1)(d) *Ibid*.
[281] Section 8(1)(e) Insurance Act 2003.
[282] Section 8(1)(f) *Ibid.*
[283] Section 8(1)(g) *Ibid*.
[284] Section 8(1)(h) *Ibid*.
[285] Section 8(1)(i) *Ibid.*
[286] Section 8(1)(j) *Ibid*.
[287] Section 8(1)(k) *Ibid*.
[288] Section 8(1)(l) *Ibid.*

(m) ‘’the Commission has received and verified not less than five complaints of failure to pay claims promptly;’’[289]

(n) ‘’the insurer has failed to set up the special reserves and provisions as prescribed under Sections 20 to 22 of this Act;’’[290]

(o) ‘’the insurer acts in any manner without the approval of the Commission in cases where this Act requires such approval;’’[291]

(p) ‘’the insurer has been wound-up or otherwise dissolved or has gone into liquidation;’’[292]

(q) ‘’the insurer, in the case of a reinsurance company has failed to satisfy the provisions of Section 23 of this Act.’’[293]

‘’The Commission shall give notice in writing to the insurer of the Commission’s intention to cancel the registration of the insurer in respect of a particular class or both classes of insurance business, as the case may be, and the provisions of Section 7 of this Act shall apply to any such notice as if it were a notice to reject an application for registration.’’[294]

‘’Where no appeal is lodged as provided for under Section 7 of this Act, the Commission shall, with the approval of the Governing Board cancel the registration of the insurer and notice of such cancellation shall be published in the Gazette.’’[295]

[289] Section 8(1)(m) *Ibid.* This is one provision which if implemented with all seriousness will lead to the revival of trust in the insurance industry. The claims ratio in Nigerian insurance industry is quite low when compared to other countries, including African countries. Most insurers don’t want to pay up even where the claims have been certified genuine. In developed economies, the norm for property and casualty products is a claims ratio in the range of 60-95%, depending on the product and distribution channel. In Nigeria, EFInA Survey, 2013 states that corporate claims ratios could reach 40% while the ratio for individual policies may be about 3%. Definitely, the Nigerian insurance industry needs a shift in its understanding of insurance business, particularly retail insurance. A higher rate of claims payments could improve customer perception and public confidence, two pre-conditions for market development. Clients need to be certain that their claims will be paid.
[290] Section 8(1)(n) Insurance Act 2003.
[291] Section 8(1)(o) *Ibid*.
[292] Section 8(1)(p) *Ibid*.
[293] Section 8(1)(q) *Ibid*.
[294] Section 8(3) *Ibid*
[295] Section 8(4) *Ibid*.

‘’Where a certificate of registration of an insurer is cancelled, the insurer shall forthwith discontinue acceptance of any new business –

(a) within twelve months from the date of cancellation, in the case of the reinsurance business in accordance with the provisions of Section 82 of this Act; and

(b) in all cases, the Commission may act as a receiver from the date of cancellation in accordance with the provisions of this Act, may appoint any person to act on his behalf.’’[296]

2.2.3 Requirement of Minimum Paid-up Share Capital[297]

For purposes of eliminating ‘mushroom’ insurers and allaying the fears of the general public towards the insurance industry, a higher minimum paid up capital has been imposed on insurers by the Act. Every insurer who intends to embark on insurance business must maintain a minimum paid-up share capital.[298]

Section 9(1) of the Insurance Act stipulates that ‘’every person intending to carry out insurance business in Nigeria shall deposit the share capital, (hereinafter called the statutory deposit) with the Central Bank of Nigeria (CBN), and the statutory deposit shall remain with the Central Bank while the insurer is lawfully carrying on business in Nigeria’’.

[296] Section 8(6) Insurance Act 2003.

[298] Section 9 *Ibid*. The recapitalization requirement now stands at N3 billion for Non-Life insurance and N5 billion for Life insurance business. This has led to the shrinking of companies from 109 to just 59 and 2 reinsurers according to NAICOM.
Part of the explanation for such high minimum capital levels is that the Insurance Act does not allow NIACOM to use a risk-based capital regime (as well as risk-based supervision), in which a lower flat regulatory capital could be better adjusted on an on-going basis by solvency requirements related to the operational size and complexity of different providers, in line with international best practices (See Insurance Core principles 4 (Licensing) and 17 (Capital Adequacy). Hence, in its laudable effort to sanitize and consolidate the sector, NAICOM has opted to set a high flat minimum capital, which stands out in the region and even globally. See Dias, D., et al, *op cit* p. 56.
Another serious controversy that has to do with the minimum paid-up capital is in relation to *Takaful* insurance. NAICOM, in the Guidelines lowered the minimum capital requirement for a *Takaful* operator to accommodate *Takaful*. However, the Provisions of Section 9(4) of the Insurance Act expressly state that the power to review minimum paid-up capital is upward and not downward. This is discussed in greater detail in the fifth chapter of the study.

2.2.4 Keeping of Books and Records

Control over the affairs of the insurance industry is further effected by the strict provision for keeping and maintaining of a variety of books and records. ‘’Every insurer must keep and maintain at its principal office, books and records which should include the memorandum and its articles of association or other evidence of the constitution of the insurer;’’[299] ‘’a record containing the names and addresses of the owners of the insurance business whether known as or called shareholders or otherwise;’’[300] ‘’the minutes of any meetings of such owners and of the policy-making executives (whether known as the Board of Directors or otherwise);’’[301] ‘’register of all policies in which shall be entered in respect of every policy issued, the names and address of the policyholder, the date when the policy was effected and a record or any transfer, assignment or nomination of which the insurer has notice.’’[302] ‘’The insurer shall also keep a register of claims;’’[303] ‘’a register of investments.’’[304] ‘’a register of assets;’’[305] ‘’a register of reinsurance ceded;’’[306] ‘’a cash book;’’[307] ‘’a current accounts book;’’[308] ‘’a register of open policies in respect of marine insurance transactions;’’[309] and ‘’management report by external auditors.’’[310] ‘’With regard to life insurance business, the insurer shall keep other books in addition those already mentioned above. These include separate registers of insured under group policies, of loans and policies, of cash surrender values and of lapsed and expired policies.’’[311]

[299] Section 17(1)(a) Insurance Act, 2003. The regulatory reporting regime today is so complex that it is difficult to form a complete picture of what a licensed insurer needs to report regularly to NAICOM. For the purpose of improving insurance regulations for all insurers, the study proposes a more streamlined, simplified reporting regime which will even make supervision much easier.
[300] Section 17(1)(b) *Ibid.*
[301] Section 17(1)(c) *Ibid.*
[302] Section 17(1)(d) *Ibid*.
[303] Section 17(1)(e) *Ibid.*
[304] Section 17(1)(f) *Ibid.*
[305] Section 17(1)(g) *Ibid.*
[306] Section 17(1)(h) *Ibid.*
[307] Section 17(1)(i) *Ibid.*
[308] Section 17(1)(j) *Ibid.*
[309] Section 17(1)(k) *Ibid*.
[310] Section 17(1)(l) *Ibid.*
[311] Section 17(2) *Ibid*.

2.2.5 Separation of Accounts and Reserve Funds[312]

There is also a provision in the Insurance Act that ‘’where an insurer carries on both classes of insurance business, all receipts of each of those classes of insurance business shall be entered in a separate and distinct account and shall be carried to and from a separate insurance fund with the appropriate name so that in case of life insurance there shall be –

(a) the individual life insurance business fund;’’[313]

(b) ‘’the group life insurance business and pension fund;[314] and

(c) ‘’health insurance business.’’[315]

2.2.6 Insurance Agents[316] and Brokers[317]

New provisions in relation to insurance agents and brokers were introduced by Sections 34 and 36 of the Act. The sections stipulate that ‘’no insurance agent or broker shall transact business in Nigeria in that capacity unless he is licensed in that behalf under the Act.’’[318] ‘’The application for license is made to the Commission accompanied by such documents as may be prescribed, from time to time.’’[319] ‘’If the Commission is satisfied that the applicant for the license as an insurance agent has met with the requirements prescribed by the law, he shall grant him a license as an insurance agent and notice thereof.’’[320] ‘’The license is renewable annually upon the payment of fees.’’[321]

[312] Section 19(1) *Ibid*.
[313] Section 19(1)(a) Insurance Act 2003.
[314] Section 19(1)(b) *Ibid.*
[315] Section 19(1)(c) *Ibid.*
[316] Section 34 *Ibid*. With 706 brokers and 1668 agents, Nigeria has a vast agency network comprised of 1668 agents. It appears that the brokerages are less efficient than agents in terms of premium per agent/broker. See Dias D., *op cit*, p. 33. The focus on the large corporate and government accounts, which has been the hallmark of Nigerian insurance industry, results in paying override commissions (ORC) in order for a company to win a contract from a broker. The ORC can be up to 50% of the premium. That is why the insurance industry will continue to struggle and stagnate if this trend should continue. Few Fat Cats are making so much money from the industry to the detriment of the majority who are underserved and excluded financially.
[317] Section 36 *Ibid.*
[318] Section 34(1)(a)&(b) *Ibid*.
[319] Section 34(2) *Ibid*.
[320] Section 34(3) *Ibid*.
[321] Section 34(4) *Ibid.* Controversy looms largely in relation to the powers of a *Takaful* who is subject to both applications of civil law (agency and law of contract) and *Shari'ah* in the discharge of his duties. Where for example, the agent exceeds his express

‘’The Act expressly disqualifies minors, persons of unsound mind and ex-convicts found guilty of criminal misappropriation of funds or breach of trust or cheating.’’[322]

‘’An applicant for license as an insurance broker must not only furnish the Commission with documents that may be prescribed,’’[323] ‘’he must also apply to it for registration.’’[324] ‘’The Commission shall only register him if it is satisfied that that the applicant has the prescribed qualification and that the applicant is a partnership or a company with limited liability duly registered under the Companies and Allied Matters Act, 1990 and that he has paid the prescribed fees. If the application is approved, the Commission shall register him as an insurance broker and issue him with a certificate of registration.’’[325] ‘’Where the Commission rejects an application for registration as an insurance broker, the applicant may appeal to the Minister of Finance.’’[326] ‘’Upon payment of the prescribed fees, a certificate issued to an insurance broker shall be renewable annually. A certificate issued to an insurance broker shall lapse if not renewed within three months from the date of expiry.’’[327]

powers and the *Takaful* operator who is the principal in this regard denies liability, the participants are the ones left in lurk and will lose out. This will definitely breed bad blood and mistrust in the industry. This is an area of ambiguity that needs to be made certain. This is discussed in detail in the fifth chapter of the study.

[322] Section 34(5) Insurance Act 2003.

[323] Section 36(2) Insurance Act 2003.

[324] Section 36(1) *Ibid.* During an interview by the researcher with a Senior Advocate of Nigeria (SAN), Mr Mahmoud Magaji, he highlighted the conflicting regulations that abound in the insurance enabling instruments when he cited the case below and went farther to indict judges who lack requisite insurance knowledge and training thereby further compounding the problems of the industry. He said a disturbing trend of confusion arose with the passing of the Nigerian Council of Registered Insurance Brokers (NCRIB) Act in 2003, same year as that of the Insurance Act. This brought some uncertainty into the relationship between the National Insurance Commission as an apex regulatory body for insurance business in Nigeria and insurance brokers. Section 1 of NCRIB provides for the establishment of a body corporate known as the Council of Registered Insurance Brokers to cater solely for insurance brokers. The powers conferred on NCRIB under its enabling legislation was not made subject to the umbrella legislation (the Insurance Act) or to the overriding power of regulation conferred on NAICOM by the National Insurance Corporation Act, 1997. However, in *National Insurance Commission of Nigeria v. the Nigerian Council of Registered Insurance Brokers*, Suit No. FHC/ABJ/CS/218/2004, cited in Funmi Adeyemi, Nigerian Insurance Law, second edition 92007 at p. 471, the Federal High Court held ‘’that power to register and deregister an insurance broker is vested exclusively in the NCRIB and not in NAICOM. In affirming the ruling, the Court of Appeal held that the NCRIB Act was perfectly consistent with both the Insurance Act 2003 and the NAICOM Act 1997. One may argue here that it is difficult to see how the NCRIB can be said not to be in conflict with the Insurance Act and the NAICOM Act. Section 36(1) of Insurance Act is unambiguous in its language. Sections 36(2)and (3) prescribe the procedure for application and the requirements. It is within the exclusive jurisdiction of NAICOM to register or not to register an insurance broker. It is equally the Commission that determines whether or not to cancel the registration of an insurance broker. It is therefore strange to state that any other law that arrogates to itself the right to register or deregister the same entity is not in conflict with the umbrella law. See Appendix 1.2 of thesis.

[325] Section 36(3)(a)&(b) Insurance Act 2003.

[326] Section 36(6) Insurance Act 2003 to be read in conjunction with Section 7 Insurance Act 2003.

[327] Section 36(7) Insurance Act 2003.

2.2.7 Miscellaneous Provisions

Some other provisions under the Act also bring the activities of the insurers under governmental control. Notable among them are:-

1. The general powers of cancellation of registration by the Commission,[328] where such circumstances so justify, has reasonably checked the notorious practice by many insures in delaying settlement of claims, particularly undisputed ones. For example, where a court of competent jurisdiction in Nigeria gives a judgement against an insurer which is not settled within 90 days,[329] or where it is satisfactorily proved that the insurer persistently fails to pay claims promptly,[330] the insurer's certificate of registration may be cancelled.[331]

2. The Act has imposed restrictions on general increase on premium rates. No insurer is allowed to make a general increase in the rates of premium, except with the prior approval of the Commission.[332] Apart from a heavy fine which awaits any insurer who offends this provision, he may in addition be suspended from carrying on such insurance business for a period of not less than six months or have his certificate of registration cancelled.[333] For the purpose of reviewing and determining reasonable and adequate rates chargeable by insurers, the Commission may appoint an ad hoc committee to be known as the Rating Committee which shall include respectively a representative of the Federal Ministry of Trade as Chairman, Federal Ministries of Finance and Economic Development, Nigerian Insurance Association, two representatives of Accident Insurance Association of Nigeria and not more than three other persons to be appointed by the Commission.[334]

[328] Section 8(1) Insurance Act 2003.
[329] Section 8(1)(e) Insurance Act 2003.
[330] Section 8(1)(m) *Ibid.*
[331] Section 8(3) *Ibid.*
[332] Section 51(1) *Ibid*.
[333] Section 51(3) *Ibid.*
[334] Section 52 *Ibid*.

3. On the control of reinsurance business in Nigeria, the establishment of Reinsurance Corporation in 1977 ushered in an indigenous business within and outside the shores of Nigeria, which hitherto had been the monopoly of the international insurance market with the attendant economic consequences to the Nigerian foreign exchange reserves. Hence forth, all registered insurers in Nigeria must re-insure every insurance policy issued or renewed with the Corporation to a minimum of 20% of the sum insured.[335]

‘’The Insurance Act 2003 provides that no person shall transact an insurance or reinsurance business with a foreign insurer or reinsurer in respect of any life, asset, interest or other properties in Nigerian businesses classified as domestic insurance unless with a company registered under this Act.’’[336]

2.2.8 The Insurance Act 2003 and the Application of Customary Insurance

The existence of customary insurance is inferred from the provisions of Section 1 of the Insurance Act, 2003 in its recognition of some forms of insurance other than those to be regulated by the Act. The implication of this provision is that those forms of insurance exempted from the Act will also be out of the regulatory purview of the Commission. This preposition implies that the insurance model exempted under Section 1(a) of the Act should either be subject to regulation by customs or the traditions of a trade association or in other cases by Cooperative Societies Laws of various states in the Nigerian Federation.[337]

The traditional perspective of insurance is highlighted by Professor Irukwu[338] in this manner;

[335] Adamu, A.I., *op cit*, p. 68.
[336] Section 72(1) Insurance Act 2003.
[337] Bukar, B.A. & Saleh, M.M., (2013) Integrating Islamic Insurance Within The Framework Of Conventional Insurance In Nigeria, *Journal of Arts and Sciences*, p. 33.
[338] Irukwu, J.O., *op cit*, p. 1.

> ‘’we live in the world dominated by numerous risks and uncertainties which we encounter in practically all aspects of our lives. Unfortunately, no amount of human ingenuity has been able to eliminate these risks. Since these risks cannot be eliminated, all we can do as rational and intelligent beings is to device effective and efficient methods of managing and controlling these risks’’[339].

The learned author further observed;

> ‘’insurance is universally recognised as a major response to risk problems. As a risk management tool, or to be specific, risk distribution tool, it is the most ingenious creation of human mind. It managed to survive for well over two thousand years.’’[340]

Succinctly put, the learned author is saying that insurance has long been a traditional concept of risk management that has long inhered in the annals of human history. In whatever form it exists, be it traditional, conventional or Islamic, the end goal is the indemnification of the insured in the event of occurrence of the uncertainty insured against.

In as much as traditional or customary insurance exists and is so recognised, the fact still remains that it is rudimentary and unviable on a large scale. The intricacies of modern insurance practice are simply overwhelming for customary form of insurance to be put on a comparative scale.

In the traditional Nigerian context, age grade and tribal associations as well as social clubs have for more than a century, and even today evolved a form of rudimentary insurance scheme for their members. They raise funds through levies and donations to assist individual members who are afflicted by instances of human tragedy. Such

[339] Irukwu, J.O., *op cit*, p. 1.
[340] *Ibid.*

contributions go a long way in assuaging the financial constraints that the family is bound to encounter as a result of the devastating loss. However, what remains pertinent is that for these traditional or quasi-insurance schemes to have proper impact on the society, they will need to be comprehensively modified and improved upon if they are to be seen as adjuncts of modern insurance businesses.

Apart from Canonical Laws, custom is the oldest source of law referred to as Native Law and Custom to distinguish it from the Received English Common Law Principles. In applying the principles of native law and custom side by side with the received English laws, the courts subjected the native laws and customs to the highly subjective test of repugnancy and compatibility with local legislations. In this instance, the transformation of customary practices to admissible native laws for the regulation of the activities of natives became hamstrung. In the case of *Labinjoh v. Abake,*[341] the condition for integrating a custom into Nigerian legal framework was elaborated;

> ''the general rule is that if there is a native law and custom applicable to the matter of controversy and if such law and custom is not repugnant to natural justice, equity and good conscience or incompatible with any local ordinance, and it shall not appear that it was intended by the parties that the obligation under the transaction should be regulated by the received English law, the matter in controversy shall be determined in accordance with the native law and custom.''[342]

In a similar way, Islamic law is administered in Nigeria as if it was one of the variant customary laws and was therefore subject to the repugnancy doctrine test applicable to customary laws.[343] That is to say that for any principle of *Shari'ah* to be upheld, it must

[341] (1924) 5. NLR at p. 36
[342] *Ibid.*
[343] See s. 14 of the Sharia Court of Appeal Law (N.N. Laws 1963, Cap. 122) which empowers the Sharia Court of Appeal of each of the northern States to administer Muslim law of the Maliki School as customarily interpreted at the place where the trial at first instance took place.

conform to the principles of natural justice, equity and good conscience within the context of English Common Law rules. This had negative impact on early evolution and integration of the *Shari'ah* based financial systems into Nigerian legal framework.[344] It should be noted that *Shari'ah* law is Divine Law as far as the Muslim is concerned. It is complete code of living in express and implied form. Canonical Law is on the same pedestal only that it has undergone modification in some aspects to suit current and evolving situations. Islamic law is rigid.[345] Therein lay the difference.

Furthermore, the integration of *Shari'ah* principles has continued to be slow despite the fact that *Shari'ah* law has been an integral part of the Nigerian legal system even before the advent of colonial administration. This can be seen from the jurisdiction of the *Shari'ah* Court of Appeal, the highest court enabled to determine appeals on *Shari'ah* principles which employs civil procedure proceedings in relation to questions of Islamic personal laws on marriage, *Waqf* (gift), will or succession.[346]

In spite of the want of strong evidence to link the traditional insurance with the advent of Islam in Nigeria, the commercial activities of some communities, particularly in northern and western Nigeria, have features of both *Takaful* and conventional insurance concepts. The idea of insurance is basically to provide security and comfort which also characteristics of living in traditional African societies and these mutual support services are rendered among Muslim faithful in accordance with basic *Shari'ah* principles.

[344] Adamu, A.I., *op cit*, p. 61.

[345] The *Shari'ah* aspect of Islamic law and not the *Fiqh* is to a great extent rigid. This view was corroborated by Muhammad Muslehuddeen where he said ''…thus all human actions are subsumed, according to a widely accepted classification, under five categories: as commanded, recommended, left legally indifferent, reprehended, or else prohibited by Almighty God. And it is only in regards to the middle category (i.e. those things which are left legally indifferent) that there is in theory any scope for human legislation. Again, he said, ''…the state itself is subordinate to the Qur'an, which leaves little room for additional legislation….''

[346] Section 262(1) & 266(1) of the Constitution of the Federal Republic of Nigeria, 1990.

The traditional Muslim communities in Nigeria live by interdependence and communal system of association. The growing culture of *Asusu*[347] (savings in a piggy bank) which has features of micro-finance attributes also acts as the most acceptable source of finance, security and investment funding to the participants. In some communities and trade associations, the system has been formalized and registered as community forum or cooperative insurance under bye-law, State Edicts or registered bodies with ministries charged with the regulation of Cooperative Societies in Nigeria. However, in the course of advancement of the cooperative culture in many communities in Nigeria, the business is continuously being subjected to regulatory controls as well as being shaped to conform with the principles of *Shari'ah* in most parts of Northern Nigeria.[348]

In order to have a clear and broad picture of how Nigerian legislation on insurance has metamorphosed since independence in 1960, it is pertinent to look into the gamut of previous legislations that have helped shape the insurance industry and laid the foundations for its existence today.

2.2.9. Insurance Act 1961

Upon the granting of independence from the British in 1960, the following year marked the beginning of insurance legislation in Nigeria. Before the enactment of the Insurance Act, the Nigerian insurance market was virtually regulated by the received English laws. All the elements of the English Common law and doctrines of equity were fully operational, including the statutes of general application which were in force in England before the 1st January, 1900. This means there was a lacuna in terms of statutory application of the law of insurance in Nigeria from the 2nd of January, 1900 up to the

[347] Nigerians without access to or unable to use formal financial services use informal options for their savings and credit needs. Informal choices such as moneylenders and Asusus are dominant in rural areas, but exist in the urban areas as well. Asusu is the oldest form of savings clubs in Nigeria. The majority operates with unwritten laws, based on oath of allegiance and mutual trust. Asusu associations contribute a fixed amount periodically and give all or part of the accumulated funds to one or more members in rotation until all members have benefitted from the pool. See http://www.microfinancenigeria.com/other-news/Asusu-expanding-nigeria%E2%80%99s-financial-services-frontier/.

[348] Adamu, A.I., *op cit*, p. 63.

time of the enactment of the Insurance Act, 1961. There was a void which needed filling but this did not happen until a year after attainment of independence. The Act introduced several pioneering requirements that helped shape insurance practice as it exists today. Chief among these requirements is that of registration or licensing of insurance companies. The other most notable contribution is that of incorporation of insurance companies as limited liability companies under the Companies Act. The issue of licensing is so critical to the sanitation of the insurance industry. Fringe insurance players were chased out of business because insurance license was not easy to obtain. In the same vein, insurers who do not settle claims or take it over are likely to have their licenses withdrawn.

In pursuance of the provisions of the Companies Act, any company wishing to establish an insurance business in Nigeria must first be incorporated as a limited liability company, unless it is either a co-operative insurance society registered under any enactment or law relating to co-operative societies or a mutual insurance company,[349] and must be properly registered under the requirements of the Insurance Act, before it commences business.[350]

2.2.10 Companies Act 1968

Although the Act was not enacted to specifically regulate insurance business, the legislation added impetus to the management of the insurance institutions. The Act merged the erstwhile dichotomy between Nigerian insurance companies and foreign insurers operating in the country with the compulsory registration requirement of all foreign companies wishing to do insurance business in Nigeria. Registration procedures had been discussed previously in the chapter as contained in the pioneer Companies Act, 1948.

[349] See Section 8(1)(a)-(c) of the Company's Act.
[350] *Ibid*, Section 9(1).

2.2.11 Marine Insurance Act 1961

The Marine Insurance Act was promulgated immediately following the coming into effect of the Insurance Act, 1961. The Act was promulgated to regulate marine insurance and to meet the demand of the growing international trade in post-independent Nigeria. The Act was modelled after the English Marine Insurance Act, 1906.

Marine insurance not only affords another example of a contract of indemnity but is also the most intricate of insurance contracts. It is an insurance under which an insurer or an underwriter agrees to indemnify the assured against loss arising from perils at sea either to the ship or to the freight on board the ship. Thus, Marine Insurance has been defined as:

> '' a contract whereby the insurer undertakes to indemnify the assured, in a manner and to the extent thereby agreed, against marine losses, that is to say, the losses incidental to adventure.''[351]

The enactment of this Act has gone a long way in shaping marine insurance and marine business in Nigeria. It is provided in the Act that every person has an insurable interest if he is interested in a marine adventure.

Some notable features of the Act[352] provide that every contract of Marine Insurance is rendered void if it is by way of gaming or wagering. The requirement of an insurable interest, therefore, helps to draw a distinction between Marine Insurance contracts properly so-called, on the one hand, and gaming or wagering or gambling contracts, on the other.[353]

[351] Section 3, Marine Insurance Act, 1961.
[352] Section 6(1). Marine Insurance Act, 1961.
[353] Okany, M.C. *op cit*, p. 858.

Many provisions in the Marine Insurance Act, 1961 are peculiar to marine insurance business. They include warrants which may be express or implied,[354] assignment of policy,[355] losses,[356] measures of indemnity,[357] right of insurer on payment,[358] return of premium,[359] and mutual assurance.[360]

2.2.12 Insurance Decree 1976

The Insurance Decree, 1976 better known as the Insurance Act repealed the Insurance Companies Act, 1961. The Federal Military Government promulgated the Insurance Act,[361]on 1st December , 1976. This was a very revolutionary Act, for it provided new and stringent rules and regulations,[362] whose principal aim was to liquidate all 'mushroom' insurance companies and replace them with strong, dependable and financially viable ones. The then existing insurance companies were given six months, expiring on 3rd, May, 1977 to comply with the new regulations, otherwise they would forfeit their licenses. On the expiry date, only 56 out of more than 200 companies satisfied the provisions of the new law and were duly registered. In addition, four more companies were registered between September and October, 1977.

The 1976 Insurance Act complimented the provisions of the 1968 Companies Act towards registration of companies. In pursuance of the provisions of the Companies Act, 1968, every company wishing to establish an insurance venture in the country must first be incorporated as a limited liability company, unless it is either a cooperative insurance society registered under any enactment or law relating to cooperative societies

[354] Sections 34-42. Marine Insurance Act, 1961.
[355] Section 51. *Ibid.*
[356] Sections 65-67. Marine Insurance Act, 1961
[357] Sections 68-79. *Ibid.*
[358] Sections 80-82. *Ibid.*
[359] Sections 83-85. *Ibid.*
[360] Section 86. *Ibid.*
[361] Act No. 59 of 1976.
[362] Insurance Regulations, 1977; it came into force on 17th, January, 1977.

or a mutual insurance company,[363] and must be properly registered under the provisions of the Insurance Act, 1976, before it commences business.[364]

The provisions of the Insurance Act were comprehensive in as much as it retained a substantial part of the old Act. The insuring public was given better protection by weeding out charlatans who were out to fleece the unsuspecting public. Several other notable provisions were put in place to facilitate an effective regulatory process of insurance business in Nigeria.

Apart from the new standards for carrying on insurance business in Nigeria, the Act raised the minimum paid up share capital from N100,000 to N800,000 and also introduced the concept of statutory deposit to safeguard the interests of the insuring public against the likelihood of insolvency or liquidation of the insurance company.[365]

It is necessary to note that under the Act,[366] every insurance in respect of goods to be imported into Nigeria must be made with an insurer duly registered in Nigeria, unless an insurance broker satisfies the Director of Insurance that it is not practicable to effect such an insurance with an insurer in Nigeria. In such exceptional circumstances, the Director may by a written permission allow the broker to insure with an insurer outside Nigeria.

The enactment of the Insurance Act, 1976, is certainly a watershed in the annals of insurance business in Nigeria. This position was succinctly summed up by Professor Okay Achike in a felicitous note when he opined that;

> ‘’we are now experiencing a new era of responsible insurance industry in Nigeria. By the creation of the office of the Director of Insurance, headed by the Director and assisted by a Deputy, Chief Actuary, Actuaries, Investigators and

[363] See Section 8(1)(a)-(c) of the Companies Act 1968.
[364] Section 9(1). *Ibid.*
[365] Adamu, A.I., *op cit*, p. 53.
[366] Section 46(1). Insurance Act, 1976.

other functionaries with wide supervisory powers and even wider powers of cancelling or suspending the license of an insurer, the *laissez-faire* attitude and unconscionable practices of many insurers are brought under scrutiny. Adequate safeguards have been made for the effective administration of the insurance industry and enforcement of the provisions of the Insurance Act, 1976.''[367]

It is interesting to note that the Code of Conduct for members of the Insurance Institute of Nigeria has fortified the operation of this comprehensive Act of 1976. Clause 4 of the Code provides as follows;

''all members should always be transparently honest in all their professional dealings and should at all times refrain from unethical conduct and must not engage in any fraudulent or corrupt practice.''

Under Clause 7, the Council of the Insurance Institute is enjoined to reprimand, suspend or remove an insurer from membership of the Institute, if he fails to conform to proper standards of professional conduct. It is evident that the above provisions spelt doom for fraudulent insurance practitioners, while promoting favourable environment for those who patronize the insurance industry in Nigeria.[368]

2.2.13 Insurance (Special Provisions) Decree No. 40 (1988)

The Insurance (Special Provisions) Law was enacted to remedy some perceived weaknesses in the 1976 Decree to accommodate the peculiarities of the Nigerian society. The Decree was innovative and proactive and was primarily aimed at modifying some settled Common Law principles or rules on what constitute insurable interest and breach of conditions and warranties. Contrary to the definition of legal relationship under Common Law, the Decree expanded the concept to include

[367] See Okay, A., *op cit*, p. 348.
[368] See Okay, A., *op cit*, pp. 347-9.

relationships under Sharia and customary laws. The Decree also limited the effect of the breach of warranties and conditions as a basis of the insurer's right to repudiate the insurance contract.[369] This legislation was introduced as a departure from the strict Common Law principles with a view to protecting the Nigerian insuring public from the harsh provisions of the Common Law on breach of warranties in a contract of insurance. The 1988 Insurance Decree was the first insurance legislation that recognized and integrated elements of Sharia and Customary law into the Nigerian insurance legal framework.

It is trite law that under conventional insurance practice the proposal form is the foundation of the contract of insurance. It is therefore necessary that this form should be filled with great care and seriousness, because the validity of the policy depends on its correctness. In technical language, the proposal form comprises the offer,[370] which if accepted by the insurers will give rise to the contract of insurance. It contains terms which the insurers will insist upon as the basis for deciding whether to accept the risk and complete the contract. The insurers may accept the offer in the proposal form unconditionally or conditionally. If the proposal form is accepted unconditionally, the parties are bound and the insurers must issue the policy to the insured. But if the offer as contained in the proposal form is accepted conditionally, for example, until the first premium has been paid within fifteen days, the contract of insurance does not take effect until the first premium is paid within the stipulated time.[371]

However, under the Insurance (Special Provisions) Decree No. 40 of 1988,

> ''where an insurer requires an insured to complete a proposal form for insurance, the form shall be drawn up in such a manner as to elicit all such information as the insurer considers material in accepting application for

[369] See also Section 55 Insurance Act, 2003.
[370] See *Rust v. Abbey Life Insurance Co. Ltd* (1982) 2. LLOYD'S Rep. 386.
[371] See Okay, A., *op cit*, p. 319; Schmitthoff and Sarre, *op cit*, pp. 513-4.

insurance of the risk, and any information not specifically requested shall be deemed not to be material.''[372]

The old proposal form used by insurance companies before the promulgation of the Decree does not contain the above provision. The Decree[373] further states that:

''The proposal form or other application form for insurance shall be printed in easily readable letters, and shall state as noted in a conspicuous place on the front page that an insurance agent who assists an applicant to fill a proposal form for insurance shall be deemed to have done so as the agent of the applicant.''[374]

The bone of contention here now is, since the Decree expects an insurer to draw up a proposal form in such a way as to elicit all the information which the insurer considers vital in accepting a proposal for insurance of the peril, one wonders whether the principle of *uberrimae fidei* makes it mandatory for the applicant to disclose all material facts that are incidental to the risk, still applicable.[375]

2.2.14 Insurance Decree No. 58 of 1991[376]

This Decree was promulgated with the objectives of correcting the weaknesses in the previous legislations on insurance and to consolidate all the various requirements in a single volume. Notably, the Act increased the minimum paid up capital of the insurance industry to a minimum of N5 million each for the life and non-life insurer. Another innovative feature is that the Act provided for the establishment of Insurance Security Fund for the purpose of settlement of claims admitted or allowed against registered insurers where the claims are not settled by reason of insolvency or cancellation by the

[372] Decree No. 40 of 1988.
[373] Section 1(2) of the Insurance Decree 1988.
[374] Decree No. 40 of 1988.
[375] Okany, M.C., *op cit*, p. 817.
[376] Decree No. 58 of 1991 Official Gazette No. 74 Vol. 78.

insurer.[377] The fund is to be applied to compensate innocent third parties disabled or killed by uninsured or unidentified drivers in cases of hit and run.[378] The Act charged the Nigerian Insurance Association (NIA) with the responsibility of managing the fund.[379]

2.2.15 Insurance Decree No. 2 of 1997

Apart from re-enacting some of the provisions of the 1991 Decree, this new Decree introduced some provisions that include the registering of insurance brokers and loss adjusters.[380] The new Decree also provided for the requirement of solid solvency margin.

2.3 INSTITUTIONAL REGULATORY LEGISLATION

2.3.1 Insurance Decree No. 62 of 1992

The Act established the National Insurance Supervisory Board (NISB). The creation of the Board has been an answer to the aspirations of the insurance players whose operations had been constrained by the inadequacies of the regulations administered by the Director of Insurance in the Federal Ministry of Finance. The NISB was created to set standards for the proper conduct of the Insurance, protection of the policy holders as well as control and supervise transactions between local insurers and their reinsurers abroad. Although NISB had contributed to the regulatory framework of the industry, it is only a supervisory body and not a regulatory one. The Board fell short in commanding the right clout to deal with emerging issues of unethical practices. It was in recognition of the identified inadequacies that the National Insurance Commission

[377] Adamu, A.I., *op cit*, p. 55.
[378] Section 66 of the Decree. See also Section 78 of the Insurance Act, 2003.
[379] Section 66(1) of the Decree; See also Section 78(1) of the Insurance Act, 2003 which now placed the responsibility under the National Insurance Commission (NAICOM).
[380] Sections 30 & 33 of the Decree.

(NAICOM) was set up to assume the responsibilities of NISB and to strengthen the regulatory powers of the supervisory body.[381]

2.3.2 The Nigerian National Insurance Commission Decree No. 1 of 1997

The Act was in effect a sister legislation to the 1997 Insurance Decree. The obvious differences between the two laws are: while the Insurance Decree deals with matters relating to operations of insurance institutions and conditions for carrying out insurance business in Nigeria, this Act mainly deals with the establishment of the governing authority, its powers and functions.

The Act establishes the Commission as the apex governing body for the underwriting industry. The Commission inherited the role and functions of NISB in addition to other statutory responsibilities to meet the challenges of the regulation task.

In pursuit of the regulatory mandate, which sometimes translates into an oversight, the Act gave the Commission extensive powers including the power to intervene which could be in the form of taking over the management of insurance institutions, appointing interim board and management as well as ultimately revocation of the insurer's certificate of registration, etc. These powers are sweeping and if used wrongly will likely result in grave injustice to insurance practitioners and stakeholders.

To further strengthen the regulatory capacity of the Commission, the Insurance Special Supervisory Fund Decree[382] was repealed and the management of the fund was vested in the Commission effectively side lining the erstwhile managers, the Nigerian Insurers Association.[383]

[381] (1999) NICON Insurance Corporation publication, ' *'The Historic Strides, 30th Anniversary*, ''p. 24.
[382] Decree No. 20 of 1989
[383] Section 63 NAICOM Act No. 2 of 1997.

2.3.3 Chartered Insurance Institute of Nigeria Act No. 22 of 1993

The Act established the Chartered Insurance Institute of Nigeria and charged the Institute with the responsibility for insurance education and maintenance of the registration of insurance practitioners in Nigeria. The Act readily contributes to the development of the insurance industry through professional training and equipping the Nigerian insurance industry with the requisite manpower.

2.4 CHALLENGES OF CONVENTIONAL INSURANCE IN NIGERIA

Conventional insurance practice has been the mainstay of insurance business in Nigeria. It is a body of highly developed practices aimed at mitigating the loss suffered by the insured. What constitutes conventional insurance, its nature, categories, elements and principles have been discussed throughout this chapter.

In spite of its sophistication, this system of insurance has not lived up to its billing in the purpose the insurance industry was set out to achieve. Contrary to expectations, the conventional insurance industry in Nigeria has only succeeded in creating an endemic gap which is becoming too difficult to fill.[384] Most Nigerians do not understand it and are afraid of it; hence they do not buy into it except the compulsory third party/vehicle insurance.[385]

The Nigerian industry is facing a myriad of challenges, chief among which is low level patronage. The problems are endemic and seem to defy solutions. Hard to believe, but the fact on ground is that out of over 186 million Nigerians, only 800,000 of the adult population have any form of insurance cover.[386] It is disheartening to observe that the insurance industry which ought to be a growth sector is struggling and stagnant despite the vast potential in the country. Several factors have been identified as reasons for the unimpressive performance. These include circumscription of the powers of the National Insurance Commission (NAICOM), inadequate capital, limited human and technical

[384] The NAICOM regulated sector makes up only 0.72% of Nigeria's GDP, which is very little compared to many countries, but still comparable to some developing countries, such as Philippines, where insurance premium reaches 1% of GDP, and Ethiopia. Only 15 of the adult population has insurance policy, which is lower than developing countries such as Philippines, where insurance covers 7% of the population. See EFInA Financial Sector Landscape, 2015.

[385] This position was also corroborated in the opinions of Barrister Ibrahim Ahmed, a lecturer in the Faculty of Law, *Shari'ah* Department, University of Maiduguri, Nigeria. He maintained that academics are in a better position to analyse the true regulatory shortcomings of most legislations and that the current insurance regulatory instruments will continue to act to the detriment of the industry's growth due their incongruent nature. Conventional insurance practice is a rip-off in Nigeria because most of the insurers are dishonest. Claims impact in the industry is worthless as one has to be lucky to get any form of indemnity in the event of a loss, he stated in an interview with the researcher. He said as long as the insurance industry continues in this trend of dubious practice then the general public would continue to shy away from participation in insurance schemes. He expressed optimism that Takaful would make a difference because it is ethical and religiously founded which will not condone injustice. See Appendix 1.3 for questioning pattern of the interview.

[386] Dateline Insurance Magazine, (2013), vol.3 no. 3, July/August, p. 5. One of the limitations of the study is the absence of reliable statistics or data on total number of insurance policy holders. The same applies for reliable statistics on Life insurance policy holders. Even NAICOM Website accessed by the researcher has not been helpful. The researcher came across several projected estimates of number of policy holders where some put it at 1.3 million while others say 1.5 million which is a pointer to unreliability.

capacities, and low-level confidence.[387] However, what have been identified as the most debilitating challenges are the twin problems of lack of public awareness for insurance and the absence of public confidence in the system.[388] Until solutions are found to these twin problems, the insurance sector cannot play its desired catalytic role in the growth and transformation of the economy.[389]

The Nigerian insurance sector's capital requirements of N3 billion for General Business; N5 billion for Life Business and N25billion for Reinsurance are unarguably the highest in Africa and among the highest in the world and have the major advantage of eliminating fringe players from the market such that the remaining insurers have adequate financial capacity to settle genuine claims as well as participate in the ''big-ticket'' risks.[390] But this has done little to stir up the industry in terms of patronage. The insurance sector has continued to face crisis of confidence, as the insuring public continues to hold insurance with contempt. Today, the average insurer in Nigeria is perceived by the insuring public as eager to collect premium only to repudiate claims at the slightest opportunity.[391] At the technical level, some challenges that have contributed to the misfortune of the Nigerian insurance industry include the circumscription of the regulator which has led to the fettering of its discretion because, presently, the desired autonomy for the insurance regulator is still far-fetched and less

[387] Dateline Insurance Magazine, (2013), vol.3 no. 3, July/August, p. 5.
[388] In an interview with the researcher on the challenges of conventional practice in Nigeria and the unwanted tag of cheats, the Managing Director of Leaders Insurance Company Nig. Plc, Mr Chris Kwajaffa said the industry recognizes its current reputation and the lack of public trust and awareness of insurance. Several insurance companies attribute mistrust to too many co-insurance arrangements (agreements by several companies to share a large account), poor record of paying claims or too many obstructions in the claims procedures, frauds (e.g. fake insurance and fake insurance agents. They believe the industry needs to improve its image, meeting the client expectation that claim is a certain and easy process. This would require consumer education and awareness building. See Appendix 1.5. Also see Dias, D., et al, *op cit*, p. 29.
[389] Dateline Insurance Magazine, (2013), vol.3 no. 3, July/August, p. 5.
[390] Dias, D., et al, *op cit*, p. 29.
[391] *Ibid*, the low claims ratio of 24% shows the industry offers very little value to insurance clients. According to NAICOM Insurance Statistics Report, 2015, the average claims ratio (gross claims over gross premium income) for all companies (including reinsurance) stood at 24.2%. The minimum recorded ration recorded by individual companies was 1.96% and the maximum 57.97%. Most companies have ratios between 10-30%.

proactive.[392] The issue of deepening insurance penetration must be quickly addressed if the insurance industry is to overturn its misfortunes.[393]

Another major contributory factor to the stunted growth of the insurance industry could be viewed from the Islamic perspective. It is a phenomenal problem because Muslims account for 50% of the total Nigerian population of 186 Million. The conventional insurance product as packaged today is un-Islamic in its entirety. The Nigerian Muslim population is reluctant to participate in conventional insurance schemes because of the usury obstacle. Conventional insurance has in its very embodiment anti-*Sharia* features which are integral to the survival of its operations. These include usury, uncertainty, speculation and gambling. This is a constraint for the Muslim. However, it needs to be mentioned that this study is not an advocacy for the replacement of conventional insurance with Islamic insurance. In as much as the two are fundamentally different, they do share a common objective which is the indemnification of the insured upon the occurrence of the peril insured against. Islamic insurance is an adjunct of conventional insurance. The two can and do exist side by side in spite of the differences. Moreover, Islamic insurance is not meant for Muslims only. It is a product that is meant to cushion the effects of devastating loss no matter the creed or conviction of the insured.[394]

2.5 *TAKAFUL* AS A PANACEA

As discussed above, conventional insurance has been the mainstay of insurance practice in Nigeria. However, the Nigerian insurance industry has faced a multitude of challenges in the course of carrying out insurance businesses to the extent that the

[392] Dias, D., *et al*, *op cit.*
[393] Dias, D., *et al*, *Ibid*, p. 26, assert that ''in general, the insurance industry is overly reliant on corporate and compulsory accounts. The sector has a small portfolio of voluntary products (e.g. less than one million individual voluntary policies in total), which could be grown via several distribution channels, including *bancassurance*. The offerings are quite basic and commoditized. Insurance companies in Nigeria have low claims ratio (around 25%), indicating the low value of their offerings. Expense ratios are high in many companies, which is influenced by market practices such as high commissions paid to win large corporate accounts and general operational inefficiency. This contrasts with high profitability (33% gross premium), which could be partially explained by the low claims ratio. Overall there are too many competitors focusing on too few clients, pushing operational expenses (particularly commissions) up''.
[394] Alabadan, S., NAICOM with Guidelines for Islamic Insurance, Daily Independent Newspaper site, 24th August, 2012.

industry is virtually the most unpopular among the populace and the financial sector in Nigeria's economic history. It has inevitably, financially, excluded a vast majority of the populace[395]. The insurance growth rate is stagnant, there are issues with non-payment of claims, there is an evident lack of deepening insurance penetration and worse of all, the ever present public distrust.[396]

Financial inclusion objectives on the global platform encapsulate the notion of financial services delivery that is easily accessible and affordable by the teeming populace irrespective of beliefs or creed. Overcoming the challenges in establishing an inclusive financial platform is, therefore, crucial in the drive towards improving the lives of populace through deepening insurance penetration and the creation of sustainable financial services in the Nigeria.[397] Therefore, taking into cognizance the substantial number of economically underserved and financially excluded segment of the Nigerian population comprising about 50 per cent who are Muslims, this portends a huge clientele for non-interest finance which can be a vital tool for the engendering financial inclusion initiatives through the application of *Takaful*.

The glaring shortcomings of financial illiteracy among the populace have been identified as major obstacles militating against the universal battle in overcoming the endemic prevalence of financial exclusion. The prevalence of financial illiteracy is especially more pronounced among women who are more vulnerable and of course the less educated members of the society. It is clearly evident that most of the underserved and financially excluded populace often lack the basic capacity to cultivate savings

[395] As mentioned earlier, insurance sales revenues make up only 0.72% of Nigeria's GDP, according to NAICOM's website accessed in April, 2015. According to EFInA survey (Access to Financial Services in Nigeria Report), it is estimated that only 1% of the adult population (about 800,000 people) have insurance. Out of these, 58.8% (0.47 million) have compulsory motor insurance and 21.6% (0.173 million) have life insurance.

[396] There is limited product diversification while the conventional insurance sector focuses mainly on mandatory and corporate insurance. The insurance portfolio is dominated by mandatory insurance, large government contracts and insurance for the oil and gas industry. There are at least six insurance products that are mandated by law in Nigeria, and offered by insurance companies. The life segment is very small and this writer found it difficult to find information on it. Life premiums make up 26% of all sales but there are less than one million voluntary individual policies. Due to difficulties in obtaining data, the best logical comparison one could make is using a life density comparison. Nigeria's life density, which is life insurance premiums per capita, is very low compared to some other developing countries. This indicates once again a market that has been ignored.

[397] Kollere, A. U., (2014), *Takaful* Insurance: Towards Deepening Insurance Penetration, *Daily Trust Newspaper,* p. 38.

culture and effectively utilize their meagre resources for effective financial resolutions.[398] A good example is that lack of financial tutelage makes many people to incorrectly assume that insurance can only be effected when there is spare resources. This erroneous perception forms the fundamental thinking among many people about risk and the corresponding need for diminishing it.[399]

In addition, the financial inclusion objectives of non-interest finance can hardly be realized without putting in place a comprehensive regulatory framework for an interest-free scheme that serves to mitigate risk like *Takaful*.

It may be stated again here that, *Takaful* is not just a product, it is more than that. In fact it is best described as a concept that is devoid of religious connotation. It is a direct contrast to risk transfer attributes found in conventional insurance because it serves to share risks instead of transferring them. *Takaful* is a form of communal sharing of burden, it is wholesome and alluring, people will partake in it. It is immaterial whether they are Christians or Muslims.[400]

Rahman and Redzuan posit that,

> ‘’unlike conventional insurance, *Takaful* complies with *Shari'ah* principles of compensation and shared responsibilities in the community. It has been expanded to cover general risks, health and family (life) plans for Muslim communities. Muslim faithful believe that insurance should be based on principles of mutuality and cooperation and this means shared responsibility, joint indemnity, common interest and solidarity. In *Takaful*, the policyholders are joint investors with the insurer (*Takaful* operator), who acts as manager for

[398] Kollere, A. U., (2014), *Takaful* Insurance: Towards Deepening Insurance Penetration, *Daily Trust Newspaper*, p. 38..
[399] *Ibid.*
[400] Daniel, F., (2012), Challenges, Prospects of *Takaful* Insurance, *ThisDay* Newspaper Article, http://www.thisdaylive.com/articleschallenges-prospects-of-takaful-insurance/118793/ accessed on Thursday 06 August, 2015 Updated 11:24. He said, ‘’ …rather than allowing people to see Islamic insurance as being designed only for the Muslim population, Christians and any other person would patronize *Takaful* insurance products by the time they understand what *Takaful* is all about and that it has a prospect of returning part of their premium at the end of the year, many people will buy into it, it is not about religion, it is about a way of sharing risks’’.

the policyholders. The policyholders share in the investment pool's profits as well as its losses. A positive return on policies is not legally guaranteed, because in Islam, any fixed profit guarantee is equivalent to paying interest.''[401]

Ahmad and Auzzir, opine that

''The workings of *Takaful* are quite simple. Policyholders or shareholders agree to guarantee each other and instead of paying premiums, they make contributions into mutual pool, creating a *Takaful* fund. The amount of contribution that each participant makes is based on the type of cover they require and their personal circumstances. As in conventional insurance, the policy or *Takaful* contract specifies the nature of the risk and period of cover.''[402]

Hassan, reiterated the point that

''The *Takaful* fund is managed and administered on behalf of the participants by a *Takaful* operator who charges an agreed fee to cover costs. These costs include the costs of sales, marketing, underwriting and claims' management. Claims made by policyholders are paid out of the *Takaful* fund and any remaining surpluses, after making provisions for likely cost of future claims and other reserves, belong to the policyholders or shareholders of the fund and not the *Takaful* operator and may be distributed to the participants in the form of cash dividends or distributions, alternatively in reduction in future contributions.''[403]

A renowned scholar, Muslehuddin says that

''In conventional insurance, the customers pay premium in return for the insurance protection. It is not so in *Takaful*. In this case, the policyholders make

[401] Rahman, Z.A. & Redzuan H., (2009) *Takaful: The 21st Century Insurance Innovation*, McGraw-Hill, Malaysia, p. 36.
[402] Ahmad, R. & Auzzir, Z.A., (2013), *Takaful*, Pearson Malaysia, p. 20.
[403] Hassan, R., (2011), *Islamic Banking and Takaful*, Pearson Malaysia, p. 190.

> contributions equitable with the risks they are bringing into the pool. This is different from the premium which is based on ratings calculated by underwriters in the case of conventional insurance.''[404]

The investment of *Takaful* funds must be compliant with *Shari'ah* principles which forbid wagering, profiteering and indulgence in alcohol, among others. Furthermore, the funds must not be sunk into economic activities which Islam expressly prohibits for example brewing of alcohol, etc.[405]

In *Takaful*, the participants are the proprietors of the undertaking and in that capacity they are eligible to partake in sharing the gains or losses incurred by their franchise. This is dissimilar to conventional insurance practice where policyholders are ordinary clients who purchase insurance cover while shareholders of the enterprise share the profits or losses as the case may be.[406]

Frenz and Soualhi maintain that

> ''claims in *Takaful* are usually paid to those unfortunate policyholders/shareholders who suffer some insured losses within the period of cover. They are compensated from the pool and reinstated accordingly. Claims experience is not disturbing as the volume is not such that would give any insurer sleepless nights but the problem lies in the frequency of usually small claims.''[407]

Furthermore,

> ''on re*Takaful* or reinsurance, *Shari'ah* principles apply to *Takaful* as much as it applies to re*Takaful*. The reinsurance contract, for Islamic companies, must be

[404] Muslehuddin, M., *op cit*, p. 5.
[405] Ahmad, R & Auzzir, Z.A., *op cit*, 48.
[406] Ahmad, R & Auzzir, Z.A., *op cit*, 48.
[407] Frenz, T. & Soualhi, Y., (2010), *Takaful* & Re*Takaful*; Advanced Principles and Practice, IBFIM/Munich RE, p. 171.

contracted in conformity with *Shari'ah*. There is need for strong and credible re*Takaful* operators to assist the growth and expansion of *Takaful* business globally. The shortage of re*Takaful* capacity and the lack of companies in the market currently present great challenge to operators. The challenge is to have a large enough *Takaful* market to justify re*Takaful* business.[408] In response to this challenge, *Shari'ah* scholars now allow *Takaful* operators to reinsure conventionally when no *Takaful* alternative is available, although re*Takaful* is strongly preferred.''[409]

The former NAICOM Commissioner, Mr Fola Daniel, buttressed the fact that:

''one of the greatest challenges that the *Takaful* operators face worldwide is the rating system. There is yet no scientific method or model for rating risks in *Takaful* insurance. In conventional insurance, there are standard rates for fire, motor, life and other lines of business prepared by actuaries. This is not available in *Takaful*. Also the high rate of default by beneficiaries of *Takaful* and lack of efficient risk management tools to eliminate fraud and other risks are among the challenges. There is also the absence of an effective risk management tool which can effectively eliminate fraud and other risks in the system as well as the absence of re*Takaful* capacity for *Takaful* insurance. In addition, there is the absence of credit information in the market and moral hazards.''[410]

Yusuf, summed up the prospects of *Takaful* by stating that:

'' on the brighter side, it has been stated unequivocally, that *Takaful* will give a huge boost to the economy from the attendant accumulation of huge micro-

[408] Frenz, T. & Soualhi, Y., *op cit*, p. 171.
[409] *Ibid.*
[410] Daniel, F., *op cit.*

finance fund and expansion of the micro-finance infrastructure[411]. In the same vein, the market regulator's job would be simplified when *Takaful* market grows, while legislations on *Takaful* and insurance, generally, would improve significantly.''[412]

Furthermore,

> ''with *Takaful* insurance, people can save regularly for a fixed period that is convenient for them. The accumulated targeted amount can be used to fund obligations such as purchase of land, house, marriage or hajj. It could also be used to meet other long term financial objectives, such as retirement, children education, travelling expenses as well as other expected commitments.''[413]

Haiss and Sumegi also added their voices to the prospects of *Takaful*, thus:

> ''*Takaful* as well serves as a guarantee to credit providers just as policyholders benefit from loss prevention services put in place by service providers and share in the surpluses recorded at the end of the accounting period. The system is also likely to reduce insurance cost and economic waste and help to alleviate poverty and increase the level of corporate social responsibility of the insurance industry.''[414]

Takaful businesses have broadened the range of coverage of their products to encompass livestock insurance, fire, burglary, motor, agricultural and many other

[411] ''The importance of economic growth and development cannot be overstated. Income growth is essential for achieving economic, social and even political development. Countries that grow strongly and for sustained periods of time are able to reduce their poverty levels significantly, strengthen democratic and political stability, improve the quality of their natural environment, and even diminish the incidences of crime and violence''. See Yusuf, T.O., (2014), Prospects for *Takaful*'s Contribution to the Nigerian Economy, *Journal of Insurance Law and Practice*, vol. 4, no. 2, p. 218.

[412] Yusuf, T.O., (2014), Prospects for *Takaful*'s Contribution to the Nigerian Economy, *Journal of Insurance Law and Practice*, vol. 4, no. 2, p. 218.

[413] Frenz, T. & Soualhi, Y., *op cit*, p. 190.

[414] The importance of the insurance-growth nexus is growing due to the increasing share of the insurance sector in the aggregate financial sector in almost every developing and developed country, according to Haiss, P. & Sumegi, K., (1999), *The Relationship of Insurance and Economic Growth-A Theoretical and Empirical Analysis*, Openaccess.htm. Insurance companies, together with mutual and pension funds, are one of the biggest institutional investors into stock, bond and real estate markets and their possible impact on the economic development will rather grow than decline due to issues such as ageing societies, widening income disparity and globalization. This trend is likely to be accelerated with the new foray of Islamic insurance (*Takaful*) into the economic space by essentially targeting a sizeable mass of low-income earners. The growing links between the insurance and other financial sectors also emphasize the possible roles of insurance companies in economic growth.

attractive products. The insurance providers encourage benefactors to establish industrial unions and cooperative associations to be entitled to partake. If the necessary regulatory platform is put in place, *Takaful* insurance may well be the key to deepening insurance penetration in the Nigerian insurance industry.

2.6 CONCLUSION

This chapter discussed the concept and application of conventional insurance in Nigeria. The study traced the history of insurance practice from the primordial rudimentary form of mutual assistance to the advent of the highly technical and sophisticated conventional insurance venture brought about by vestiges of colonial conquest to the projected trending practice of Islamic insurance (*Takaful*). Conventional insurance practice in Nigeria is carried out on the platform of basic Common Law principles which have been domesticated by local legislations with some modifications where expedient and the statutory regulatory legal framework which control and supervise insurance application. These insurance principles and legislative instruments are intertwined and they collectively constitute the body of laws which facilitate the operation of conventional insurance in Nigeria.

The statutory legal framework in Nigeria has always been under constant review in order to cater for both the insurer and the insuring public. This has been the case since Nigeria became independent in 1960. However, in spite of all these proactive reviews, the insurance industry has virtually stagnated and has contributed pittance to the growth of the Nigerian economy. It is disheartening to note that less than 1 million Nigerians actually have any form of insurance cover out of a population of over 150 million. As a growth sector in the economy, its performance leaves much to be desired. The universal objectives of financial inclusion are not being realized. The global economy is facing unprecedented distress and the Nigerian economy is no exception. The insurance

industry, as a growth sector, stands in a perfect position to help assuage these problems. The study identified certain key elements that are responsible for the poor performance of the industry and among solutions proffered is a case for *Takaful* and a wholesome *Takaful* statutory underpinning that would help build an insurance industry that is financially inclusive in order to improve the lives of the people. Details are discussed in depth in the subsequent chapters of the study.

CHAPTER 3: THE CONCEPT OF ISLAMIC INSURANCE (*TAKAFUL*) AND ITS APPLICATION WITHIN NIGERIAN LEGAL FRAMEWORK

3.0 INTRODUCTION

The previous chapter laid the foundation of the thesis and analysed the context of conventional insurance practice and its legal framework in Nigeria by first tracing the origins of insurance and highlighting the existence of rudimentary or customary insurance as practiced at the traditional level. It also identified and examined the law regulating conventional insurance which is mainly in two parts comprising the law of contract itself *inter se* between the parties and secondly, the regulatory framework which regulates the conduct of insurance business and the attendant supervision. The chapter also examined the specific challenges facing the insurance industry and proposed *Takaful* as panacea.

The Nigerian insurance industry is battling with a myriad of challenges thereby resulting in its stunted growth. The endemic gap has widened over the years and solutions seem farfetched. The problem of poor insurance penetration has been a source of great concern to practitioners and stakeholders alike. With the gross premium income remaining almost stagnant at the close of each financial year, the regulator, the National Insurance Commission (NAICOM), and stakeholders have been deploying series of strategies to boost penetration as a way of increasing GPI.

It is an irony that even with the level of huge human and natural resources[415] available in the country the insurance sector contributes an abysmally paltry 1.0 per cent of the country's Gross Domestic Product.[416] Compared to the official population of 186 million,[417] only about 800,000 Nigerians have some form of insurance policy because

[415] Nigeria is a country that is made up of about 250 ethnic tribes and Muslims constitute 50% of the total population of 186 million. It is home to the largest Muslim population in Sub-Saharan Africa. See ''The Emerging Islamic Finance Market Outline and Challenges, posted by Detail Solicitors, 14th Floor, 38/39, Conoil Building, Marina, Lagos, available at www.google.com, accessed on 24th August, 2015. See also Aliyu, S.U.R., muchen.de/425573, accessed on 7th May, 2015, pp. 1-3.

[416] Adekoya, A.I.B., (2012) *Will Takaful Make a Difference?* Dateline Insurance Magazine, vol. 1, no. 5, p. 3.

[417] Nigeria is a populous, young, diverse country, and still growing. Nigeria is the most populous country in Africa and 7th most populous in the world and the population is still growing with about 2.5% every year (See CIA Fact Book 2017). The median age is 19.2 years and life expectancy stands at 52%. Half of the population are in rural areas, most of them engaged in subsistence

penetration has always remained very low with life insurance still below 0.3 per cent and non-life slightly above 0.5 per cent.[418]

Even with more products, designed to be attractive , placed on the shelves from time to time by the insurers, lack of disposable income, religious beliefs as well as superstition are taking the value of insurance away from majority of Nigerians.

It is a combination of factors stated above and many more that have snowballed into a huge clamour by Muslims and subsequent emergence of *Takaful* in the Nigerian insurance landscape. The big question still remains: Will *Takaful* make the difference? Will it boost the much talked about penetration? These are some of the research questions this thesis hopes to address in due course.

Takaful, simply put, is a mutual agreement between two parties for a mutual co-operation in protecting one's life or property from any unprotectable and unavoidable risk, danger or tragedy.[419]

Technically, the concept of *Takaful* in the area of insurance means mutual assurance or guarantee amongst the members of a group between each other.[420] It is also the pooling of resources to help who are in need,[421] a method which in spirit is close to the principles of compensation and shared responsibility as practised between the *Muhajiruns* and the *Ansars* in Madinah.

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agriculture. Sixty-eight per cent of the population is literate which includes English, Arabic and other languages. The most widely spoken languages are Hausa, Yoruba, Fulani, Igbo and Fulani. About 70% of the population is Muslim while Christians constitute 25%. The remaining 5% are animists. The North and South of the country is mostly Muslim, while Christians concentrate in the East. See Dias D., *et al*,(2013) *Towards Inclusive Insurance in Nigeria: An Analysis of the Market and Regulations*, Eschborn, p. 17.

[418] Adekoya, A.I.B., *op cit*, p. 3.

[419] Billah, M.M., (2006), *Shari'ah Standard of Business Contract,* A.S. Noordeen Publishers, Kuala Lumpur, p. 81.
The Islamic Financial Services Act 2013 of Malaysia defines *Takaful* as ''an arrangement based on mutual assistance under which *Takaful* participants agree to contribute to a common fund providing for mutual benefits payable to the Takaful participants or their beneficiaries on the occurrence of pre-agreed events''. It should be noted that there are several salient differences between the 1984 definition and 2013 definition of *Takaful*. It can be inferred that the 2013 definition of *Takaful* is more comprehensive and accurate compared to that of 1984. The 2013 definition includes the term 'common fund' i.e. *Tabarru'* or Participants' Risk Fund (PRF). Also another important distinction is the inclusion of 'the beneficiaries' of the *Takaful* participants as the recipients of the *Takaful* benefits upon the occurrence of the pre-agreed events. See generally Abd Hamid, M.H. & Hassan, R., (2014), Islamic Financial Services Act 2013: A Preliminary Note on its Impact to *Takaful* Industry, 2 *Malaysian Law Journal*, p. lxvii.

[420] Ahmed, S., (2006), Islamic Banking, Finance and Insurance: A Global Overview, A.S. Noordeen Publishers, Kuala Lumpur, p. 512.

[421] Ahmed, S., (2006), *Islamic Banking, Finance and Insurance: A Global Overview,* A.S. Noordeen Publishers, Kuala Lumpur, p. 512.

Research has revealed that *Takaful* is one of the world's fastest growing segments in insurance at around 20 per cent per annum on the average. Its net worth is conservatively estimated at around $7 billion, comprising 60 per cent General *Takaful*, and 40 per cent Family *Takaful.*[422] Additionally, *Takaful* has a progressive world-wide geographical spread across South and East Asia at 56 per cent, Middle East at 36 per cent, Africa at 7 per cent, and Europe, the United States and others at 1 per cent.[423] In the case of Nigeria, the thesis submits that feelers appear to be positive in this regard as more Muslim faithful believe that emergence of the model, which allows for risk sharing by everyone involved, would not only boost grassroots awareness but also increase penetration by a reasonable percentage.[424]

The development of *Takaful* has evolved into one of the rapidly growing industries in the world today. It occupies a strategic position in the financial sector of many countries and significantly acts as a catalyst of economic activities and a source of funds for investment in about exactly the same way as conventional insurance does, albeit, with some modifications.[425]

Due to globalisation and wider reach, *Takaful* transcends borders of narrowed faith-based Islamic transactions and has developed into an integral system of alternative financial model. The companies that offer *Takaful* insurance have attracted a wide range

[422] Adekoya, A.I.B., *op cit*, p. 3.
[423] *Ibid.*
[424] One of the objectives of this study is to gauge the attitude of the Nigerian populace towards the legal application of *Takaful* insurance in Nigeria. Feelers for this positive attitude and the subsequent excitement generated was observed I the course of interviewing representative respondents as found in the thesis.
[425] According to the Banker (2001), ''the Islamic insurance sector or *Takaful* has expanded in many major markets and in Muslim dominated countries around the world. Among the 25 companies in the world, ranked by the Banker, Brunei's *Takaful* IBB Bd is first followed by SCA's of Iran Insurance Company and Malaysia's Syarikat *Takaful* Malaysia Berhad with *Shari'ah* compliant assets worth $31.5 billion, $1.5 billion, and $824.8 million respectively, while the Gulf Cooperation Council (GCC) companies, is led by Saudi Arabia's Company for Cooperative Insurance. The impact of Islamization has not only been felt where Islam is practiced, but also in countries where the Muslim population has increased tremendously and this is particularly true in the Western world, Europe and North America''. See Fisher, O. & Taylor, D.Y., (2000), Prospects for Evolution of Takaful in the 21st Century, available at http://www.takaful.com.sa/m4sub3.asp.openaccess.htm. See also Yusuf, T.O., (2014), Prospects for *Takaful*'s Contribution to the Nigerian Economy, *op cit* p. 222.
Another indicator for *Takaful* vibrant growth in the future is the size of the Muslim market. (This is of significant relevance to the Nigerian situation because of the 70% majority population of Muslims out of 150 million individuals). Experts estimate on the number of Muslims in 1999 was 1.2 billion representing between 19.2 to 22 per cent of the world's population and growing at 2.9 per cent per year (2.3 per cent growth rate for total world population).. According to another estimate, Muslims have grown by more than 235 per cent in the last 50 years and now stands at almost 2 billion. Population size and demographic consideration is certainly of vital concern for an enterprise before embarking on a new venture, because the larger the population, the larger is the potential market size while social structure also plays an important role in dictating demand. See Yusuf, T.O., *op cit.*

of customers because of their equity based dealings as opposed to faith. This is exemplified in countries like Sri Lanka where less than 10 per cent of the population is Muslim but around 15 per cent of the policy holders of *Takaful* company are non-Muslims.[426]

This study submits that the integration of *Takaful* into the legal framework of many countries has not been without teething challenges especially the conflicting regulatory obstacles. Malaysia went through it and came out strongly culminating in the promulgation of *Takaful* Act, 1984 and subsequently the Islamic Financial Services Act, 2013 that harmonized all the regulatory conflicts inherent in the *Takaful* insurance system. This has provided regulatory certainty and clarity leading to sustainable development of *Takaful* in Malaysia. Nigeria is expected to toe the same line.

The primary sources and roots of *Takaful* are embodied in the Noble Qur'an[427] and the Hadiths of The Prophet (pbuh).[428] The other secondary sources of *Ijma* (consensus of Islamic jurists) and *Ijtihad* (analogical deductions of jurists) have significantly contributed in the evolution and development of *Takaful*.

In the Nigerian context, *Takaful* as a concept has the tacit support of the enabling insurance legislation as found in Section 1 of the Insurance Act, 2003 even though the support is by inference. It remains disturbing that there is no substantive mention of *Takaful* in the main Insurance Act of 2003. This makes the application of *Takaful* in the regulatory instruments fraught with uncertainty and ambiguity. It is in this spirit that this study undertakes to bring to the fore the application of *Takaful* within the

[426] Kazi M.D. and Mortuza A., (2011), *Present Scenario and Future Potentials of Takaful*, p. 8.

[427] This concept of *Takaful* is in fact, justified by the Divine Command of mutual cooperation, brotherhood, solidarity and cooperative help which is provided for in the following words of the Noble Qur'an ''…Cooperate with one another in righteousness and piety, do not help one another in furthering evil and enmity'' See Nobel Qur'an Chapter 5 Verse 2. Therefore, *Takaful* scheme (relying on the concept of mutual help and cooperation) aims at undertaking joint responsibility towards the material safeguard and protection of the vulnerable members of the society and also those who suffer the misfortune of unexpected loss or damage to their property.

[428] The Sunnah of the Noble Prophet pbuh justified *Takaful* when he pbuh said to a Bedouin Arab who left his camel untended to '' tie your camel first before leaving it to the trust of Allaah SWT''. (Tirmidhi). Furthermore, the Noble Prophet pbuh said ''whosoever removes a worldly hardship from a believer, Allaah SWT will remove from him one of the hardships on the Day of Judgement. Whosoever alleviates from one, Allaah SWT will alleviate his lot in this world and the next''. (Bukhari).

framework of *Shari'ah* principles and also its legal basis under the enabling regulatory framework of the industry with a view to making a case for substantive and specific legislative enactment.

The study laid a foundation for this incision in *Takaful* emergence and application in the Nigerian insurance industry with an in depth descriptive analysis on the concept of *Takaful* as is known and applied world-wide. This descriptive precursor is imperative as a beacon for gauging the strides the Nigerian regulators have made towards the successful application of *Takaful* as a viable insurance concept in the country.

3.1 THE LEGAL BASIS OF *TAKAFUL* UNDER *SHARI'AH*[429]

Shari'ah factually means a path or way to a watering place.[430] Technically, the word means submission to the Will of Allaah (SWA) or Divine instructions regarding all aspects of a Muslim's existence. It is therefore aptly labelled a body of divine laws, rules, code of conduct and instructions which are envisioned to profit the individual and humanity at large.[431]

The fundamental objective of *Shari'ah* is to ensure the wellbeing and welfare of mankind,[432] therefore, the objective of *Shari'ah* is targeted at founding an expedient life for the believer and removing hardship.[433]

In this respect, *Shari'ah* has laid down rules and guidance which are to be adhered to strictly in all dealings and relationships, financial dealings inclusive. The operation and conduct of Islamic finance such as banking, economics, insurance, assets management

[429] *Shari'ah* refers to Islamic law and governs all aspects of both personal religious practice and Muslim society at large. Its literal meaning of 'way to water' – the source of all life – signifies the way to God, as given by God. It can also be seen as a code of best conduct regarding all ways of life. It is often described as divine, universal, realistic and flexible.
Shari'ah is enshrined in the two revealed sources, the Noble Qur'an and the genuine Sunnah. By virtue of being revealed, they are considered divine and fully protected by God. Throughout Islamic history, the servants of Islam interacted with these two sources, and endeavoured to explain them to the public who lack the ability to understand the divine speech. In the area of Islamic jurisprudence, Muslim scholars interpreted all the verses and Hadiths pertaining to Halal (permissible) and Haram (prohibited), producing huge corpuses and compendiums that laid the foundation of Islamic jurisprudence known as *Fiqh*. However, the four schools of jurisprudence and their doctrines constitute part of *Shari'ah* as long as they are based on the firm principles and objectives of the *Shari'ah.* See Tobias, F. & Younes, S., (2010), *Takaful & ReTakaful: Advanced Principles and Practices,* IBFIM, Malaysia, p. 22.
[430] Nasser Y., (2011) *Takaful: Study Guide,* Kuala Lumpur Publishers, p. 3.
[431] *Ibid.*
[432] Qur'an, Al Maidah, Chapter 5 verse 6; Al Bakarah Chapter 2 verse 185.
[433] Fadzli M. *et al,* (2011) *Fundamentals of Takaful,* Kuala Lumpur Publishers, p. 3.

and investment must be in line with the requirements and practices of *Shari'ah* which is the body of rules and rulings in accordance with Islamic injunctions.[434] *Shari'ah* is based on two primary sources namely the Noble Qur'an and the Sunnah or Hadiths (sayings of the Noble Prophet) pbuh. Apart from these primary sources, there are other secondary sources of *Ijma* and *Qiyas* or the process of comparison or making analogical deductions from existing rulings to be applied to new situations of similar nature. In view of this position, this discourse will examine the legal basis of *Takaful* from the perspectives of the afore-mentioned sources of the *Shari'ah*.

3.1.1 Fundamental Basis of *Takaful* in the Noble Qur'an

Granting that the word *Takaful* does not expressly appear in the Noble Qur'an, it is a derivative of the term *Ta'awun,* or mutual support which indicative of the same meaning. The second verse of Surah Al Maidah in the Noble Qur'an exhorts the individual to assist others:

> ''assist one another in the doing of good and virtuousness. Assist not one another in sin and wrongdoing, but keep your duty to Allaah.''[435]

The word *Ta'awun* in the above cited verse of the Qur'an is the underlying concept of insurance practice which means to aid, to help, or to assist through mutual cooperation. The idea of insurance is inferred in the verse to mean providing financial support to any unfortunate participant suffering a loss or detriment. Human beings are always exposed to catastrophes and disasters thereby giving rise to sufferings and penury. The Noble

[434] The contractual relationship in Islamic insurance companies strictly observes *Shari'ah* rules and principles and avoids *Riba*-based transactions, especially when investing the collected contributions. Again, the contract and policy certificate must comply with the requirements of *Shari'ah* in respect of the agreement. In other words, it is not a requirement that a particular *Takaful* contract should comply with a *Shari'ah*-nominated contract or that such *Takaful* contract must exist in the Qur'an or Sunnah. All what is required is that the contract must not violate *Shari'ah* principles. This is because as a general principle, all contracts concluded by men are considered valid unless otherwise explicitly prohibited by *Shari'ah*. This thus necessitates the appointment of *Shari'ah* Boards and Internal *Shari'ah* Advisors in order to advise on how insurance operations should be carried out according to the *Shari'ah* requirements. See *Takaful* Act, 1984 now Islamic Financial Services Act, 2013.
Islam has a clear set of rules or general principles governing the terms and conditions of doing business. So long as the boundaries are not violated, the business should be permissible and valid. The original legal position of any matter is permissibility until there is evidence prohibiting it. See Ismail, A., (2002) Islamic Risk, Asset Management and Wealth Distribution, Lecture Series, for *Persatuan Remisier Bumiputra Malaysia*. The Prophet pbuh clearly stated in a Hadith ''…Muslims are bound by contracts, except contracts which prohibit what is permitted or permit the prohibited''. See the Directory of Islamic Insurance, 1999.

[435] Noble Qur'an, Chapter 5 Verse 2.

Qur'an therefore enjoins Muslims to adopt a means to avoid such unfortunate occurrences by taking pro-active steps to cushion or mitigate the devastating impact of such tragedy.[436]

As the objective of Islam is the fulfilment of life and its conveniences within the precincts of *Shari'ah,* Islam upholds trade and mutual assistance and at the same time prohibits wastage and vanity that occasion losses in trade often resulting in untold hardship and needless suffering. *Takaful* claims are aimed at alleviating such suffering. The Noble Qur'an enjoins believers to:-

> ''….render to the kindred their due rights and also those in want, and the wayfarer; but squander not (your wealth) in the manner of spendthrift.''[437]

Also, in the Noble Qur'an, Allaah (SWA) admonished believers on trade and mutual goodwill which form the fundamentals of *Takaful*:-

> ''Oh you who believe, eat not up your property among yourselves and vanities; but let there be amongst you traffic and trade by mutual goodwill.''[438]

3.1.2 Legal Basis of *Takaful* Under Sunnah[439]

The Prophetic Sunnah of Prophet Muhammad (pbuh) is the second arm of the primary source of *Shari'ah.* It is the most recognized medium for the clarification and expounding of the provisions of the Noble Qur'an. In spite of the belief in Al Qadr (predestination) in Islam, *Shari'ah* enjoins believers to make provisions in their lifetime

[436] Noble Qur'an *Surah Al Isra,* Chapter 17 Verse 17.
[437] Noble Qur'an *Surah Al Isra,* Chapter 17 Verse 26.
[438] Qur'an Surah Al-Nisa' Chapter 4 Verse 29.
[439] Besides the Noble Qur'an, Prophet Muhammad's pbuh life (*Sirah*) and his recorded and validated sayings, acts and tacit approvals (Hadith) – known as the Sunnah – are upheld by Muslims. Prophet Muhammad pbuh was sent not just to deliver the Book of Allaah, but to expound it and demonstrate a practical example of its contents. Thus his life set an example of how Muslims should live their lives and the Sunnah can be seen as an essential clarification of the Noble Qur'an and a supplement to it. See Tobias, F. & Younes, S., (2010), *Takaful & ReTakaful: Advanced Principles and Practices,* IBFIM, Malaysia, p. 13.

to lighten the burden on their families in the event of death.[440] In a hadith narrated by Sa'ad bn Abi Waqqas (r.a.) , the Prophet (pbuh) admonished his companions that:-

> ''verily it is preferable for you to leave your off-springs wealthy than to leave them poor, asking others assistance.''[441]

In the same spirit, the Prophet (pbuh) implored Muslim communities to protect one another from any form of hardship and difficulties, when he said to the effect that:-

> ''whosever removes a worldly grief from a believer, Allaah (SWA) will remove from him one of the grieves of the Day of Judgment.''[442]

Abu Hurrairah (r.a.) narrated from the Prophet (pbuh) that:-

> ''whosoever alleviates a needy person, Allaah (SWA) will alleviate suffering from him in this world and the next.''[443]

The elements of insurance are enshrined in a hadith narrated by Anas bn Malik (r.a.) where he said:-

> ''The Holy Prophet (pbuh) told a Bedouin Arab who left it untied trusting it to the will of Allaah The Most High: hobble the camel first and then leave it to Allaah The Most High.''[444]

Instances of insurance abound in the practice of the Arabs as exemplified by the custom of *al-Aqilah* which was a mutual agreement among tribes for the paternal relatives of a person charged with a case of murder to make contributions for the purpose of settling blood money to the victim's relations. This system of pooling contributions to assist

[440] See Ahmad R. & Auzzir, Z.A., (2012), *Takaful*, Pearson Malaysia, p. 12.
[441] Sahih Al Bukhari Kitab Al-Fara'id.
[442] *Ibid.*
[443] *Ibid.*
[444] Al Tirmidhi and Ibn Majah.

others in need encapsulates the idea of insurance. The tradition gained acceptance with the advent of Islam.

As mentioned earlier, a substantial number of the customs that existed in the pre-Islamic period of *Jahiliyya* were validated and acknowledged ''Islamic'' by the Prophet Muhammad (pbuh) when he said, '' the virtues of the *Jahiliyya* are accepted in Islam.'' The Prophet pbuh further elucidated this point in the constitution promulgated in Madinah:

> ''They (Muslims of the Quraish and Yathrib tribes) are one community (Ummah) to the exclusion of all men. The Quraish immigrants, according to their personal custom, shall pay the blood-rite (*Aqilah*) within their number and shall redeem their prisoners with the kindness and justice common among the believers.''[445]
>
> ''Believers are to other believers like parts of a structure that tighten and reinforce each other.''[446]
>
> ''The Believers in their affection, mercy and sympathy towards each other, are like the body- if one of its organs suffers and complains, the entire body responds with insomnia and fever.''[447]

Given the Qur'anic command to support one another and the *Sunnah* of Prophet Muhammad (pbuh) regarding reciprocal assistance, *Takaful* may be assumed as imperative in the lives of Muslim believers: ''…..a scheme anchored on camaraderie, placidity and shared fortification which offers reciprocal financial and other forms of

[445] Ahmad R & Auzzir, Z.A., *op cit*, p. 5.
[446] *Ibid.* See also (Al Bukhari and Muslim)
[447] Muslim.

assistance to the members (of the group) in case of explicit needs, whereby members jointly agree to donate monies in support of this collective goal.[448]

Still on the origins and development of *Takaful*, before the advent of the time of Prophet Muhammad (pbuh), invasions and plundering as reprisals were regular features of nomadic Arab life. The adversities of harsh desert life and a war-like watchfulness forged the coming together among various groups resulting in the group acting as a collective unit[449]. Muslehuddin observed that:

> ''….not only does the unit consider the loss of its individual member as its own, it also takes steps to cover such loss, either by revenge and blood-letting, or alternatively, by the payment of ''blood money'' on behalf of the individual.''[450]

Such a standpoint towards life and early communal bonding can be understood as an initial practice of Islamic insurance (conjoint self-protection).[451]

The custom of recompensing blood-money, or *wergild* was kept alive for nearly ten centuries as a safeguard against jeopardy to which an aggregate of individuals are all equally subjected to protection. An aggregate of tribesmen united by kinship and family ties comes to the assistance of a member through communal action. Hence the action of sharing is common. This practice was used for pillaged assets as well as recompense for the destruction of life in order to avert vendetta and unchecked devastation.[452] The Arabic word for blood bond is *Maaqil*, which is a derivative of *Aql* or *Aqilah.*[453]

During the advent of Islam (623-670 CE), some of these pre-Islamic norms, *Aqilah* inclusive, were endorsed by the Prophet (pbuh). In this way, these cultural practices

[448] Fisher, O and Taylor, D.Y., (2000), *Prospects for Evolution of Takaful in the 21st Century*, Havard University, USA. See also Ahmad, R. & Auzzir Z.A., *op cit*, p. 6.
[449] Rodziah, A and Zairol, A.A., (2013), *Takaful*, Pearson Malaysia Sdn Bhd, p. 3.
[450] http://www.takaful.com.pk
[451] *Ibid.*
[452] Rodziah, A and Zairol, A.A., (2013), *op cit*, p. 3.
[453] *Ibid.* The Prophet's pbuh rationale for upholding the tenets of *Aqilah* was that it served the good interest of society and ultimately united the warring parties. In this connection, the Muslims were practicing what was preached in the Noble Qur'an (*Surah Al-Nisa'* 4:92) which enjoined upon the believers not to waste human lives in retaliation but to let the law take its course and if the aggrieved party agreed to a reasonable compensation, brotherly love is better than retaliation.

became integrated into the *Sunnah* (aphorisms and practices of the Prophet (pbuh) and subject to principles of the *Shari'ah*[454]

The norm of *Maaqil* was acknowledged by the Prophet (pbuh) as encapsulated in the following narration of the *Sunnah*:

> ''Allaah (SWT) gave this verdict about two ladies of the Hudhail tribe who had fought each other and one of them had hit the other with a stone. The stone hit her abdomen and as she was pregnant, the blow killed the child in her womb. They both filed their case with the Prophet (pbuh) and he judged that the blood-money was for what was in her womb. The guardian of the lady who was fined said, O Allaah SWT! Shall I be fined for a creature that has neither drunk nor eaten, neither spoke nor cried? A case like that should be nullified. On that the Prophet (pbuh) said, this is one of the brothers of the soothsayers.''[455]

The Prophet (pbuh) adjudicated that the victim be compensated with either a slave or a bonds-woman as blood-money. Narrated by Ibn Shihab, Said bin Al-Mussayab said:

> ''Allaah (SWT) judged that in the case of a child killed in the womb of its mother, the offender should give the mother a slave or a female slave in recompense. The offender said, how can I be fined for killing one who has neither ate nor drank, nor spoke nor cried: a case like this should be denied. On that Allaah SWT said, he is one of the brothers of the foretellers.''[456]

Cooperative support amongst aggregate affiliates of a tribe was not originally a money-making venture and contained no yield or gain at the expense of others.[457] Rather, it

[454] Rodziah, A and Zairol, A.A., *op cit*, p. 3..
[455] Rodziah, A and Zairol, A.A., *op cit,*, p. 4.
[456] Sahih Bukhari, Volume 7, Book 71, Number 654-655, Narrated by Abu Hurrairah. The decree in this case was that Prophet Muhammad pbuh decided that the second woman's kin would pay a penalty to the relatives of the first woman whose baby was killed (*Aqilah*), in accordance with established custom.
[457] Obviously, no one will question the very aim of *Takaful*, which is to spread the risks and losses among the large number of participants. In other words, *Takaful* re-enforces the idea of shared responsibilities, joint indemnity, common interest and solidarity which are reasonable and acceptable to the people of a sound nation. Therefore, it is not an exaggeration to say that the concept of

developed as a communal institution to alleviate the burden of an individual by spreading the liability among his fellow aggregate associates (group) or clan. Contrastingly, most contemporary insurances (even joint stock insurance ventures, but not mutual associations) are a capitalist-based money-making undertaking, where losses are anticipated in advance and resources (premiums) apportioned to risks to shield them. Premiums are remunerated in line with such projections of peril.[458]

Succinctly, the erstwhile practice involved recompense for definite losses upon occurrence by spreading them amongst members of the group, whereas, the second involves the transmission of losses well in advance based on preceding experiences. This transmission is almost always from policyholders (the group) to shareholders (owner of insurance company) and thus negates the long-standing norm of reciprocal assistance.[459]

After the demise of the Prophet (pbuh), the companions continued to practice *Aqilah*. The perfect example can be observed during the period of Caliph Umar (r.a.) when the government encouraged people to practice *Aqilah* nationwide. *Diwan* of *Mujahiddeen* was well-known in districts whereby those whose appellations were etched in the *Diwan* owed each other reciprocal co-operation to donate the blood-money for any killings committed, whether it be from one's own tribe or another tribe.[460]

The Ottoman Empire was the first Islamic regime to introduce the concept of marine insurance, similar to what has been practiced by the West in its Maritime Code of

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Takaful has been practised by people in the early days of Islam based on the Islamic principles of mutual help and cooperation in good and virtuous acts.

[458] Rodziah, A and Zairol, A.A., *op cit*, p. 4.

[459] *Ibid*, p. 5.

[460] Rusni, H., (2011), *Islamic Banking and Takaful*, Pearson Custom Publishing, p. 185. See also Ahmad Nordin, M.T., (1990) Seminar on ''Introduction to Takaful'', Institut Teknologi MARA. Also see Billah, M., (2003), *Islamic and Modern Insurance*, Ilmiah Publishers, Malaysia. See also Rispler-Chaim, V., (1991) Insurance and Semi-Insurance Transactions in Islamic History until the 19th Century, *Journal of Economic and Social History of the Orient*, Vol. 34, No. 3, pp. 142-158. See also Rashid, S.K., (2005), A Religion Legal-Experiment in Malaysia, *Religion and Law Review*, 2(1): pp. 16-40.

1863[461]. In 1874, the Ottoman Law of Insurance was introduced to cover other aspects of non-life insurance.[462]

In the 19th century, a Hanafi scholar, Ibn Abidin, discussed the idea of insurance and its legal basis and successfully introduced the insurance concept as a legal institution where the practice of *Takaful* is based on the public interest.[463] In the 20th century, Muhammad Abduh issued a *fatwa* in 1900-1901 legalizing life insurance as in line with the teaching of the *Shari'ah*. He was also of the view that the contractual nexus between the insured and the insurance group is of a *Mudharabah* contract. This is because the insurance operators assume the role of the *Mudharib* while the insured is known as the *Rabbul-Mal*. This can be observed when the *Takaful* operator undertakes the role of entrepreneur and invests the pool of funds and specifies how the expected profit generated is to be shared among the insured. Thus, the mutual help among the insured is observed through the concept of *Tabarru'*.[464]

3.1.3 Legal Basis of *Takaful* Under other Sources of *Shari'ah*

Other sources of *Shari'ah* presuppose those medium of regulating issues of the law outside of the Noble Qur'an and the Prophetic *Sunnah* of Prophet Muhammad (pbuh). The *Ijma* or consensus of the Muslim jurists in a particular matter in Islamic jurisprudence has a binding legal effect.[465] The greater majority of renowned Islamic scholars are unanimous in their views that conventional insurance practice is unlawful as it stands due to the manifestation of elements of interest, gambling and uncertainty.[466]

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[461] Rusni, H., *op cit.*
[462] Nik, R. M., (1991), *Takaful: The Islamic System of Mutual Insurance-The Malaysian Experience*, Arab Law Quarterly, 6, p.281.
[463] *Ibid.*
[464] Rusni, H., (2011), *Islamic Banking and Takaful*, Pearson Custom Publishing, p.186.
[465] Consensus here does not necessarily mean all the scholars are on board. What it means is that a greater number agree that conventional insurance is unlawful as it stands due to the *Shari'ah* prohibitive factors. Of course, there are dissenting voices in any situation and Islam is no exception to such. Some scholars see nothing wrong at all with conventional insurance, however, that is not the majority voice, *Ijma* comes in because it is the voice of the greater majority.
[466] Most *Shari'ah* scholars agree that insurance contract cannot be considered as a contract of sale due to uncertainty in the subject matter of the contract. The subject matter of insurance relates to uncertain event such as death, injury, disability, fire and theft. These events may or may not occur. So there is uncertainty as to whether the subject matter of the insurance contract exists or not. There is also *Gharar* regarding the time compensation will be paid out, since the payment is conditional upon the occurrence of an uncertain event. Furthermore, the obligation of an insurer to pay compensation is conditional upon the occurrence of the loss, and the amount of insurance benefit is conditional upon the size of loss. While the insurer may or may not compensate the insured, depending on the occurrence of the loss, the insured has to continue paying premium regardless of the occurrence or non-occurrence

This means there is no ambiguity whatsoever concerning its prohibition in light of the principles of *Shari'ah.*

Through the concepts of *Ijma* and *Ijtihad,* Islamic scholars classified all matters either as *halal* (those permitted or lawful) or *haram* (those prohibited or unlawful).[467] In this instance, *Takaful* based on the concept of shared responsibility was held as *halal.*[468] In contrast, on the issue of conventional insurance, *Shari'ah* prohibits exploitation and risky investments and therefore the majority of jurists upheld its illegality as a result of *Gharar* (uncertainty) and speculative nature embodied in it.

The views of the scholars with regard to the legality of *Takaful* vary from one to another.

1. The majority of Muslim scholars including Shaikh Muhammad Abduh, Ibn Abidin (Hanafi), Mustafa Ahmad al-Zarqa', Al-Khafif all regard *Takaful* as lawful, provided that it is free from the elements if *Riba.*[469]

2. Some scholars such as Muhammad Abu Zahra, Shaikh al-Azhar, Shaikh Jad al-Haq, Ali Jad al-Haq, and the Muslim League Conference in 1965 legalized the practice of insurance or *Takaful* on asset or property only but not for life insurance. This is because life insurance involves elements of *Maysir* and *Gharar*.

3. Mustafa Zaid, Abdullah al-Qalqeeli and Jalal Mustafa al-Sayyad however, reject the practice of *Takaful* based on the arguments that *Takaful* involves elements of *Riba, Maysir* and *Gharar.*[470]

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of loss. See Abdul Rahman, Z. & Redzuan, H., (2009), *Takaful*, The 21st Century Insurance Innovation, McGraw-Hill, Malaysia, p. 23. See also Al-Qardawi, Y., (2001) The Lawful and Prohibited in Islam, Islam Book Trust, p. 37. See also Matraji, S., (2004) A Journey From the Commercial Insurance Contract to *Takaful*, 1st Islamic International Conference for Young Scholars, Langkawi, Malaysia.

[467] Other forms of classification of Islamic law apart from the two extremes of Halal (permitted) and Haram (prohibited) include Mubah, Mustahabb, and Makruh.

[468] See Fisher, O. & Taylor, D.Y., (2002), *Prospects for Evolution of Takaful in the 21st Century*, available at http;//www.takaful.com.sa/m4sub3.asp.openaccess.htm., where they reiterated that ''on the views of *Ulamas*, for as long as the *Shari'ah* conditions are met, i.e. risk sharing under the *Ta'awuni* principle, coincidence of ownership, participation in management by the contributors of funds or participants, avoidance of *Riba* at all costs and shying away from haram investments, and the incorporation of the management practices of *Mudharabah*, *Takaful* is definitely acceptable in Islam''.

[469] Rusni, H., *op cit.*

Due to the differences in opinions among Muslim sages regarding insurance contract, it has led to misconception among Muslims in respect of the same. The common misconceptions on insurance or *Takaful* can be summarized as follows:

(a) *Takaful* contains the elements of *Riba, Gharar* and *Maysir* where it is associated with risks and uncertainties in a contractual agreement. In *Takaful*, the customer is paying a certain amount of money (policy) for the protection of life, whereas in real life, there is the uncertainty of life and death.[471]

However, this perception is wrong since the subject matter of *Takaful* is dealing with life or property (in which the risk is assumed will occur in future), and not the exact time of death of a certain individual or the exact time of the damage done to the property. It is also wrong to claim that there exists an element of *Maysir* in which the aim is for a chance to gain material wealth while beating the other gamblers at the same time.[472]

Opponents argue that *Maysir* exists in the case of life insurance, when the sum paid out by the insurer in the event the insured dies during the earlier period of the contract, exceeds what the insured has paid in premiums. Another argument against *Takaful* is that policy money is paid together with bonuses and dividends. In the case of non-life insurance, the insured will recover more than what he has paid out as premiums in the event he suffers great loss over the insured property.[473]

(b) *Takaful* differs with the doctrines of *Mirath* and *Wasiyyah* (will and succession). This is because in life insurance, or *Takaful*, the nominee is the absolute beneficiary from the policy after the death of the insured. This will divest the rights of the legal

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[470] *Ibid.*
[471] Rusni, H., *op cit.*p. 187.
[472] *Ibid.*
[473] *Ibid.* This is untrue because the payment for the policyholder (in the case of early death or early termination) is from the social contribution fund provided by other policyholders based on the concept of *Tabarru'*. The *Takaful* concept deals with pure risk and not the speculative one. Thus, *Maysir* cannot be associated with *Takaful* since the element of risk that exists in *Maysir* is not a pure risk but instead creates new unnecessary speculative risks.

heirs based on the doctrines of inheritance (*Mirath*) and will (*Wasiyyah*). This contention is contradictory. This is because the nomination of the nominee in the policy as an absolute beneficiary is not a right conferred by insurance law. Instead, it is a right conferred by the contract between the insurer and the insured and can therefore be easily removed or modified without affecting the validity of the contract of the life insurance itself.[474] A nominee named in the insurance policy is no more than an executor who is under an obligation to collect the benefits from the policy on behalf of the heirs of the insured (deceased) and bestow the benefits.[475]

(c) *Takaful* is contrary to the principle of *Tawakkul*. The opponents' argument is based on the fact that the insured puts a trust in the insurer to protect him against unexpected loss instead of putting the trust in Allaah. This can be rebutted by understanding the real concept o*f Tawakkal*, whereby one does his best part to protect the risk and hope afterwards for the best by putting trust in God and His blessings. As *Takaful* is protection against the occurrence of loss, initiative or effort to the best of the insured's ability to overcome future unexpected difficulties, is always encouraged.[476] This was aptly summed in the Prophet's Hadith when he (pbuh) said to a Bedouin who left his camel untended:

> ''why don't you tie your camel? The Bedoiun answered: I put my trust in Allaah. The Prophet (pbuh) said to him: tie your camel first, then put your trust in Allaah.''[477]

In a nutshell, this study posits that all the misconceptions about *Takaful* arose as result of lack of understanding about the true nature and benefits of the concept - which is mutual assistance aimed at assisting orphans, widows, infirm, less fortunate and other

[474] Nik, R.M., *op cit*, p. 285.
[475] *Amtul Habib v Musarrat Parveen* (1974) PLD 185 (SC).
[476] Rusni, H., *op cit.*
[477] Sahih Bukhari and Sahih Muslim.

dependants as well as aiding one's self against unexpected future peril or losses. Most scholars are agreed in their analogical deductions that *Takaful* is perfectly legal and is here to play a very important role in the emerging commercial and world economic order.[478]

3.2 GENERAL PRINCIPLES OF *TAKAFUL*

Takaful insurance is not only subject to general principles of law of contract but has certain legal principles that are peculiar to the system. *Takaful* contract incorporates some principles of conventional insurance[479] on the concept of fairness in dealings as expounded by *Shari'ah.* The legality of *Takaful* contract is subject to the existence of operators established in accordance with the following *Shari'ah* requirements and other legal framework;[480]

a) ''*Niyyah* or utmost sincerity of intention to engage in and adhere to the rules of *Takaful*;

b) Integration of *Shari'ah* conditions namely: risk protection sharing under *Ta'awun* principle, coincidence of ownership, participation in management by policyholders, avoidance of *Riba* and prohibited investments, and inclusion of *Mudharabah* or *Wakalah* principles for *Takaful* management.

c) Presence of moral values and ethics. The business must be conducted purely in accordance with utmost good faith, honesty, full disclosure, truthfulness and fairness in dealings.

[478] See Fisher, O. & Taylor, D.Y., (2002), *Prospects for Evolution of Takaful in the 21st Century*, available at http://www.takaful.com.sa/m4sub3.asp.openaccess.htm.

[479] This underscores the importance of mutuality between the two distinct forms of insurance practice. Dato' Abdul Hamid Bin Haji Mohamad, Chief Justice, Federal Court of Malaysia, puts it succinctly when he opined that: ''what strikes me is that Islamic banking, insurance and finance are actually Islamized conventional banking, insurance and finance. The products are products of conventional banking, insurance and finance but ''Islamized'' by removing the features prohibited by *Shari'ah* and applying *Shari'ah* principles to achieve the same or similar effects. That Islamic banking, insurance and finance developed that way is a matter of practicality: that it is the only practical way to do so under the existing circumstances''. See Bakar, M.D. & Ali, E.R.A.E. (eds), (2008), Essential Reading in Islamic Finance, CERT Publications Sdn. Bhd, Kuala Lumpur, Malaysia, p. v.

[480] *Takaful* Elements; Academy for International Modern Studies, e-library/ Islamic Banking and Finance, p. 1.

d) No unlawful elements that contravene *Shari'ah* and strict adherence to Islamic rules for commercial contract, namely;

(1) Parties must have legal capacity (i.e. 18 years and above and mentally fit;

(2) Insurable interest

(3) Principles of indemnity

(4) Payment of contribution

(5) Mutual consent

(6) Specific period of policy and underlying agreement.''[481]

The fundamental principles that distinguish *Takaful* from conventional insurance are ethical in content in addition to the strict requirement for adherence to the principles of *Shariah*. The general principles of *Takaful* are derived from the textual authorities of the Noble Qur'an, traditions of the Prophet (pbuh) and the practices of the people of Madinah.

3.2.1 Insurable Interest under *Takaful*[482]

Insurable interest is the legal right to provide cover/insurance arising from the legitimate financial interest which a participant/insured has in a subject matter of *Takaful*. If the subject matter of *Takaful* is not legally recognized, it lacks the necessary insurable interest to effect a valid *Takaful*. Example: a thief cannot effect a valid *Takaful* on the goods stolen by him.[483]

[481] *Takaful* Elements; Academy for International Modern Studies, e-library/ Islamic Banking and Finance, p. 1.
[482] The concept of insurable interest under *Takaful* is basically the same as that found under conventional insurance, except here, the *Shari'ah* prohibitive elements embedded in conventional insurance practice are removed to make it *Shari'ah* compliant otherwise it is void. That is why *Takaful* is often referred to as 'insurance with a human face' because of its ethics-based content. To those who may not be Muslims, the equity factor where premium is returned at the end of the transaction is considered a fair business deal.
[483] Nasser, Y & Jamil, R., (2011), *Takaful*: A Study Guide, IBFIM, Kuala Lumpur, p. 105.

For general *Takaful* contract, insurable interest must be present at the commencement and at the time of occurrence of the peril insured against – otherwise, the *Takaful* insurance is void. For example, a person cannot authentically arrange for motor *Takaful* on a car which he expects to possess in the future.[484]

However, this general rule is not applicable to marine *Takaful*. In marine *Takaful*, the participant/insured must have insurable interest at the time a loss ensues to be able to enter into a binding contract. Example: Due to the nature of business transaction, an importer of goods will be able to genuinely arrange for *Takaful* on the goods or merchandise he expects to import so long as he later secures insurable interest that is by acquiring ownership of the goods prior to the occurrence of an insured peril.[485]

For family solidarity *Takaful*, insurable interest must be present at the commencement of the contract only. The policyholder only needs to have insurable interest at the time of entering the family *Takaful* contract.

Nasser and Jamil, stated that

> ''In property *Takaful* (*Takaful* cover related to property), an owner, trustee, agent, mortgagee or hirer has insurable interest on the property owned, held in trust, held in commission, mortgaged and hired respectively. However, liability *Takaful* can be effected by anyone who has potential legal liability and legal costs and expenses associated with it. With respect to personal accident *Takaful*, a person has unlimited insurable interest for his own. Under the Malaysian *Takaful* Act[486], a person shall be deemed to have insurable interest in relation to another person who is his spouse, child or minority at the time the *Takaful* is

[484] Nasser, Y & Jamil, R., *op cit*, p. 104.
[485] Nasser, Y & Jamil, R., *op cit*, p. 105..
[486] The 1984 Malaysian *Takaful* Act has been repealed and replaced by the new Islamic Financial services Act, 2013. The new Act has the *Takaful* Act and the Banking Act under one umbrella – The Islamic Financial Services Act. The same changes have also been effected in the conventional sector where you now have the Financial Services Act, 2013. Most of the provisions in the *Takaful* Act remain exactly the same.

effected; his employee; or a person on whom he is at the time the *Takaful*, wholly or partly dependent.''[487]

3.2.2 Principle of Utmost Good Faith

Utmost good faith is an obligation of the insured to disclose material facts[488]. A material fact is a fact that would influence the judgment of a prudent underwriter in deciding whether to accept a risk for insurance and on what terms. The proposer has a duty to disclose material facts at the inception, renewal and in respect of mid-term alterations where there has been a change in risk. Example: a person's health history is a material fact for a life insurance policy. However, the information is not a material fact for a fire policy.[489]

Though the insurance company must reciprocate, in practice the duty weighs more heavily on the insured. A breach by the insured makes the contract *voidable ab initio* at the company's option. Breaches may be through concealment; non-disclosure; fraudulent misrepresentation and innocent misrepresentation. The duty is pre-

[487] Nasser, Y. & Jamil, R., *op cit.* See also Alhabshi, S.O., *et al* (2012), *Takaful*: *Realities and Challenges*, Kuala Lumpur, Pearson Malaysia, p. 563.
See generally, Islamic Financial Services Act, 2013 which refers to insurable interest as permissible *Takaful* interest. This requirement was not specified under the 1984 *Takaful* Act. See specifically paragraph 3, Schedule 8 of the IFSA 2013. Further see paragraphs 3(1), 3(3) and 3(6) on the applicability of permissible *Takaful* interest/insurable interest in Family *Takaful* and the effect of lack of it thereof. It should be noted that although the concept of permissible *Takaful* interest has been inserted in the IFSA 2013, it seems that schedule 8 of the IFSA 2013 only caters for permissible *Takaful* interest only in Family *Takaful* Business whereas it kept mute in relation to its application under General *Takaful* Business. This is an area of controversy likely to play out in the coming years and a veritable field for further research.

[488] A material fact need not be in *totidem verbis* (in so many words); a word spoken if it is material will suffice and will by necessary implication pass the test of utmost good faith. See *MacKenzie v. Coulson* (1869) L.R. 8 Eq. 368., where the court said ''there is no class of documents as to which the strictest good faith is more rigidly required in courts of law than policies of insurance''. See also *London General Omnibus Co. Ltd. v. Holloway* (1912) 2 K.B. 72., where the court held inter alia, ''No class of case occurs to my mind, in which our law regards mere non-disclosure as a ground for invalidating a contract except in the case of insurance. That is an exception which the law has widely made in deference to the plain exigencies of this particular and most important class of transaction''.

[489] Ezamshah, I. (2011) *Basic Takaful Broking Handbook*, IBFIM, Kuala Lumpur, p. 77. An interesting contrasting point of note here is that in Nigeria, the Insurance Act, 2003 modified the common law principle of utmost good faith to suit the local environment. Section 54(1) of the Act shifted the burden of materiality of information from the insured or proposer to the insurer by requiring that all proposal forms should elicit such information considered by the insurer to be relevant. This is in total contrast with the provisions of standard common law insurance practice. The confusion here with regards to *Takaful* application in Nigeria is that will *Takaful* application in Nigeria follow the normal standard practice in the world or is it going to adjust to the requirements of Section 54 of Insurance Act, 2003? The *Takaful* Operational guidelines 2013 have not made specific provisions insulating the *Takaful* Guidelines from the authority of the Act which is the foremost insurance legislation in Nigeria. The imperative for the harmonization of these regulatory discrepancies in the enabling instruments of the Nigerian insurance industry gives this thesis unprecedented legitimacy and importance because the whole research is premised on these regulatory challenges.

contractual but revives at the renewal stage and to certain mid-term alterations affecting the risk.[490]

Concealment is defined as the wilful failure to disclose a material fact before the insurance contract is concluded. It is a breach of utmost good faith rendering the contract *void ab initio* and entitling the company to sue for damages because of deceit. If fraud is proved, the insured is not entitled to a return of premium.[491]

Non-disclosure by the proposer before the insurance contract has been concluded may render voidable *ab initio* but the option of doing so lies with the company. If the company exercises the option, then, the full premium will be returned. Fraudulent misrepresentation is also a beach of the duty of utmost good faith and it occurs when the person knowingly makes a false statement relating to a material fact, does not believe it to be true or makes it recklessly without due regard to its accuracy.[492]

Sometimes, the proposer may unintentionally supply misleading information relating to a material fact and this can be in breach of the duty of utmost good faith. Where the company exercises the right of avoidance *ab initio*, the risk does not exist and the full premium must be returned. Under the industrial code of practice of some developed countries, companies have agreed not to avoid policies issued to private individuals where the innocent misrepresentation is due to nature of a technical error.[493]

This is in line with the two-step test that was laid down by the House of Lords in *Pan Atlantic v. Pine Top* (1995). The two-step test enables the companies to have a right to treat the certificate/policy as avoided if the facts misstated or withheld are material in

[490] Ezamshah, I., *op cit*, p. 78.
[491] *Ibid.*
[492] See *Unic v. Unic Ltd* (1999) 3 NWLR p. 18., where the court held that ''a contract of insurance is a contract of the utmost good faith *uberrimae fidei*. It is the duty of the parties to help each other to come to a right conclusion. It is the duty of the insured not only to be honest and straightforward but at all times to make full disclosure of all material facts. In the same vein, it is the duty of the insurers and their agents to disclose all material facts within their knowledge''. See also MacGillivray and Parkington (1988) *Insurance Law*, 8th Edition, p. 544, where it was mentioned that good faith forbids either party by concealing what he privately knows to draw the other into a bargain from his ignorance of that fact and his believing the contrary. However, whether a contract requires utmost good faith or not depends on its substantial character and how it came to be effected. See *Lee v. Jones*, (1864) 17 K.B. 482.
[493] *Ibid.*

the objective sense that they would have been of interest to a prudent underwriter in the market at the time; and had the subjective effect of inducing the actual companies to enter into the certificate/policy on the terms finally agreed.[494]

However, in this case, the House of Lords is of the opinion that the insured is not required to disclose facts:

(i) Which he did not know and could not have known in the ordinary course of his business;[495]

(ii) Which diminish the risk;

(iii) Which were known or ought to have been known by the companies;

(iv) Which were waived by the companies; or

(v) Which are covered by an express term in the certificate/policy.

From the *Shari'ah* view point, the principle of utmost good faith is in line with Islamic teachings as contained in the verses of the Noble Qur'an where Allaah, The Exalted said:

> ''O you who believe! Eat not up your property – among yourselves in vanities: but let there be amongst you traffic and trade by mutual good-will: nor kill (or destroy) yourselves: for verily Allaah hath been to you Most Merciful.''[496]

[494] The principle of utmost good faith applies to all kinds of insurance policies. Anyone who proposes to insure is bound to tell the insurer all facts, which he knows or he ought to know which would influence the mind of a prudent insurer. The material facts are meant to give a complete picture of things to be insured to enable the insurer to decide whether to accept, reject or accept at a higher premium and on which terms. The contention seems to be that the proposer knows everything and that the insurer knows nothing of the subject matter, it is therefore the duty of the insured to present up-to-date facts to the insurer. The requirement of good faith is satisfied by acting in disinterested manner, without any conflicting consideration of self-interest and also considering the interest of the parties. See The Business Lawyer, Vol. 42, No. 2, February 1987 at p. 409. See also Ezamshah, I., *op cit.* See also *Law Union and Rock Insurance Ltd. v. Onuoha* (1998) NWLR (pt 555) 576 at 588., where the court stated that ''a thing is, however, deemed to have been done in good faith when it is in fact done honestly''. See also *Akpata and Garrick v. African Alliance Co. Ltd.* (1967) NWLR 12.

[495] See *Joel v. Law Union and Crown Insurance Company* (1908) 2 K.B. 863. See also *Akpata and Anor v. African Alliance Insurance Co. Ltd.* (1969) FNLR 111.

[496] Al- Nisa', Chapter 4, Verse 29.

Furthermore, in a Hadith related by Hakim ibn Hazim who reported that the Prophet (pbuh) as saying:

> '' Both parties in a business transaction have the right to annul it so long as they have not separated; and if they speak the truth and make everything clear, they will be blessed in their transaction; but if they tell a lie and conceal anything, the blessing in their transaction will be blotted out.''[497]

In another Hadith related by Abdullahi bn Dinar who narrated that he heard Ibn Umar as saying;

> '' a man mentioned to the Prophet (pbuh) that he was deceived in a business transaction, whereupon the Prophet (pbuh) said: 'when you enter into a transaction, say: there should no attempt to deceive.''[498]

3.2.3 Indemnity[499]

Takaful contracts promise to make good the participant's/insured's loss or damage. When a loss takes place, the sum which the participant can recover is called the 'measure of indemnity'. The dictionary meaning of the word indemnity is compensation for losses or injuries sustained. The principle of indemnity requires the operator to restore the participant to the same financial position as he had enjoyed immediately before the loss.[500]

All property and pecuniary *Takaful* are contracts of indemnity i.e. the amount payable on the happening of an event insured against is limited to the extent of participant's pecuniary loss only. Thus, the intention of the *Takaful* operator following a loss is to

[497] Sahih Bukhari and Sahih Muslim.
[498] Sahih Bukhari and Sahih Muslim..
[499] It is a fundamental principle of insurance law that all insurance policies, except those of life and personal accident, are contracts of indemnity. When an insurance policy is said to be a contract a contract of indemnity, it means that in the event of a loss arising from an insured peril, the insured shall be placed in the same position that he occupied immediately before the happening of the event insured against. See *Dalby v. India and London Life Assurance Co.* (1854) 15 CB. 365; of course, it is virtually impossible to restore the assured back to life in life assurances or to restore the insured's blinded eye back to normal in personal accident insurances. In these instances, the principle of indemnity does not apply. There can only be a claim for the insurance money on the happening of these events by the insured.
[500] Nasser, Y & Jamil, R., *op cit*, p. 107.

restore the participant to the same pecuniary position as he occupied immediately before its occurrence, subject to adequacy of sum insured and other restrictions such as application of average, excess and limits.[501] Indemnity fixes the maximum payable under a *Takaful*, subject to the limit of sum insured. The sum insured is the limit of the operator's liability.[502]

General *Takaful* contracts are contracts of indemnity where insurable interest is measurable, for example property, pecuniary and liability *Takaful* contracts. Personal accident and family solidarity *Takaful* contracts are not strictly contracts of indemnity. The measure of indemnity depends on the nature of *Takaful*. Generally, indemnity in property *Takaful* is based on either replacement cost less depreciation, or the market value; while in liability *Takaful*, it is measured by the amount of court award or negotiated out of court settlement plus approved costs and expenses. Indemnity in pecuniary *Takaful* is measured by the amount of financial loss suffered by the participant. In a Fidelity Guarantee *Takaful* Scheme, indemnity is measured by the amount financial loss suffered as a result of an employee's dishonesty. *Takaful* operators may use the following methods to indemnify losses: payment by cash, repair, replacement or reinstatement.[503]

3.2.4 Subrogation[504]

This is a corollary of the principle of indemnity. Subrogation is the right of an operator who has granted an indemnity to receive, after payment of a loss, the advantage of every right of the participant, against a third party who has caused a loss. This right is implied

[501] *Ibid*, p. 108. Here, the participant can only claim for the material loss sustained i.e. sentimental losses or consequential losses of any kind are excluded. Moreover, the participant cannot make a fortune from the misfortune suffered by him. Where the damage is partial, the participant is not entitled to claim a total loss, but is entitled to claim only for the amount of actual damage incurred. Where the participant has been fully indemnified, he must transfer to the operators all his rights against third parties; the participant cannot obtain further indemnity from third parties because that would amount to making profit. (This concerns the rights of subrogation). The participant is not entitled to recover his loss more than once irrespective of the number of policies he holds; he may not obtain more than the full amount of the loss from various insurers. (This concerns the principle of contribution).

[502] Nasser, Y & Jamil, R., *op cit*, p. 107.

[503] *Ibid.*

[504] The doctrine of subrogation arises in all policies, which are contracts of indemnity. Contracts of indemnity include marine insurance policies and others like fire, motor, fidelity, burglary to mention a few. The objective of subrogation is to prevent the insured from recovering more than full indemnity. See *Castellan v. Preston* (*supra*), per Brett, L.J. See also *John Edwards and Co. v. Motor Union Insurance Co. Ltd* (1922) KB 249. The doctrine is based on equitable considerations. It is not an original right but a secondary one, which requires certain conditions to be satisfied before the right can be claimed.

in all contracts of indemnity. It need not, therefore, be expressed in such contracts, although in practice it almost always is.

Before the implied right of subrogation operates in favour of the operators, two conditions must be fulfilled:

a) The *Takaful* contract must be one of indemnity. Therefore, subrogation does not apply to non-indemnity certificates like personal accident *Takaful* and family solidarity Takaful contracts.

b) The operator must have settled the claim. In practice, the operators by expressly stating this condition in the certificate usually obtain these subrogatory rights before the payment of claim.[505]

3.2.5 Contribution[506]

Contribution is another corollary of indemnity. It is also an implied condition in a contract of indemnity whereby if any other contract (or contracts) of indemnity is in existence covering the same interest in the same subject matter against the same peril, any claim must be apportioned amongst all the operators. Contribution applies to contracts of indemnity only, and the following conditions must exist before the principle of indemnity can be applied:

(i) The same interest (i.e. when the same person participated with the same interest with more than one operator).

[505] Contrast this *Takaful* provision with that of conventional insurance where the doctrine has been modified. Though subrogation is vested in the insurers after they have paid the claims made against them, by the insured not before, however, in recent times a practice has developed whereby a clause or a condition embodied in all non-marine policies provides that the insurers may exercise their subrogation right before payment has been made. The effect of this clause is to modify the common law doctrine of subrogation to the extent that the insurers may be subrogated to the insurer's rights and remedies before payment has been made. This in effect prevents the insured from waiving or compromising his rights against third parties having been indemnified by the insurers. In Nigeria, this clause is, however, against the provisions of the Marine Insurance Act, 1961 on subrogation as it provides that the insurer's subrogation right arises only after indemnifying the insured.

[506] Contribution is a principle which originated from equity and not contract. It is a part of the principle of indemnity that a person may take out as many policies as he desires against the same risk but when a loss occurs, he is also free to demand payment from any of his insurers, but he cannot recover more than his indemnity. See *Scottish Amicable Heritage Securities Association v. Northern Assurance Co.* (1883) 11 R. 287.

(ii) The same subject matter (i.e. both policies must cover the same item in respect of which a claim is made).

(iii) The same peril (i.e. both the policies include the same perils which caused the loss).[507]

By expressly incorporating a condition of contribution in the *Takaful* certificate, the operators will not be liable to pay or contribute more than its rateable proportion of any loss, damage, compensation or expense. If this condition is not expressed in the policy, the participant will have a right to claim against either of the operator/insurer. Subsequently, the operator that has paid the loss proceeds against the other operator and recovers his rateable proportion.[508]

A good example to understand the principle of contribution in *Takaful* is where a participant, in compliance with the requirement for his housing loan, had purchased a fire *Takaful* insurance for his property, without knowing that his banker had also done the same, effectively having two certificates covering the same interest and peril. In the event of a claim, both operators will contribute their rateable portion of the loss so that the participant does not make a 'profit' by having two operators paying for the same claim.[509]

[507] Nasser, Y. & Jamil, R., (2011) *op cit*, p. 109.
[508] Nasser, Y. & Jamil, R., *op cit.* See also *Sickness and Accident v. General Accident* (1892) 19 R (Ct of Session) 977d per Lord Low
[509] *Ibid.* See also Section 81(1) of Marine Insurance Act, 1961, which provides that '' where the assured is over-insured by double insurance, each insurer shall be bound, as between himself and other insurers, to contribute rateably to the loss in proportion to the amount for which he is liable under his contract.
(2) If any insurer pays more than his proportion of the loss, he shall be entitled to maintain an action for contribution against the other insurers, and be entitled to the like remedies as a surety who has paid more than his proportion of the debt''.
Lord Mansfield also stated in *Godin v. London Assurance Co.* (1758) 1 Burr. 489, that if the insured is to receive but one satisfaction, natural justice says that the several insurers shall all contribute pro-rata to satisfy that loss against which they have all insured. See also *American Safety Co. of New York v. Wrightson* (1910) 16 Comm. Cas. 37.

3.2.6 Proximate Cause[510]

In an insurance claim, the insurer is only liable for a loss caused by an insured peril. The insurer is not liable for a loss caused by either an uninsured peril or excluded peril. Losses may arise due to two or more causes which involved both the insured and excluded perils. This principle provides that when a loss is the result of many causes, the proximate cause (the dominant or effective cause) must be identified and attributed as the cause of the loss.[511]

In *Pawsey v. Scottish Union and National* (1907), the court stated that the:

> '' proximate cause means the active, efficient cause that sets in motion a chain of events which brings about a result, without the intervention of a starting force and working actively from a new and independent source.''[512]

Example: under a fire policy damages, as a result of smoke from a fire, is non-claimable if it is excluded. However, if the policy is silent with regards to damages as a result of smoke emission, the company is liable for the loss.[513]

3.2.7 *Tabarru'* (Donation)

Tabarru' (literally means donation) is a shared responsibility and shared guarantee principle which explicitly mentions that the money collected is to be used for the

[510] ''*Causa proxima non remota spectatur* ''– 'the proximate and not the remote cause must be looked into'. In effect, the proximate cause may not be the first, the last or the sole cause of the loss; it must be the dominant, effective or operative cause of the loss. See *Leyland Shipping Co. v. Norwich Union Fire Insurance Society* (1918) A.C. 350; See also *Yorkshire Dale S.S Co. v. Minister of War Transport* (1942) A.C. 691. In insurance policies, as in all commercial documents of similar nature, the proximate rule depends on the presumed intention of the parties. See *Becker Gray v. London Assurance* (1918) A.C. 101, 112, per Lord Sumner. The insurers are liable for any loss which is proximately caused and within the risks covered, but they are not liable if it is within the excepted perils. See *Samuel v. Pumas* (*supra*)

[511] Ezamshah, I. *op cit*, p. 83.

[512] See Ezamshah, I. *op cit*, p. 83.. The *causa proxima* rule is not a statute law; therefore the practical working often presents some difficulties. It must be borne in mind that the doctrine of proximate cause is based upon the presumed intention of the parties, and this intention must not be arbitrarily defeated.

[513] Ezamshah, I., *op cit.* Proximate cause in Islamic insurance is exactly as it is under conventional insurance. There is nothing in it which violates Shariah rules and principles. In essence, this means where there is no such violation, conventional insurance basis could be of persuasive authority. This researcher has not been able to come across a single basis of proximate cause in any literature in the course of the study.

purpose of assisting 'fellow participants who require assistance according to the terms agreed as long as these terms are not in conflict with the *Shari'ah*.[514]

In general and family *Takaful* business, *Tabarru'* (*Takaful* donation) is a contract where a participant agrees to donate a pre-determined percentage of his contribution (to a *Takaful* fund), the purpose of which is to provide assistance to fellow participants in the event they suffer defined losses. In this way he fills his obligation of joint guarantee and mutual help should another participant suffer a loss. This concept eliminates the element of *Gharar* (uncertainty) from the *Takaful* contract.[515]

Taking into account these basic *Takaful* concepts, practitioners have taken a step further to expand the model into a more commercially viable model of *Takaful*. In practice, whenever one of the members suffers a defined loss and makes a legitimate claim, operators would settle the claim by using funds from the *Tabarru'* pool. In the meantime, the funds in the pool are invested in *Shari'ah*-compliant investment portfolio without exposing the certificate/policy holders to any extra significant risk. Islam accepted this principle of reciprocal compensation and joint responsibility.[516] The concept of *Tabarru'* also eliminates the issues of mistake, fraud and misrepresentation because the donor voluntarily gives away his right or contribution to the benefit of co-participants.

3.2.8 The Prohibitive Elements in *Takaful*[517]

As Islam does indeed support and encourage the management of risks, one might rightly ask why conventional insurance is not allowed. There have been many rulings by Islamic scholars stating that conventional insurance as currently practiced is unlawful

[514] Nasser, Y & Jamil, R., *op cit*, p. 114.
[515] *Ibid.*
[516] Nasser, Y & Jamil, R., *op cit*, p. 114.
[517] These prohibitive elements in *Takaful* are what distinguish *Takaful* insurance from conventional insurance otherwise both systems of insurance are the same thing. The end product of any insurance scheme is the indemnification of the insured and returning him to the position he was before the occurrence of the unfortunate event insured against.

under Islam as it contains elements prohibited under the *Shari'ah*, namely *Riba*, *Gharar* and *Maysir* as well as haram elements.[518] These are considered *seriatim* below.

3.2.8.1 *Riba*[519]

Riba literally means increase, addition, expansion or growth. It is understood here as an increase incurred upon usurious items and upon debt, due to the deferred payment term. This is underlined in a well-known Hadith:

> ''Gold is to be paid for by gold, silver by silver, wheat by wheat, barley by barley, dates by dates, and salt by salt, like for like and equal for equal, payment being made hand to hand. If these classes differ, then sell as you wish if payment is made hand to hand.''[520]

Riba, thus, applies to certain goods as well as gold and silver and by extension also to currency. The Hadith states that trade in goods of the same type and kind but different quantities is prohibited. Two types of *Riba* are usually referred to in Islamic finance:

(a) *Riba al-Nasi'ah* refers to the charging of interest on loans or payment of interest on deposits. It is also known as *Riba al-Jahiliyyah* (pre-Islamic era) whereby an interest rate is charged in excess of the loan principal if the borrower is unable to repay the debt at an agreed time. *Riba al-Nasi'ah* is confined only to monetary loans. Contemporary examples include late payment charge or the imposition of interest on credit card charges not fully paid.[521]

(b) *Riba al-Buyu'* was not common during the *Jahiliyyah* period. It was until the 7th year of the *Hijrah* when Prophet Muhammad (pbuh) was reported to have said:

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[518] Tobias, F. & Younes S., (2010), *Takaful* & Re*Takaful*, IBFIM, Kuala Lumpur, p.118.
[519] See Ahmad, R. & Auzzir, Z.A., *op cit*, p. 10, where they stated that *Riba* is taken from the Arabic word that means interest. There are many verses in the Noble Qur'an that prohibit *Riba*. What constitutes *Riba* has always been a disagreement among scholars. Some scholars are of the opinion that interest, whether on principal or late payment is *Riba*. According to scholars, as an insurance contract is a contract of exchange, there exists *Riba al- Fadhl* and *Riba al-Nasi'ah* simultaneously.
[520] Sahih Muslim.
[521] Tobias, F. & Younes, S., *op cit*, p.119.

''gold is to be paid for by gold, silver by silver, wheat by wheat, barley by barley, dates by dates, and salt by salt, like for like and equal for equal, payment being made hand to hand. If these classes differ, then sell as you wish if payment is made hand to hand.''[522]

This type of *Riba* is of two sub-categories:

(c) *Riba al-Fadhl* refers to the exchange of *Ribawi* items i.e. the six items mentioned in the *Hadith* above, on spot basis but with a difference in value. For instance, selling 10 grams of gold for 15 grams of gold on spot.

(d) *Riba al-Nasa'* refers to exchanging *Ribawi* items on deferment basis. E.g. exchanging 100kg of salt now against 120 of salt in one year.[523]

Riba[524] is strongly condemned by the Qur'an[525] and Sunnah. Monetary capital in the conventional system is treated on par with production factors like land or labour, each being entitled to a return (rent, salary) regardless of profit or loss. However, a key principle of the Islamic financial system is that any profit from trade and business has to be accompanied by a liability or a risk. Money capital in Islamic finance is here seen as being on par with an enterprise that comes with both risks and rewards.[526]

While *Riba* is prohibited, it certainly does not imply that every increase or growth has been prohibited by Islam. Profit leads to an increase in the principal amount, but it has not been prohibited.

[522] Sahih Muslim.
[523] Tobias, F. & Younes, S., *op cit,* p. 119.
[524] In essence, *Riba* is seen as a premium that must be paid along with the principal amount as a condition for the loan or for an extension of its maturity. This gives *Riba* the same meaning as interest. The rationale behind the prohibition is to ensure justice and remove all forms of exploitation through 'unfair' exchanges. Interest is unjustified based on the arrangement that the financier is assured of a positive return without sharing in the risk, while the entrepreneur is not assured of such positive return. *Riba* represents, in the Islamic value system, a prominent source of unjustified advantage. See Abod, S.G.S., Agil, S.O.S. & Ghazali, A. H. (eds.), (2008) *An Introduction to Islamic Economics & Finance*, CERT Publications Sdn Bhd., Malaysia, p. x.
[525] Condemnation of Riba in the Noble Qur'an could be found in twelve different places. These include: Verses 130-131 of Surah al Imran, 276-82 of Surah al Baqarah, 161-162, Surah al Rum etc.
[526] *Ibid.* See the word *Riba* in Ibn Manzur's lisan al 'Arab (Beirut: Var Sadir Li al Taba'ah wa al Nashr (1968), vol. 14, pp. 304-307), al Zubaydi's Tajal 'Arus (Cairo: Al Matba'ah al Khairiyyah, (1306), vol. 10, pp. 142-143 and Raghid al Isfahani's *al Mufradat fi Gharib al Qur'an* (1961), Cairo: Mustafa al Babi al Halabi, pp. 186-7). The same meaning is also unanimously indicated in all classical Qur'an commentaries.

Pre-agreed payments are also allowed under the *Shari'ah*, for instance fixed rental income from a leasing arrangement (*Ijarah*). The point is that there is still an element of risk for the parties involved, unlike in a conventional 'I owe you' (IOU) relationship.[527]

As is often the case under *Shari'ah*, different interpretations exist and a few *Shari'ah* scholars have challenged this strict interpretation of *Riba* and argue that only excessive commercial interest is prohibited (e.g. charged by loan sharks). However, the general and widely accepted view is that any form of interest is prohibited under the *Shari'ah*, whether at a 'reasonable' or an 'excessive' rate. A few isolated opinions expressing a different view do not create a dent in the consensus.[528]

As regards conventional insurance, there are two obvious areas of *Riba* transactions:

> (1) Paying and/or receiving interest is not permissible; in insurance companies this relates to the investment side (e.g. investments in fixed interest rate assets like deposits or bonds) as well as to the liability side (e.g. interest on policy loans).[529]
>
> (2) There is a mismatch between premiums paid and claims benefit received. The discrepancy is both between the amount paid and the difference in timing (*Riba al-Fadl* and *Riba al-Nasi'ah*). It could be partially solved if the claims amount were restricted to the sum of the premiums paid, but limiting it to this amount would make insurance of limited or questionable use to the buyers[530].

[527] Tobias, F. & Younes, S., (2010), *op cit*, p. 119. See Chapra, M.U., (2008) in *An Introduction to Islamic Economics and Finance: The Nature of Riba and Its Treatment in the Qur'an, Hadith and Fiqh*, *op cit*, p. 47. See also Abd. A; Karim al Khatib, *Al Siyasah al Malaiyyah fi al Islam*, (1975), Beirut: *Dar al Ma'rifah*, pp. 141-6.

[528] Tobias, F. & Younes, S., *op cit*,. ''The Muslims are agreed on the authority of their Prophet pbuh that the condition for an increase over the amount lent is *Riba*, irrespective of whether it is a handful of food, as indicated by Ibn Mas'ud, or a particle of grain'' (Muhammad bin Ahmad al Qurtubi, *Al Jami' li Ahkam al Qur'an*, popularly known as *Tafsir Qurtubi*, (1967), Cairo: *Dar al Kitab al 'Arabi li al Taha'ah wa al Nashr*, vol. 3, p. 241.

[529] This does not mean that if the insurance premium were to be invested in non-*Riba* yielding ventures it would make conventional insurance permissible under Islamic law because there are several other components of *Shari'ah* which need to be complied with, not just the *Riba* aspect alone. The insurance undertaking must have total and full compliance with *Shari'ah* principles before it can be adjudged compliant. These have been discussed throughout the thesis.

[530] Tobias, F. & Younes, S., *op cit.*

3.2.8.2 *Gharar*[531]

Gharar can loosely be translated as uncertainty, but the definition varies by *Madhhab* (school of thought). Commonly found definitions of *Gharar* include 'that whose consequences are hidden', 'that whose nature and consequences are hidden', 'that which admits two possibilities, with the less desirable one being more likely' or 'that whose consequences are unknown'. Economically, it can be compared to asymmetric information.[532]

Gharar, for instance, means that it is not acceptable in contract arrangements to make payments conditional upon the outcome of an uncertain event. This might apply to 'selling fish in the water' or the 'fruits on the trees at the beginning of the season'. It may result in the unjustifiable disadvantage/loss of one party and equally undue enrichment of the other. *Gharar* is forbidden in order to ensure the full consent and satisfaction of the parties to a contractual agreement. This can only be achieved through certainty, full knowledge, disclosure and transparency.[533]

Unlike *Riba*, which makes any business transaction involving it prohibited, it is understood that uncertainty cannot be totally avoided in any business; it is excessive uncertainty that is prohibited. Uncertainty or risk in respect of the business outcome, or *Ghurm*, is an inherent feature of Islamic finance and is allowed. That is why uncertainty is classified into two types, major and minor. *Gharar Fahish* is minor and is tolerated while *Gharar Yasir* is major and is forbidden.[534]

[531] See Wan Ahmad, W.M., (2008) *Some Issues of Gharar (Uncertainty) in Insurance: in Essential Readings in Islamic Finance*, Bakar, M.D. & Ali, E.R.A.E., eds., *op cit*, p. 251. The word *Gharar* comes from the root verb *Gharara* signifying to reveal oneself and one's property to destruction without being aware. Generally, it means danger, risk, peril, jeopardy or hazard. See also Ibn Manzur (1990), *Lisan al-'Arab*, vol. 4, p. 314.
[532] *Ibid.*
[533] Tobias, F. & Younes, S., o*p cit*, p. 121. See also Yusoff, S. (1998), *Defective Contracts in Islamic Commercial Law: With Special Reference to al-Ghabn, al-Istighal* and *al-Gharar*, pp. 206-229, Rayner, pp. 216-239. See also Sanusi, M.M., (1993), 'Gharar', *International Islamic University of Malaysia Journal*, vol. 3, no. 2, p.88.
[534] See Wan Ahmad, W.M., *op cit*, p. 255. See also Rahman, A., (1984), *Economic Doctrine of Islam*, vol. 4, pp. 134-140.

The uncertainty in conventional insurance is that both the timing and the amount of an insured event are unknown at the inception of the policy. Opinions vary on whether this uncertainty can be classified as excessive, taking into account that the policyholder is informed about this condition in his policy contract. Other experts have argued that overall the uncertainty might not be major, as the pricing is based on credible mortality and morbidity tables. Although there is uncertainty as to the time of an individual's death, actuaries can predict the mortality of the total portfolio of insured with reasonable certainty, based on the law of large numbers. However, this may remove the uncertainty for the insurer but not for the insured and each contract has to be considered independently.[535]

3.2.8.3 *Maysir* (Gambling)[536]

Maysir can be closely aligned to gambling, gaming or wagering. Expanding its meaning, *Maysir* refers to a situation in which unnecessary risk is created by entering into a transaction with a hope of gain and a fear of loss. It also implies to a condition that involved undertaking of risk in the spirit of speculation.[537] Islam views insurance transaction to have some resemblance to gambling or wagering. The insured pays instalment of premium, and if a defined loss occurs by chance, a large sum of money, which the sources are not made known, will be collected from the insurer. There is also a possibility that an insurance contract is entered into with speculative purposes. Moral hazards such as intentionally causing a loss, faking a loss, submitting fraudulent claim

[535] Tobias, F. & Younes, S., *op cit.*

[536] Many proponents against conventional insurance argue that such insurance be rejected as it is a form of gambling (*Maysir*). This is so as the payment of the sum insured depends on pure chance. *Maysir* literally means getting or profiting something too easily without having to work for it. Islam forbids all forms of gambling and this has been clearly stated in several verses of the Noble Qur'an, e.g. Surah Al-Maidah Chapter 5 verses 90-1. However, under *Takaful*, the concept of *Tabarru'* (donation) where the participants voluntarily contribute to the common pool in the form of donation with the condition of compensation eliminates the elements of *Maysir.* See Ismail, E., (2011), Basic *Takaful* Broking Handbook, IBFIM, Malaysia, p. 30.

[537] Mahmood, N.R., (1991), *Takaful: The Islamic System of Mutual Insurance-The Malaysian Experience,* Arab Law Quarterly, Vol. 6, No. 3, pp. 280-296.

or inflating the amount of claim, are examples in which insurance is used by the insured for gain purposes.[538]

In the case of life insurance, if an insured dies early in the insurance period, the amount of premium that would have been paid is not likely to be very large. The death benefits to be collected, however, can be much larger than the amount of premiums since sum assured of a policy is predetermined at the inception of the policy period. In this case of general insurance, the insured is required to pay premium in order to enforce the contract. If a loss occurs during the insurance period, the insured will be compensated for an amount not exceeding the loss, but usually larger than the premium that would have been paid. On the other hand, if no loss occurs, the insured would collect nothing, not even a refund of premium.[539]

Hence, there is always one party who is at the losing end at the conclusion of an insurance contract. Even though the requirement of insurable interest in insurance contracts seeks to eliminate the element of gambling and wagering, *Maysir* may still prevail in insurance contract. Unlike *Gharar* which is tolerated to a certain degree, *Maysir* is completely not permissible by *Shari'ah*. It is clearly stated in the Noble Qur'an that men must abstain from gambling:

> ''…They ask you concerning wine and gambling. In them is great sin and some profit for men, but the sin is greater than the profit.''[540]

Another Surah that advises against gambling says that:

> ''Intoxicant and gambling, stones and arrows, are an abomination.''[541]

[538] Zuriah, A. & Hendon, R., (2009), *Takaful: The 21st Century Insurance Innovation*, McGraw-Hill (Malaysia) Sdn Bhd, p.24.
[539] *Ibid*, p. 25.
[540] Noble Qur'an, Surah Al-Baqarah, Chapter 2 Verse 219.
[541] *Ibid*, Surah Al- Maidah, Chapter 5 Verse 90.

Some writers have argued that *Maysir* or gambling is a form of *Gharar* and a zero sum game where no additional value is created. Conventional insurance is regarded as a form of gambling as the insured makes a bet on the loss occurrence and the same applies in reverse for the insurer. It is also regarded as acquiring wealth through luck or by chance and at the cost of others.[542]

3.2.8.4 *Haram*

Conventional insurers often invest in assets that are strictly forbidden by *Shari'ah*, e.g. certain commodities or activities like conventional banking, alcohol, *Shari'ah* prohibited entertainment and gambling, or pork are forbidden. Conventional insurers also underwrite policies that might be problematic under *Shari'ah*, such as property insurance for a conventional bank or a pub.[543]

The discussions on whether or not conventional insurance is in line with the *Shari'ah* are manifold, but the widely accepted view is that conventional insurance is unlawful. This was stressed by the Islamic *Fiqh* Academy, which stated in the 'Resolution No. 9 concerning insurance and re-insurance' (Jeddah/KSA 1985):

> ''First: The commercial insurance contract, with a fixed periodical premium, which is commonly used by commercial insurance companies, is a contract, which contains major elements of risk which void the contract and, therefore, is prohibited (haram) according to the *Shari'ah*''.[544]

The Islamic *Fiqh* Academy is often regarded as the highest authority in Islamic jurisprudence matters, though its resolutions are not binding. However, as the Academy

[542] Tobias, F. & Younes, S., *op cit*, p. 122.
[543] *Ibid.* See also Section 25 of the Insurance Act, 2003, laws of the Federation Nigeria is instructive here because there is an apparent conflict with the *Takaful* Operational Guidelines, 2013 on the issue of investment portfolio. The Act requires all insurances to invest according to the regulations provided in that section. In the same vein, Section 24(13) of the Act states that interest is of essence to admissible assets under the provision. *Takaful* is quite different from conventional insurance because of the *Shari'ah* prohibitive features of conventional insurance practice that are central to its operations. The requirement for *Takaful* Operators to comply with Section 25 of the Insurance Act is untenable because of the above stated reasons. *Takaful* Operators cannot invest in Haram products or enterprises. The Insurance Regulator, NAICOM, has not made it very clear as to the exemption of *Takaful* operators from the requirements of Section 25 of the Act. The harmonization of these conflicting and ambiguous provisions in the Insurance Act, 2003 and *Takaful* Operational Guidelines, 2013, is the main thrust of this study.
[544] Fiqh Academy Report 1985.

is a subsidiary body of the Organisation of Islamic Conference (OIC), it becomes clear that its resolutions do have an impact on *Shari'ah* issues.[545] It needs to be pointed out here that other opinions exist on conventional insurance. Some scholars argue that conventional insurance is allowed as long as it does not involve *Riba*. Then there is another group condemning life insurance but accepting non-life insurance for the reasons stated above. Whatever it is, the bottom line is that conventional insurance cannot exist within the confines of *Shari'ah* if its very embodiment negates the prohibitive elements of *Takaful*.

3.2.9 The Essence of *Takaful*

Potential losses faced by humans arise from risks, which human life can never be free from. Risk can be defined as uncertainty concerning the occurrence of a loss. Although it is not possible to entirely eliminate risks, they can be managed and reduced. Insurance is one of the devices that is used to manage risks in order to minimize potential losses. The heart of insurance system is pooling resources from many to help the unfortunate few. Insurance is allowable in Islam as a risk-sharing mechanism, so long as any elements that contravene Islamic principles are avoided, and all requisites of an Islamic insurance system are met.[546] Sharing the risk with the purpose of helping each other is commendable as Allaah mentioned in the Noble Qur'an:

> ''….Help you one another in virtue, righteousness and piety, but do not help one another in sin and transgression.''[547]

Drawing from the Malaysian experience which is bound to impact heavily on Nigeria as it seeks to kick-start its *Takaful* sojourn, the development of *Takaful* industry was largely triggered by the decree issued by the National Fatwa Committee which ruled that life insurance in its present form is a void contract due to the presence of *Gharar*,

[545] Tobias, F. & Younes, S., (2010), *op it*, p. 123.
[546] Zuriah, A. & Hendon, R., (2009), *op cit*, p. 26.
[547] Noble Qur'an, Surah al- Maidah, Chapter 5 Verse 2.

Maysir and *Riba.* Subsequently, a Special Task Force was set up by the government in 1982 to study the viability of establishing an Islamic insurance company. In its report, the Special Task Force concluded that:

> ''under the Islamic insurance system, a portion of the contribution from every participant must be made with the intention of *Tabarru',* and not for buying and selling, the existence of *Tabarru'* makes the transaction permissible and valid according to *Shari'ah.*''[548]

The Islamic *Fiqh* Academy, emanating from the Organisation of Islamic Conference (OIC), made a resolution in 1985 that the commercial insurance contract is prohibited according to *Shari'ah.*[549] It subsequently issued a decree that states:

> ''the alternative contract, which conforms to the principles of Islamic dealings is a contract of a co-operative dealings, which is founded on the basis of charity and cooperation.''[550]

A prominent scholar, Sheikh Dr. Yusuf al-Qardawi, suggested a modification to the insurance against hazards, to bring closer to the Islamic principle by means of contract a of 'donation with a condition of compensation.'[551] He suggested that an insurance buyer would donate his payments to the company with the stipulation that the company would compensate him should he suffer from a loss to reduce his financial burden.

The majority view point by many contemporary Islamic jurists and scholars is that, for an insurance system to be acceptable by Islamic tenets, it must be founded on the principles of:

1) Donation (*Tabarru'*)

[548] Special Task Force Report on the Viability of Setting up an Islamic Insurance Company, 1982.
[549] Resolution No. 9 Concerning Insurance and Reinsurance (The 1985 Islamic *Fiqh* Academy Ruling, Emanating from the Organization of Islamic Conference, meeting in its Second Session in Jeddah, Saudi Arabia, 22-28 December, 1985).
[550] Resolution No. 9 Concerning Insurance and Reinsurance (The 1985 Islamic *Fiqh* Academy Ruling, Emanating from the Organization of Islamic Conference, meeting in its Second Session in Jeddah, Saudi Arabia, 22-28 December, 1985)..
[551] Al-Qardawi, Y., (2001), The Lawful and the Prohibited in Islam, Islamic Book Trust.

2) Mutual cooperation (*Ta'awun*)

These are the essence of an Islamic insurance which embraces the elements of mutual guarantee, mutual protection and shared responsibility.[552] Since these elements constitute the pillars of *Takaful*, it is pertinent to have a closer look at their composition in order to fully comprehend aims and objectives of *Takaful*.

3.2.9.1 *Tabarru'*[553]

As stated earlier in this study, *Tabarru'* means donation, gifts or contribution. The participants in a *Takaful* scheme mutually agree to relinquish as donation, a certain portion of their contributions, into a *Takaful* fund, to provide financial assistance to any members of the group suffering from a loss. Under *Takaful* contracts, each participant contributes a certain portion of the full amount of his contribution as *Tabarru'*. The donations from all participants are accumulated into a common fund called *Tabarru'* fund or risk fund, from which compensation is paid to participants suffering a defined loss.[554]

Tabarru' is the essence of an insurance system acceptable to the Islamic faith. It is the mechanism to uphold the concept of joint guarantee among participants by allowing them to share their contributions to help and assist each other in the event of a defined loss occurring. Participants contribute to a pool of funds to mutually protect and indemnify each other from a defined risk.[555] Losses arising from these risks are paid out from the common fund sourced from donations of the participants. The remaining of the fund after *Takaful* benefits are paid is the surplus, and it will be shared among the

[552] Zuriah, A. & Hendon, R., *op cit*, p. 27.

[553] In any insurance transaction, be it Islamic or conventional, the premium mobilization forms an integral part of the operations. This is because the premiums are core of the business of insurance and *Takaful.* In conventional insurance, the contract is based on the principles of exchange of mutual interest. The relationship is designed in such a way that the insured buys protection by payment of premiums and the insurer provides protection against the insured risk. In this way, the contract becomes a form of sale contract on uncertain event for which is not compatible with Islamic principles of exchange contracts. The concept of *Tabarru'* which is based on donation tolerates elements of *Gharar* (uncertainty) and ambiguity, because these invalidating elements do not affect contracts of charity. See Arbouna, M.B., (2008) *Regulation of Takaful Models: A Shari'ah Overview of Contractual Aspects of Takaful Models*, in Bakar, M.D. & Ali, E.R.A.E (eds)., *Essential Readings in Islamic Finance*, *op cit*, p. 222. See al-Darir, Muhammad al-Ameen, *al- Gharar wa Atharuhu fi al-Uqud fi al-Fiqh al-Islami* (1995), Jeddah: Dalalah al-Barakah, p. 643. For more on qualified charity-based contracts, see Qahf, Munzir, *al-Waqf al-Islami*, (2000), Beirut: Dar al-Fikr, pp. 137-142.

[554] Obaidullah, M., (2005), *Islamic Financial Services* [http://www.islamic-finance.net]

[555] Shankar, S., (2008), *Conventional Insurers Slow to Capitalize on Takaful Potentials*, MIF Monthly, *Takaful* Supplement.

participants. The profit or surplus is only rewarded after the obligation to share losses among participants has been fulfilled.[556]

The concept of *Tabarru'* permits the avoidance of many sources of *Gharar* (uncertainty) prevalent in a conventional insurance contract, particularly with regard to the sources of insurance benefits payable to the insured or his beneficiary. Even if the element of *Gharar* may not be completely avoided, *Tabarru'* permits a *Takaful* contract to be allowable under the *Shari'ah*. The *Ulama'* (Islamic scholars) rule that if the risk premium (portion of contribution that is donated to *Tabarru'*) is donated to the participants' risk pool (*Tabarru'* fund), then this is a gratuitous contract in which *Gharar* does not apply.[557]

3.2.9.2 *Ta'awun*[558] (Mutual Cooperation)

Insurance is permissible in *Shariah* when operated within the framework of *Takaful* (mutual guarantee), *Ta'awun* (mutual cooperation) and *Tabarru'* (donation). Besides *Tabarru'*, the core of *Takaful* is the principle of mutual cooperation and risk-sharing. Mutual cooperation (*Ta'awun*) is achieved through contributions from *Takaful* participants to the *Tabarru'* fund which allows participants to provide financial assistance to fellow participants suffering a loss. A *Takaful* system can be described as a co-operation among participants who mutually protect and guarantee the interest of one another, by jointly sharing responsibility to pay for potential losses that may occur, through donations into a common fund.[559]

Takaful is built on the principle of mutual cooperation where each participant participates in each other's loss, while *Takaful* operator facilitates this cooperation using

[556] *Ibid.*
[557] Zuriah, A. & Hendon, R., *op cit*, p. 28.
[558] The word '*Takaful*' does not appear in the Noble Qur'an but conceptually has its origins from the word ''*Ta'awun*'', which means mutual assistance. The prophet pbuh also clarified that some of the virtuous pre-Islamic practices are Islamic and can be adopted on the basis of ''assisting one another''. The concept of *Ta'awun* predates the Islamic era when the rough model for *Takaful* was practiced by Arab tribes, holding to the principle of pooled resources to help the needy on a voluntary and gratuitous basis. Among the examples of early *Takaful* were the merchants of Makkah who pooled funds to assist victims of natural disasters, misfortunes or piracy. See Yassin, N. & Ramly, J., (2011), *Takaful: A Study Guide*, IBFIM, Malaysia, p. 86.
[559] Zuriah, A. & Hendon, R., *op cit*, p. 28.

its expertise.[560] The participants assume all the risk involved in the operation of the *Takaful* business. If the operation results in surplus, they would be entitled to the whole sum, or to a certain pre-agreed percentage (depending on the *Takaful* model adopted). If the fund is insufficient, participants would not be asked to pay additional premium.[561] Instead, the *Takaful* operator will provide interest-free loan (*Qard Hasan*), from the shareholders' fund to meet the deficit.

Essentially a cooperative risk-sharing plan, *Takaful* system aims to provide insurance protection against risks such as premature death, illness, disability and property damages. It embraces the elements of mutual help, mutual protection and shared responsibility among participants, supported by the principle of *Tabarru'*. *Takaful* is a type of joint-guaranteed insurance mechanism, based on the law of large numbers, in which members pool their financial resources together against certain loss exposures[562]. In conventional insurance, the risk of potential loss is assumed by the insurer, while in *Takaful*, the risk of loss is shared is shared by the participants, in a cooperative arrangement. *Takaful* is similar to mutual insurance in that members are the insurers as well as the insured.[563] Participants in *Takaful* schemes are not involved in the fund management as well as in the day-to-day operation of the business. A *Takaful* operator is delegated to manage the fund and to run the operation commercially as a business venture for profit.[564]

Dr. Yusuf Qardawi[565], asserts that a cooperative system established to assist its members who suffer from misfortune must meet the following conditions in regard to the money collected from the members:

[560] Jching, Y.B., (2008), *MARC's Approach to Rating Institutions Offering Takaful*, MIF Monthly, *Takaful* Supplement.
[561] Ahmad Nordin, M.T., (2007), *Understanding Takaful and the Challenges Ahead*, General and *Takaful* Agents Convention.
[562] Maysami & Kwon, (1999), *An Analysis of Islamic Takaful Insurance*, Journal of Insurance Regulation, p. 12.
[563] Mohd Kassim, Z.A., (2005), *The Islamic Way of Insurance Contingencies*, p. 18.
[564] Zuriah, A. & Hendon, R., *op cit*, p. 29,
[565] A renowned Islamic scholar of the 21st century.

1) Every member makes his share of payments into a common fund as a donation, in the spirit of brotherhood. Financial assistance is provided to members who suffer a loss from this common fund.

2) Any investment of the money from the common fund must be done in *halal* (permissible by *Shari'ah*) business activity which is free from usury or interest.

3) A member shall not seek a pre-determined amount of compensation in the event of a loss. Rather, he will be indemnified for his loss either totally or partially, depending on the available resources in the common fund.

4) Being donation, the money that has been paid into the common pool becomes a gift, and withdrawing it would be *haram*[566] (unlawful)

3.2.10 Basic Features of *Takaful* Model

The basic features of a *Takaful* model highlight the subject of *Takaful* concept and its operations. Understanding these basic features makes explicit the operational models being practiced by the *Takaful* operators.

It must be noted that *Takaful* concept aims at providing the same services that are offered by conventional commercial companies to policyholders. The theme of *Takaful* is to protect the participant against inability to overcome future unwanted events and difficult times. This objective is achieved on the basis of different features altogether. The most important features of *Takaful* model can be summarized as follows:

a) The Islamic insurance companies strictly observe *Shari'ah* rules and principles. This relationship is built on avoidance of *Riba*-based transactions, especially when investing the collected contributions. Again, the contracts and policy certificates must comply with the requirement of *Shari'ah* in respect to agreement. In other words, it is not a

[566] Zuriah, A. & Hendon, R., *op cit*, p. 29.

requirement that a particular *Takaful* contract, activity or relationship should comply with a *Shari'ah*-nominated contract or that such a *Takaful* contract must exist in the *Qur'an* and *Sunnah*. All what is required is that the contract must not violate *Shari'ah* principles. This is because, as a general principle, all contracts concluded by men are considered valid unless otherwise explicitly prohibited *Shari'ah.* This feature of *Takaful* necessitates appointment of *Shari'ah* Boards and internal *Shari'ah* Advisors in order to advise on how insurance operations should be carried out according to the *Shari'ah* requirements.[567]

b) Formation of two separate accounts at the beginning of insurance policy. One account manages the movement of funds of the shareholders. The other account manages the movement of funds belonging to the participants alone. It must be noted here that this segregation will also create a partnership relationship between the participants and the operator.[568]

c) In principle, the relationship between the operator and the participants is either ''agency-agency'' relationship or ''agency cum *Mudharabah*'' relationship. In other words, the insurance company is authorized by the participants to manage the operations and insurance services including, among others, preparation of documents, collection of contributions and payment of indemnities. The participants also authorize the company to invest the mobilized contributions, either on the basis of investment agency and/or *Mudharabah*, in accordance with terms and conditions agreed upon by the parties.[569]

[567] Arbouna, M.B., (2008), *Regulation of Takaful Business: A Shari'ah Overview of Contractual Aspects of Takaful Models, in Essential Readings in Islamic Finance*, *op cit*, CERT Sdn Bhd, p. 213.
[568] Arbouna, M.B., *op cit*, See also Hassan, H.H., (2000), *''al-Ta'min Ala al-Hayat''*, Hawliah Albarakah, December, pp. 38-69.
See also al-Qarafi, al-Furuq, vol 3, pp. 150-1; al-Darir, Muhammad al-Ameen, (1995), *al-Gharar wa Athruhu fi al-Uqud fi al-Fiqh al-Islami*, Jeddah: Dallah al-Barakah, pp. 525-544.
See also Ibn Hajar, *Fath al-Baari*, vol. 5, p. 222; al-Shawkani, *Nayl al-Awtar*, vol. 6, p. 100.
[569] Arbouna, M.B., *op cit*, p. 220.

d) Islamic insurance companies endeavour to meet the objective of cooperation and solidarity among the participants or policyholders. This is achieved through payment by the participant of premium or contribution amount with the view that this amount is donated in whole or in part to remedy damage or catastrophe that befalls any registered participants in the insurance portfolio. Therefore, the donated sum belongs to all participants and does not belong to the shareholders as practiced by conventional insurance companies.[570]

e) Islamic insurance involves uncertainty as to compensation and its value. This affects exchange contract and not donation-based contract which is the basic philosophy of *Takaful*. This is because the uncertainty or *Gharar* in Islamic insurance occurs between the participants who constitute one entity to meet mutual benefit. In conventional insurance, the uncertainty or *Gharar* is between the insured persons and the insurance company. These are two separate parties whose interests conflict. The *Gharar* in conventional insurance is that a person is paying a premium and waits for indemnity when the risk insured occurs, which may or may not occur.[571]

f) Islamic insurance companies distribute the surplus to the participants according to their contributions. The surplus accumulates through contributions minus compensation, expenses and reserves.[572]

g) In the ideal situation, the *Takaful* participants must contribute additional money in the case of deficit to meet the insured risk.[573]

[570] *Ibid.*
[571] Arbouna, M.B., *op cit*, p. 220.
[572] *Ibid.* p. 222.
[573] *Ibid.* However, with due respect to the learned author, this researcher is of the opinion that this assertion is not correct because there are several rulings which state that the participants are not required to contribute any further money to shore up deficits because it is incumbent on the *Takaful* operator to provide interest-free loan (*Qard Hasan*), from the shareholders fund to meet the deficit. If not carefully handled, the issue of *Qard Hasan* could be detrimental to the *Takaful* enterprise where the operator elects to abuse this facility. Insurance contracts are contracts *uberrimae fidei* (utmost good faith) and as such any abuse of trust by the operator will lead to dire consequences. In the case of the Nigerian insurance industry, one of the factors responsible for its stunted growth is the pervading apathy by Nigerians about anything insurance due to the mistrust of the industry by Nigerians. Claims are never settled even if proven to be genuine and sharp practices abound which have completely eroded the trust of the populace. The Nigerian *Takaful* industry must not fall into this error.

h) The participants are entitled to participate in the administration and supervision of the activities of the *Takaful* operator. This participation could be achieved by the creation of Association of Participants which shall appoint a representative to attend management meetings or Board meetings on behalf of the participants. This participation will help to overcome the problem associated with the mutual exchange of loan between the *Takaful* operator and the participants should the operator choose to operate on this basis.[574]

3.3 *TAKAFUL* OPERATIONAL MODELS

The conceptual frameworks of the underlying Islamic insurance concept are realized through the *Takaful* operating models employed by the operators. *Takaful* operators are afforded flexibility in operating their *Takaful* business under different models. Although the operators are generally required to fulfil certain fundamental components that characterize their operations, some operational differences that do not contradict essential religious tenets are tolerated. As such several *Takaful* models have been introduced to suit the business objectives of the operators.[575]

The overall structure of a *Takaful* set up comprises three parties namely the participants (policyholders), operator and *Shari'ah* Board. It should be emphasized that neither the participants (i.e. the buyer of *Takaful* contracts) nor the staff and management of the *Takaful* operator need to be Muslim.[576]

Several forms of contract or model govern the relationship between the participants and the *Takaful* operator in its core functions as investment and risk manager. The main issues are basically:

(a) Who pays for the expenses incurred in the business venture?

(b) Who is liable for any losses arising from the venture?

[574] For the acceptance of exchange loans, see *Qararat wa Tawsiyat Nadwat al-Baraka li al-Iqtisad al-Islami*, (2001), p. 156.
[575] Mahmoud, H., (2008), *Insurance; Takaful Gaining Ground*, The Actuary. See also Rahman, Z.A., *op cit*, p. 30.
[576] See Rosly, S.A., (2010), *Critical Issues on Islamic Banking and Financial Markets: Islamic Economics, Banking & Finance, Investments, Takaful and Financial Planning*, Dinamas Publishing, Kuala Lumpur, Malaysia, p. 487.

(c) Who provides the start-up capital for the operation?

(d) How are profits from underwriting and investments shared between the parties?[577]

Islamic contracts that have been considered are the following:

(i) Agency contract – *Wakalah*

(ii) Joint venture contract – *Mudharabah*

(iii) Joint ownership contract – *Musharakah*

(iv) Performance based contract – *Ju'alah*

(v) Guaranteed trust or safekeeping – *Wadi'ah Yad Damanah*

(vi) Pious endowment/trust – *Waqf*[578]

In practice, almost all companies use *Wakalah* or *Mudharabah* contract but the discussion on which is the most appropriate contract for a *Takaful* operation is still on-going.[579]

3.3.1 The *Ta'awuni* Model

The *Ta'awuni* model establishes cooperative insurance, and practices the concept of pure *Mudharabah* in its transactions.[580] This is essentially a profit-sharing model. Under this model, the *Takaful* operator and participant share the direct investment income. In addition, the participant is entitled to 100 per cent of surplus, with no deduction made

[577] Rosly, S.A., *op cit.*
[578] Rosly, S.A., *op cit.,* p. 488.
[579] Tobias, F. & Younes, S., *op cit,* p. 133.
[580] *Takaful* Insurance Companies, (2008), Best's Rating Methodology.

prior to distribution. Pure *Mudharabah* model encourages solidarity, unity, brotherhood and mutual cooperation between the contracting parties.[581]

Flowing from the *Ta'awuni* concept, there are two basic models that are critical to the operations of *Takaful*. These are the *al-Wakalah*[582] and the *al-Mudharabah*[583] models.

3.3.2 Basic Concept of *Wakalah*

Wakalah is an Islamic form of contract, in which an agent (*Wakil*) is authorized to act on behalf of a principal to carry out a predefined task, usually in return for a fixed compensation, very much like a third party administrator (TPA). This service fee (*Ujrah*) may be pre-agreed as an absolute figure or as a percentage of the turnover, but not as a share of the profits of the venture. The fee is called *Wakalah* fee.[584]

Wakalah is an Islamic agency contract. In such a contract, all rights and liabilities remain with the principal i.e. any capital losses are to borne by solely by the principal or capital provider. However, the agent is required to act with prudence and in good faith and is responsible for losses incurred due to his wilful negligence. He is expected to employ and manage the capital in a manner that does not violate the values of Islam[585].

Wakalah is independent of the actual performance of the assigned task, which can create some principal-agent issues altogether. An alternative would be to incorporate a performance based element such as *Ju'alah* in which the agent (*Takaful* operator) will charge commissions for the services rendered. However, the payment to the agent is not fixed, but is measured based on the agent's output and performance or the parties could apply one of the profit and loss sharing contracts such as *Mudharabah* or *Musharakah*. Al-*Musharakah* model works in such a way that both participants and *Takaful* operator

[581] Zuriah, A. & Hendon, R., *op cit*, p. 34.
[582] In Islamic Finance, *Wakalah*, literally means a contract in which one person appoints another as an agent on his or her behalf in a transaction.
[583] The *Mudharabah* contract is essentially a basis for sharing profit and loss between the *Takaful* operator and the participants. The *Takaful* operator manages the operation in return for a share of the underwriting surplus and a share of profit from the investments.
[584] Tobias, F. & Younes, S., *op cit*, p. 133.
[585] Tobias, F. & Younes, S., *op cit*, p. 133.

provide capital and contribution to the *Takaful* fund. This model is similar to a joint venture. Profit is split according to a mutually agreed ratio, or distributed in proportion to capital contribution. Al-*Mudharabah* model, basically, is a profit-and-loss sharing model in which the participant and the *Takaful* operator share the surplus.[586]

3.3.3 Basic Concept of *Mudharabah*

Mudharabah[587] is a form of partnership contract, in which one partner provides his skills and work (*Mudharib*) and the other partner (*Rabb al-Mal*) provides capital. Both share the profits of the joint venture in accordance with pre-agreed ratio. This is very different to the *Wakalah* model where the compensation cannot be related to the actual performance of the joint venture.[588]

Mudharabah is defined as a profit-sharing Islamic contract. Any losses are to be fully borne by the capital provider with the exception of cases of wilful negligence or misconduct by the *Mudharib*. The capital provider does not have any executive functions in this undertaking.[589]

3.3.4 Segregated Funds

As stated earlier in the discourse, the split of the insurance business into administration/asset-management and risk-carrying functions obliges the *Takaful* operator to maintain strictly segregated funds. One fund is for the equity of the shareholders' of the *Takaful* operator, i.e. the shareholders' fund and the other for the contributions of the participants (policyholders):

[586] Billah, M.M., *op cit*, p. 82. See also Ahmad, S. *op cit*, pp. 512-3.
[587] The *Mudharabah* business model was the most popular model in Malaysia during the early stages of Takaful set up in the country, whereas the *Wakalah* business model was made popular later. In a recent development, *Takaful* operators have a new business model comprising a combination of *Wakalah* and *Mudharabah* models, which allows less *Wakalah* fee charges and attractive *Mudharabah* package for the participants. The *Wakalah* fees are deducted from the PSA while the *Mudharabah* profit sharing between the *Takaful* operator and participants are applied on the net profit from investment. See Ahmad, R. & Auzzir, Z.A., *op cit*, p. 31.
[588] Tobias, F. & Younes S., *op cit*, p. 133. See also Bambale, Y.Y., (2007) Islamic Law of Commercial and Industrial Transactions, Malthouse Press Ltd, Nigeria, p. 195.
[589] Bambale, Y.Y., (2007) Islamic Law of Commercial and Industrial Transactions, Malthouse Press Ltd, Nigeria, p. 195.

(i) **Shareholders' Fund (SHF):** This is funded by initial seed capital (paid-up capital or working capital) and subsequent management fees and by any additional capital injunctions. Surplus distribution in the form of commission fee (*Ju'alah*) could constitute part of the SHF fund if approved by the *Shari'ah* Board. All management expenses and shareholders' dividends would normally have to be borne by this fund[590].

(ii) **Participants' Risk Fund (PRF):** It works on the basis of mutual assistance, where all participants sign a contract (*'Aqad*) to participate and to fulfil their obligation, which is to make a contribution (*Tabarru'*) to mutually assist other participants who suffer a misfortune. There is usually a separate risk fund for each line of business (individual family, group family, investment linked, fire, motor, treaty, facultative, etc). The PRF is sometimes also referred to as Participants' Special Account or Participants' *Takaful* Fund.[591]

Another fund is needed for savings or investment-linked family (life) *Takaful* products:

(iii) **Participant's Investment Fund (PIF):** The part of the contribution not needed to cover the risk is placed in a separate fund for investment and invested by the *Takaful* operator. This fund is not mutual in nature but is the sole and exclusive property of the individual who participates in a family *Takaful* contract. This fund is also used for regular or single-premium contracts where the *Tabarru'* charges are ''dripped'' on a regular basis (e.g. monthly or yearly) from the PIF to the PRF.[592]

Thus, a family (life) *Takaful* operator manages three main funds, while a general (non-life) *Takaful* operator only two. The *Takaful* fund will normally be split into several sub-funds to account for the various lines of business. This segmentation is often prescribed by the regulator and mirrors statutory accounts.[593]

[590] *Ibid.*
[591] Tobias, F. & Younes, S., *op cit*, p. 134.
[592] Tobias, F. & Younes, S., *op cit.*
[593] *Ibid*, p. 135.

3.3.5 *Tabarru'*

Under the current practice, the *Tabarru'* is in fact not an actual donation but a commitment to donate. This allows the *Takaful* operator to claim the contribution payments from the participants on behalf of the fund in accordance with the *Takaful* contract signed. Under a pure *Tabarru'* arrangement, the transfer of ownership to the fund takes place on actual payment and there is no obligation at all to pay. Thus, the *Takaful* contract establishes an obligation to make future contribution payments.[594]

3.3.6 *Takaful* Benefits

For general *Takaful*, the *Takaful* benefit is the indemnification (sum covered) as per the contract terms, paid out of the PRF. Under family *Takaful*, the investment account PIF has to be considered as well. The benefit when a claim is made is thus the sum covered plus the amount accumulated in the PIF and if applicable a proportional share of the surplus in the *Takaful* fund on termination of the contract. On surrender, usually the amount in the PIF is paid out (sometimes less a surrender charge). On maturity, the PIF amount plus an additional share of the surplus in the *Takaful* fund on termination of the contract (akin to a terminal bonus under conventional with-profit life insurance) is paid out.[595]

3.3.7 Surplus Sharing

The surplus arising from the participants' funds will usually be distributed to participants (generally to the PIF under family *Takaful* where it accumulates, otherwise as a cash dividend, a reduction in future contributions or an additional *Takaful* benefit) and, depending on the *Takaful* model, also shared with the *Takaful* operator. The surplus from the risk fund may also be donated to charities selected by the operator's *Shariah* Advisory Board. It is common to build up a claims contingency reserve within

[594] *Ibid.*
[595] Tobias, F. & Younes, S., *op cit.*

the risk fund from past underwriting surpluses to smooth claims experience over time. The surplus distributed to participants is usually proportional to their contributions to the PRF net of any claims that have been paid during the valuation period.[596]

3.4 PURE *WAKALAH* MODEL

Under the pure *Wakalah* model, the *Takaful* operator (TO) acts as the agent and invests and administers the fund(s) on behalf of the participants, thereby ensuring appropriate treatment, equity and fairness among all participants. In return, the TO receives a pre-agreed up-front *Wakalah* fee comprising both administrative and investment fees to cover the operational expenses. It is inclusive of distributors' commission, but does not share in the underwriting or investment profits. The *Takaful* operator can be thought of as being a third party administrator.[597] The overall workflow is summed up below:

(a) The net contribution after deduction of the up-front *Wakalah* fee is split into the *Tabarru'* for the risk fund and the investment contribution:

(b) The Participants' Risk Fund (PRF) is a mutual pool out of which insured claims, re*Takaful* contributions and reserve adjustments are funded.

(c) The other part of the *Takaful* contribution is placed in the Participant's Investment Fund (PIF) for savings and investment under family *Takaful*. For general *Takaful* business, there is no PIF, only the PRF.

(d) The assets in the PIF and PRF are invested in *Shariah* compliant assets. The investment profits from the PIF and PRF are either retained within their respective fund or allocated to the PIF. The PIF balance is then released to the participant upon claim, surrender or expiry.

[596] *Ibid.*
[597] *Ibid*, p. 135.

(e) Any underwriting surplus arising in the PRF goes to the participants by allocating it to the PIF for family *Takaful* products or directly to the participant.

(f) In the event of an underwriting deficit in the PRF, e.g. due to the adverse claims experience, the operator is obliged to make up for the deficit and provide a *Qard Hasan* or interest-free loan. This benevolent loan will be repaid out of future surplus arising, though both timing and repayment amount are uncertain.[598]

The *Wakalah* fee is typically a fixed percentage (e.g. 10% to 30%) of the *Takaful* contribution plus an additional fee for the fund investment. This could be a flat fee, or variable as a percentage of the fund value. This guarantees the operator a steady fee-based income, but there is no upside potential, as the TO does not share in any profits. This is a crucial difference from conventional insurance, where underwriting profit is a major source of income for the insurer.[599]

3.4.1 *Wakalah* Model with Performance Incentive

Critics of the pure *Wakalah* model cite the lack of incentives for the operator to properly run the *Takaful* fund as it does not share in any surplus or profits. As income is a fee based on turnover (i.e. *Takaful* contributions), it might be tempted to write as much business as possible without proper underwriting or claims handling. This is a typical principal-agent problem.[600]

Therefore, some operators apply a *Wakalah* model with incentive compensation (also sometimes referred to as ''modified *Wakalah*'') where the *Wakalah* fee comprises an up-front fee (e.g. 20%) as well as a proportional share in the underwriting surplus (e.g.

[598] Tobias, F. & Younes, S., *op cit*, p. 135.
[599] Theoretically, the *Takaful* operator bears no insurance risk himself. The risk is seen as a process of solidarity between participants and takes place solely among the collective of the insured persons (hence the name ''joint guarantee''). However, due to his obligation to make up for any underwriting losses in the Takaful fund, the operator is in fact exposed to considerable insurance risk. He may not be able to cover a *Qard Hasan* if insufficient surplus is generated over time. Furthermore, no interest can be charged on the outstanding loan as that would be in breach of an intrinsic principle of Islamic finance that has to be strictly followed. This study submits that this is an interesting area for further research. See Tobias, F. & Younes, S., *op cit*, p. 135.
[600] Tobias, F. & Younes, S., *op cit*, p. 139.

25%). A concern with this model is that it blurs the clear distinction between *Wakalah* and *Mudharabah.*[601]

Many *Takaful* operators would consider it reasonable to reward an operator retrospectively with a share in the surplus generated as an incentive for good performance. It is evident that the policy wordings must clearly state this practice to avoid *Gharar* (uncertainty). The incentive can be in the form of a gift (*Hibah*), performance fee (using the contract of *Ju'alah*) or waiver (*Tanazul*), where the participants waive parts of their surplus share. An issue arises here though as two Islamic contracts relating to the same thing are merged and this is not accepted by all scholars if it violates substance over form principles, i.e. used to circumvent *Shariah* principles. This practice is widespread, e.g. approved by National *Shariah* Council of Malaysia and applied in Indonesia (*Wakalah bi'l-Ujrah*, i.e. *Wakalah* with service fee), but it is not acceptable to all scholars and practitioners for two reasons:

(1) One side argues that the operator makes a profit from the underwriting surplus but it is not responsible for losses – unlike the participants. This would indicate a distorted and inequitable system.

(2) Of greater importance is the general reservation of many *Shariah* scholars towards a sharing of underwriting surplus originating from the pool of donations.

(3) Because the issue of incentive fee is debatable among Muslim jurists, *Takaful* operators are invited to resolve the conflict and propose a model that by-passes the polemics over the issue. Meanwhile, other means can be implemented to compensate through portfolio diversification and investment, effectively applying economics of scale, raising *Wakalah* fee, or adopting more cost effective practices.[602]

[601] *Ibid.*
[602] Tobias, F. & Younes, S., *op cit*, p. 139..

3.4.2 Risk Management Charge

Some *Takaful* operators applying the dripping method in Malaysia also levy a so-called risk management charge (RMC) on the *Tabarru'* fund, i.e. a percentage of the yearly risk rate is deducted as the risk administration charge. It is charged prospectively but not paid before the end of the accounting/valuation period, i.e. it is provisioned. Only if claims experience has proved to be positive will the amount be paid, i.e. transferred to the shareholders' fund. In the event of a deficit, the provision can be used to offset parts of the deficit.[603]

3.5 *MUDHARABAH* MODEL[604]

The *Mudharabah* model is based on classic profit sharing principle, i.e. a partnership model where the participants provide the capital (contributions), while the *Takaful* operator provides expertise and management for the *Takaful* fund. An essential feature of *Mudharabah* is that a contract has to detail how underwriting and investment profits are to be shared between operator and participants, very much as in conventional insurance. The key difference from the *Wakalah* model is that no up-front *Wakalah* fee is deducted, as the only source of income is the ex-post profit on the risk and/or investment fund.[605]

A number of technical issues arise when implementing this model:[606]

(a) Whilst investment profits are clearly defined as excess return over invested capital, the same does not hold true for the ''underwriting profit''. If that definition were applied, there would never be any underwriting profit, even if there were no claims (the return would then be zero, as it would equal the invested capital or contributions).

[603] *Ibid.* p. 141.
[604] This has been introduced in several sections of this chapter but the discussion here is more detailed in conceptual analysis, thus underscoring its importance.
[605] Tobias, F. & Younes, S., *op cit.*
[606] *Ibid.*

Hence it is technically correct to refer to underwriting surplus instead, i.e. the excess of contributions over claims and reserves.

(b) Under a *Mudharabah* model, the participants as capital providers would have to bear the capital losses i.e. through their contributions. The requirement for a *Takaful* operator to provide *Qard Hasan* in the event of an underwriting deficit (which is essentially a capital loss) is thus not a *Shari'ah* requirement. It was introduced for practical purposes and only to deal with temporary deficits that can be covered out of future surplus.

(c) A capital loss under *Takaful* can far exceed the aggregate contributions of all the participants. However, even as *Rabb al-Mal* (capital provider), their liability is limited to the capital outlay. The question then is who guarantees the claims payments under this model? If the *Takaful* operator as *Mudharib* would provide an indemnification commitment, it would contravene the essential principles of *Mudharabah* and would not be allowed under *Shari'ah.* In practice though, there is a clear expectation by the participants that their claims will be paid in full, as is the case under conventional insurance. Hence *Takaful* operators provide an implicit guarantee through the *Qard Hasan* promise. If the loan cannot be recovered, it will have to be written off partly or in full. This translates more or less to a guarantee by the operator.

A variation of this model is that the profit-sharing for the *Takaful* operator is only applied to the investment portion, while all underwriting surplus is returned to the participants (pure *Mudharabah*). However, that model may not be commercially viable in the end as insufficient investment income might be generated for the *Takaful* operator.[607]

[607] Tobias, F. & Younes, S., (2010), *op cit*. Another variation of this model covers operating expenses directly from the *Takaful* fund instead of funding them from the shareholders' fund, i.e. the underwriting result is the net of *Tabarru*', claims, re*Takaful* , reserve adjustments and operating expenses. An area of concern is the type and amount of expenses charged to the fund and it follows that it should be set out for the participants in a transparent manner.

3.6 HYBRID *WAKALAH/MUDARABAH* MODEL[608]

A combination of both models is the common used by new *Takaful* set-ups. Here a *Wakalah* is used for the underwriting function and a *Mudharabah* on the investments. Thus, the operator charges a *Wakalah* fee from the *Takaful* contribution and underwriting profits are distributed to the participants. However, investment profit is shared between participants and operator on the basis of a pre-agreed ratio. This model has its appeal as investment profits can be a source of income and a *Wakalah* fee earned on the underwriting activities creates a stable and predictable source of up-front income, which can be used to fund the initial acquisition. Although the operator is exposed to the risk of adverse claims experience, this can be easily minimized by using quota share re*Takaful* arrangements.[609] A variation of this model combines the *Wakalah* with performance incentive (a.k.a. modified *Wakalah*) with a *Mudharabah* on the investments.

3.7 *WAQF* MODEL[610]

This model works on a non-profit concept, emphasizing the idea of donation among the participants. The *Takaful* operator initiates the *Waqf* fund by contributing the initial sum into the fund, and the participants make donations to help the less fortunate members of the community. This model is general undertaken by a social or governmental enterprise operating on a non-profit basis. A *Waqf* deed is drawn to assist in the distribution of funds should a loss occur to any participants. Surplus and profits resulting from

[608] This is a new model that is making waves in the *Takaful* industry because of its presumed guarantee of high yielding returns. What remains imperative or critical is its complete compliance with the intrinsic principles of *Shari'ah.* The model looks attractive but is enmeshed in controversy as to its legitimacy. Innovations are critical to the continued survival of *Takaful* but it remains to be seen how far the *Ulamas* can go in accommodating some ambitious trends.

[609] Tobias, F. & Younes, S., *op cit,* p. 140.

[610] In order to eliminate the element of *Maysir* , the concept of *Waqf* and *Tabarru'* is introduced into this model. In relation to this, participants agree to relinquish as ''donation'' certain amount of money. A *Waqf* fund is established by the shareholders of the Takaful company through the contribution of 'ceding amount' (part of the capital) to compensate the beneficiaries or participants of Takaful scheme. See Ismail, E., *op cit,* p. 49.

investment activities are not distributed to the participants. The operator retains the surplus fund to support the community.[611]

The relationship of the *Takaful* operator with the participants is rather loose and indirect as the collective of participants is not a clearly defined entity. This has a couple of effects on the *Takaful* operation.

(i) ***Shari'ah*-related/legal:** It is difficult to formally define the rights and obligations of the participants in *Shari'ah* terms under the pretext of the contribution being a contingent gift and the fact that the *Takaful* fund is ''owned'' by the participants, which are not a separate legal entity as such.

(ii) **Technical:** the possibility of insufficient contingency reserves in the *Takaful* fund, which increases the probability of interest-free loans for the shareholders, with all the problems involved in their recovery (e.g. inter-generational unfairness).[612]

The concept is to set up the *Tabarru'* fund as a *Waqf* to remedy some of the inherent disadvantages of the above mentioned operational models. The management contract between the *Waqf* and the operator is then based on other contracts, with *Wakalah* being the more viable. The same applies to the investments, i.e. they can be managed on the basis of *Wakalah* or *Mudharabah*. In practice, the *Waqf* is usually operated using a hybrid *Wakalah Mudharabah* model for the risk and investment portion.[613]

The shareholders of the *Takaful* operator have to inject initial share capital to create the *Waqf* fund and the *Takaful* participants become members of the *Waqf* fund. The initial amount is advised by the *Shari'ah* Board and it is usually not a major burden. The *Waqf*

[611] Zuriah, A. & Hendon, R., (2009), *op cit*, p. 35.
[612] Tobias, F. & Younes S., *op cit*, p. 144. It is really a question of who owns the *Tabarru'* fund and this is the topic of an on-going debate among many scholars. Pakistani scholars have developed the idea of using *Tabarru'* fund on a *Waqf* . A *Waqf* in the traditional sense is a legal and religious institution wherein one person dedicates some of his properties for a religious or charitable purpose. The properties, after being declared as *Waqf* , no longer remain in the ownership of the donor. The beneficiaries of a *Waqf* can benefit from the corpus or the proceeds of the dedicated property, but they are not it's owners. The ownership vests in Allaah SWT. Many Muslim jurists have treated the *Waqf* as a separate legal entity.
See also Ismail, E. *op cit*, p. 50.
[613] See also Ismail, E. *op cit*, p. 50..

fund will operate under rules laid down in the *Waqf* deed. As such, the operational model is the same as the *Wakalah Mudharabah* model but with the addition of the initial seed capital (donation) into the *Tabarru'* fund (PRF).[614]

Such a model solves both of the problems outlined above:

(iii) **Shari'ah-related/legal:** the formal difficulties have been resolved, as a *Waqf* fund is a separate legal *Shari'ah* entity with a right of ownership (comparable to corporate legal entity). Thus it can become full proprietor of the funds handed over by the shareholders and of the contributions paid by the participants.

(iv) **Technical:** the fund itself would also contain the seed capital, thereby reducing the need for interest-free loans. However, as the seed capital for the *Waqf* fund is usually only a nominal amount, the buffer might be insignificant in practice.

While numerous problems related to *Shari'ah* terms could be solved in this way, it is not clear whether the *Waqf* concept can be generally applied and widened to serve as a substitute for the Western concept of legal entity (which does not exist in the *Shariah*).

The draft regulations in Pakistan include the *Waqf* concept but do not explicitly mention *Waqf* as such; the *Waqf* concept is also used in South Africa.[615]

3.8 *WADI'AH* MODEL[616]

A model that has been proposed as an alternative model for re*Takaful* operations is based on a *Wadi'ah*, or safekeeping/trust deposit contract. Under this model, all participants would cooperate under the *Ta'awuni* model and contributions would be

[614] *Ibid.*
[615] Tobias, F & Younes, S., *op cit*, p. 146.
[616] This is a model that is being proposed to solve the problem of re*Takaful* that has been plaguing the *Takaful* industry. How effective this model will be remains to be seen as it is still shrouded in controversy. *Takaful* must address such challenges in order for it to thrive. The *Takaful* industry has been accused of being slow in innovation but innovations that are controversial will only serve to compound the existing problems. The reinsurance industry is largely dominated by conventional insurance practice. They are stronger and have the requisite experience. Whereas the *Takaful* industry is still very young hence some jurisdictions allow *Takaful* operators to reinsure with conventional companies. However, this has been seriously criticized because the *Darrurah* factor no longer subsists. *Takaful* companies must come together and pool resources in order to circumvent this problem. The *Takaful* industry in Nigeria is in more dire straits because of the numerous conflicting provisions in the regulatory instruments. These challenges must be quickly addressed in order for it to succeed. The re*Takaful* challenge is one of them.

allocated to the *Wadi'ah Yad Damanah* fund. The *Takaful* operator would be engaged under a *Wakalah* contract to manage the operation and the *Wadi'ah Yad Damanah* fund. The *Wakil* (*Takaful* operator) can invest the *Wadi'ah* fund under a guaranteed safekeeping (*Wadi'ah Yad Damanah*) contract and enjoy the full investment profit. However, a discretionary *Hibah* (gift) can be distributed, similar to what is done in Islamic banking for savings account holders.[617]

Another set up for *Wadi'ah* is to create a full-fledged *Wadi'ah* contract where no *Tabarru'* or *Wakalah* are required. In this set up, the operator acts as a depository institution permitted to receive deposits. The participants deposit their contributions based on *Wadi'ah Yad Damanah*, which would mean that those contributions are guaranteed by the operators. The participants would waive their right to receive their whole deposit due to claims payment, which would ultimately reduce those deposits either partially or substantially. At the end of the financial year, the participants receive their deposit minus the claims value. The operator as depositor can charge a *Wadi'ah* fee given the high volume of assets he is managing, even though the *Wadi'ah* fee for ordinary *Wadi'ah* is not permitted unless it is significant in volume and requires facilities to safeguard it such s coffers or the employment of security guards. The principle of charging a *Wadi'ah* fee is permitted if the safekeeping of *Wadi'ah* incurs substantial expenses and the size of the *Wadi'ah* asset is big.[618]

3.9 THE MODEL OF CHOICE

The choice of the *Takaful* operating model affects regional acceptance, product design, marketing and pricing, as described in more details below:

[617] A variation would be that the participants only promise to *Tabarru'* in the event of a claim via a *Tanazul* (waiver). The difference here is that the donation only occurs after a claim occurred. The contributions still belong to the individuals as with a *Wadi'ah* contract. The underwriting surplus of the *Wadi'ah* fund, thus, fully belongs to the participants as pointed out earlier and no ownership issues arise. This is of particular importance in an insolvency when disputes can arise over who actually owns the *Tabarru'* fund – the *Takaful* operator or the participants.
See Tobias, F. & Younes, S., *op cit*, p. 146.
[618] See Tobias, F. & Younes, S., *op cit*, p. 146..

(1) The *Wakalah* model is accepted worldwide and has the positive effect of providing a fixed and steady income stream for the operator. A key advantage over a *Mudharabah* is that the fee can be collected up-front and support acquisition costs. On the other hand, a high up-front *Wakalah* fee might look unattractive to participants and thus hinder sales. In its purest form it has no upside potential as the only source of income is the *Wakalah* fee regardless of actual claim experience.[619]

(2) The *Wakalah* model with a performance incentive has been developed to overcome the deficiency in the pure *Wakalah* model. It can be seen as an amalgam of pure *Wakalah* and *Mudharabah*, the best of both worlds so to speak from a profitability perspective. It is also the most flexible operationally as its parameters can be set such that it mirrors that of a pure *Wakalah* or a *Mudharabah*. For companies operating internationally, either model could be used by simple parameterisation. However, it should be kept in mind that this model is disputed amongst the scholars due to the sharing of underwriting surplus.[620]

(3) A *Mudharabah* model might be more attractive as profit is shared with the contract with the contract holders and the operator participates in the upside potential in the event of a positive claims experience, but the model might not be acceptable worldwide.

(4) Another problem with *Mudharabah* is the lack of up-front income to finance acquisition costs/commissions, resulting in a strain on the surplus if significant new

[619] *Ibid.* p. 147.
[620] See also Section 2.2 of Operational Guidelines, 2013 for *Takaful* Operators in Nigeria. The Nigerian *Takaful* regulatory framework as enacted in the *Takaful* Operational Guidelines for Operators, 2013, only recognizes three types of operating models namely;-
(1) *Takaful* insurance based on *Mudharabah* (profit-sharing) contract;
(2 *Takaful* insurance based on *Wakalah* (agency) contract; and
(3) Takaful insurance based on *Hybrid Wakalah-Mudharabah* (agency-profit sharing) contract.
However, Section 2.5 of the Operational Guidelines 2013, provides that, ''where the *Takaful* insurance operator is implementing an operating model that is not in line with paragraph 2.2 of the Operational Guidelines, or decides to change its operating model, the *Takaful* insurance operator will require approval from the Commission (NAICOM) before further implementation.

business is written or if the company is in its early years with no income from existing in-force business to subsidise the shortfall.[621]

(5) There has been a trend towards a *Wakalah* model for underwriting and *Mudharabah* on the investment part, i.e. a hybrid model accepted by the vast majority of *Shariah* scholars. Considering that investment income can make up the bulk of the profits for certain family savings products, it is a sensible choice for such products. Combined with a *Wakalah* with a performance incentive, it would be the most flexible model proposition from a *Takaful* operator's perspective.

(6) The *Wadi'ah Yad Damanah* plus *Wakalah* offers a viable alternative to the *Waqf* model as it clarifies any ownership ambiguities. Combined with the *Wakalah* model, it complies with AAOIFI guidelines, which is of increasing importance for internally oriented operators.[622]

3.10 RE*TAKAFUL*

Re*Takaful*, which is ''*Takaful* for *Takaful* operators'', is strictly based on *Shari'ah* principles. Re*Takaful* is a transaction whereby one company (the re*Takaful* operator) agrees to indemnify another *Takaful* company (the ceding company or cedant) against all or part of the loss that the latter sustains under *Takaful* contracts that it has issued. For this service, the ceding company pays the re*Takaful* operator a contribution.

Re*Takaful* allows operators to share risks that they cannot, or do not wish, to absorb themselves. The main purpose of re*Takaful* is similar to that of reinsurance – to spread risk and add capacity so that larger or more risks can be written. By spreading risk within the *Takaful* industry, re*Takaful* enables the *Takaful* industry to function more efficiently.[623]

[621] Tobias, F. & Younes, S., *op cit*, p. 146.
[622] *Ibid.*
[623] Tobias, F. & Younes, S., *op cit*, p. 146. p. 263.

This sounds very much like reinsurance, but the fundamental difference is that re*Takaful* is about sharing the risk, i.e. the risk is not transferred to the re*Takaful* operator. The re*Takaful* operator becomes a risk manager instead of a risk taker. This is a mirror of the relationship between a *Takaful* operator as agent and the *Takaful* participants as owner of the *Takaful* fund. The risk remains with the participants and by extension to re*Takaful* it implies that the risk remains with the ceding *Takaful* operator. This is the theoretical view, though in practice, the requirement for a *Qard Hasan* puts the re*Takaful* equally at risk.[624]

Several strong reasons have been put forward for obtaining a re*Takaful* cover and these include:

(a) **Catastrophe:** It protects the *Takaful* operator against a single, catastrophic loss (high exposure and low frequency risk) or multiple large losses, which makes it difficult to estimate the financial loss due to the lack of credible claims experience. Munich Re's re*Takaful* unit, for instance, has offered the first catastrophe excess of loss solution worldwide for family *Takaful* risks.[625]

(b) **Withdrawal:** It provides a means for the cedant to withdraw from a line of business or geographical area or production source. Here, the *Takaful* operator would simply cede all of the business concerned to a re*Takaful* operator who would let it run-off until the last policy has expired.[626]

(c) **Market entrance:** It helps the *Takaful* operator to spread the risk on new lines of business until contribution volume reaches a certain level of maturity; this can add confidence in unfamiliar coverage areas. This addresses two points; firstly, the technical

[624] This sounds very much like reinsurance, but the fundamental difference is that re*Takaful* is about sharing the risk, i.e. the risk is not transferred to the re*Takaful* operator as in conventional reinsurance. The re*Takaful* operator becomes a risk manager instead of a risk taker. This is a mirror of the relationship between a *Takaful* operator as agent and the *Takaful* participants as owners of the *Takaful* fund. The risk remains with the participants and by extension to re*Takaful* it implies that the risk remains with the ceding i operator. This is the theoretical view, although in practice, the requirement of a *Qard Hasan* puts the re*Takaful* operator equally at risk. See Tobias, F. & Younes, S., *op cit*, p. 263.
[625] Rodziah, A. & Zairol, A.A., (2012), *op cit*, p. 82.
[626] *Ibid.*

expertise needed to price risks that the re*Takaful* operator might not be familiar with and secondly, to provide capacity and/or some sort of financing until a critical mass has been reached where the *Takaful* operator can retain more risks. This is a key area for international re*Takaful* operators due to their technical experience, capacity and strong capital base.[627]

(d) **Expertise:** It provides the *Takaful* operator with a source of underwriting information when it is entering a new line of *Takaful* class or a new market. The services provided by the international re*Takaful* operators or reinsurers are due to their long experience and global networks where experience from markets all over the world is gathered. Smaller or regional re*Takaful* players may find their niche in the field of local market knowledge.

(e) **Financial:** It eases the strain on the cedant's capital during rapid contribution growth.[628]

3.11 THE CONCEPT OF GENERAL *TAKAFUL*[629]

General *Takaful* schemes[630] are basically contracts of joint guarantee, which are on short term basis, based on the principle of *Tabarru'*, *Wakalah* and *Mudharabah*, between a group of participants to provide mutual compensation in the event of a defined loss.

A *Takaful* contract is a form of unilateral contract between the participants and the *Takaful* operator i.e. a donation made without an expectation of any return and the

[627] *Ibid.*
[628] Rodziah, A. & Zairol, A.A., (2012), *op cit*, p. 83.
[629] In principle, as stated earlier on, *Takaful* system is based on mutual cooperation, responsibility, assurance, protection and assistance between groups of participants who agree to mutually guarantee among themselves against defined risk/loss. The concept of General *Takaful* is to provide a form of *Shari'ah*-compliant risk management via risk-sharing to cover participants against financial losses due to misfortune occurring to their properties or assets. See Nasser, Y & Jamil, R., *op cit*, p. 259.
[630] Section 2.1 of the *Takaful* Operational Guidelines, 2013, provides that General *Takaful* Insurance is typically a short term agreement between the *Takaful* Insurance Operator and the *Takaful* Insurance participant providing financial compensation for specified losses such as theft or damage etc, but will exclude Family *Takaful.*

Takaful operator, in turn, is also deemed to enter into a unilateral contract with the participant (donor) to cover its risks.[631]

The contracts clearly define the rights and obligations of both parties. The schemes are designed to meet the needs of protection of both individuals and corporate bodies in relation to material loss or damage consequent upon a catastrophe or disaster inflicted upon properties, assets or other belongings of its participants.[632]

The amounts of participants' contributions are determined by the terms agreed in the contract, by considering the value of the property and risk involved and tariffs that are fixed by the regulatory bodies.[633]

In Malaysia, for example, in line with the legislative provision of the *Takaful* Act,[634] the operator is required to segregate the assets of the *Takaful* funds from the assets of the *Takaful* operator. Within the *Takaful* funds, *Takaful* operators are required to establish and maintain separate *Takaful* funds in respect of Family *Takaful* business and General *Takaful* business.[635]

In General *Takaful*, the company raises a fund known as ''*Tabarru*"' fund or account, where the participants give their contributions to the fund. A small portion of the money will be deducted as *Wakalah* fee for the *Takaful* operator if they are engaged in a combination of *Wakalah* or *Mudharabah Aqad.*

The company will invest the remainder of the fund after deducting the operational cost of the scheme. Any profit or return from the investment will be returned to the fund. If there is any participant who suffers loss or damage to his property or belonging, then

[631] Rodziah, A. & Zairol, A.A., *op cit*, p. 40.
[632] Bambale, Y.Y., *op cit*, p. 195.
[633] *Ibid.*
[634] *Takaful* Act, 1984, now contained in the new Islamic Financial Services Act, 2013.
[635] Rodziah, A & Zairol, A.A., *op cit*, p. 40.

the particular participant will be compensated from this fund, by considering the level of damages and losses the participant has suffered.[636]

Based on the established legal maxim of *Fiqh* concept that *''all things are permissible unless prescribed otherwise''*, General *Takaful* contract assimilates six general insurance principles in its practices that embody the *concept of fairness* as encouraged by *Shari'ah.*

The adopted six general insurance principles are:

i) Principle of Insurable Interest (known as permissible *Takaful* Interest in *Takaful* parlance).

ii) Principle of Utmost Good Faith

iii) Principle of Indemnity

iv) Principle of Subrogation

v) Principle of Contribution

vi) Principle of Proximate Cause.

These six principles have been earlier on discussed in the chapter. The main purpose of General *Takaful* is to place the participants in the same financial position as that occupied before the occurrence of the covered perils (subject to the maximum limits of the covered amount).[637]

It is instructive to add that the practice of licensing *Takaful* business varies among the various jurisdictions throughout the world. In some jurisdictions, the licensing of the business, i.e. the permission to transact the business is granted as a composite (both Family and General Business) entity. Whilst in some other jurisdictions, only single or

[636] Billah, M.M., *General Takaful Business*, www.kantakji.com/fiqh/Files/Insurance/147.doc
[637] Nasser, Y. & Jamil, R., *op cit*, p. 262.

mono line of business is granted to a single entity. In this case, if an organisation wants to conduct both the Family and General Business, it has to set up two separate entities and apply separately for each of the licenses.[638]

In Malaysia, as prescribed under the Act,[639] licenses are granted on a composite basis. The same situation applies in Brunei where the existing *Takaful* operators conduct both the Family and General Businesses under a single license and entity. In countries like Pakistan, Sri Lanka, the Kingdom of Saudi Arabia and Indonesia, the authorities only allow a single line of business for each entity,[640]

3.12.0 FAMILY *TAKAFUL*[641]

A family *Takaful* plan is a long time savings and investment programme with a fixed maturity period. Apart from enjoying an investment profit, the plan provides mutual financial assistance in the event of death, disability or critical illnesses, depending on the *Takaful* plan among the participants.

The plan pools efforts to help the needy in times of need due to untimely death and other mishaps resulting in personal injury or disablement. Designed by the *Takaful* operator, the family *Takaful* plan enables participants to:

(a) Save regularly;

(b) Invest with a view of earning profits which are *Shariah*-compliant; and

(c) Have access to cover in the form of payment of *Takaful* benefits to heir(s) should he or she die before the maturity date of his or her *Takaful* plan.[642]

[638] Ezamshah, I., *op cit*, p. 85.
[639] *Takaful* Act, 1984, now Islamic Financial Services Act 2013.
[640] Ezamshah, I., *op cit*, p. 85.
[641] Section 2.1 of the *Takaful* Operational Guidelines, 2013, provides that Family *Takaful* Insurance is typically a long term arrangement between the *Takaful* Insurance Operator and *Takaful* Insurance participant providing the policyholder with financial relief, for instance- bereavement, critical illness or disabling injury to a fund contributor.
[642] Rodziah, A. & Zairol A.A., *op cit*, p. 63.

In Malaysia, for example, if one participates in family *Takaful*, he will be eligible for personal tax relief as in life insurance. The maximum amount of relief for an ordinary family *Takaful* is RM6,000 per year less any contributions paid to approved retirement benefit schemes i.e. Employees Provident Fund. For medical and educational plans, the tax relief is RM3000 per year.[643]

So in essence, family *Takaful* provides you with a protection and long-term savings. You and your beneficiaries will be provided with financial benefits if you suffer a tragedy. At the same time, you will enjoy a long-term personal savings because part of your contribution will be deposited in an account for the purpose of savings and investments. You will be able to enjoy investment returns from the savings portion based on a pre-agreed ratio.[644]

3.12.1 The Operations of Family *Takaful*

(1) Family *Takaful* Fund

A person who participates in any family *Takaful* plan is called a participant. A person may choose any of the plans offered by the *Takaful* operator. Family *Takaful* plans have a defined period of participation.[645]

The *Takaful* company and the participant will enter into a long-term *Takaful* contract which is based on the principle of *Mudharabah* (profit sharing), *Ta'awun* (mutual guarantee) and *Tabarru*' (donation).[646]

The *Takaful* contract spells out clearly the rights and obligations of the parties to the contract. The participant is required to contribute regularly by the *Takaful* instalments in consideration for his or her participation in the *Takaful* plan. The participant will decide

[643] Nasser, Y. & Jamil, R., *op cit*, p. 319.
[644] *Ibid.*
[645] Nasser, Y. & Jamil, R., *op cit*, p. 319..
[646] Rahman, Z.A. & Hendon, R., *op cit*, p. 57.

the amount of *Takaful* instalments that he or she wishes to pay, but such an amount shall be subject to the minimum sum as determined by the *Takaful* operator.[647]

Within the family *Takaful* funds, *Takaful* operators shall separately establish two funds for the participants' contributions:

(a) Participants' Special Account (PSA) to care for the risk (death, disability and 36 critical illnesses). This is for Malays. Another term used by operators for PSA is Participants' Risk Investment Fund.

(b) Participants' Account (PA) to cater for savings/investment components. Another term used for PA is Participants' Investment Fund.[648]

The separation of the risk and savings/investment components is necessary to recognise the different ownership, purpose and risks associated with the contributions. A description of the PSA and PA are as follows:

1. The Participants' Special Account (PSA) shall be used to pool the *Tabarru'* portion of the contributions, and serves to provide mutual financial aid and assistance when claims are made for risks covered under the *Takaful* contracts such as death or permanent disability. For annuity products, the PSA shall be used to pool the *Tabarru'* contributions meant to provide payments during the annuity period. Under the *Tabarru'* contract, the fund is owned by the pool of participants. In managing the PSA, the *Takaful* operators shall adopt appropriate set of policies and procedures to ensure the availability of funds to meet *Takaful* benefits when due.[649]

2. The Participants' Account (PA) shall be used to pool the savings and/or the investment portion of the contributions. Consistent with the requirements of *Shari'ah*,

[647] Rodziah, A. & Zairol, A.A., *op cit*, p. 63.
[648] *Ibid.*
[649] Rodziah, A. & Zairol, A.A., *op cit*, p. 63.

the PA is individually owned by the participants. In managing the PA, the *Takaful* operator shall adopt appropriate investment and management strategies to achieve returns that are in line with the participants' reasonable expectations. For investment-linked *Takaful*, the PA shall be in a unitised form (where the amounts invested are converted into units).

Any profits generated from the investment shall be shared between the participant and the company in a pre-agreed ratio within the contract of *Mudharabah.* For instance, if the ratio agreed is 7:3, then the participant shall be entitled to 70% of the profits whilst the company shall be entitled to 30% or vice versa, depending on the contractual terms.

The participant's share of the profits shall be credited into his or her Participant's Account. With the accumulation of such profits, the balance in the Participant's Account will increase over a period. The amount of *Mudharabah* profit will be refunded to the participant on a later date when there is a benefit payment on claims, surrender or maturity.[650]

3.13 *TAKAFUL* APPLICATION UNDER NIGERIAN LEGAL AND REGULATORY FRAMEWORK

In discussing this sub-topic of the thesis, it is pertinent to sound a caveat here. What is striking is that Islamic banking, insurance and finance are actually Islamized conventional banking, insurance and finance. The products are products of conventional banking, insurance and finance but ''Islamized'' by removing the features prohibited by *Shari'ah* and applying *Shari'ah* principles to achieve the same or similar effects. That

[650] Rodziah, A. & Zairol, A.A., *op cit*, p. 64.
It suffices to posit that there are three main objectives held by those who participate in the family *Takaful* scheme. First, it is to provide financial coverage for their beneficiaries in the event of premature death. Secondly, it is to have a form of savings for future use or for old age. Thirdly, it is to be financially prepared in case of an accident which results in long-term disability or in case of a chronic disease. Thus the *Takaful* operator will normally offer a scheme which provides cover to achieve such objectives. See Sudin, H. &Wan Nursofiza, W.A., *op cit*, p. 452.

Islamic banking, insurance and finance develop that way is a matter of practicality: that it is the only practical way to do so under the existing circumstances.[651]

As stated in the previous chapter, the law regulating conventional form of insurance is broadly classified into two. The first part is the law of insurance contract itself which deals with the legal relationship between the insurance company or insurer and the person taking out the insurance policy or the insured. The second part of the regulatory framework is the body of laws that regulate the conduct of the business of insurance and the entire regulatory machinery through which the insurance industry is controlled and supervised. Although insurance principles and legislative instruments are so closely connected and collectively constitute the body of laws that regulate the affairs of the industry, the two are distinct in their features, effects and historical sources.[652] This scenario stated above is what is exactly replicated in the course of the application of Islamic insurance (*Takaful*) in Nigeria.

A descriptive analysis of what is *Takaful* as it is known world-wide was made at the beginning of this chapter to equip the study with basic toolset of Islamic insurance. This is necessary for purposes of threading and linkage so that a smooth flow is achieved in grasping the rudiments of *Takaful* insurance and how it dove-tails with conventional insurance in reinventing and reinvigorating insurance practice world-wide. To those who are not too familiar with *Takaful*, its concise inclusion here makes it readily available as reference.

The basic components of *Takaful* insurance are the same the world over with some slight differences in understanding and interpretation due to differences in adherence to the teachings of *Madhabs* (schools of thought). The Nigerian Muslim community adheres to the *Maliki Madhab* but this is of no great significance since the application of

[651] Bakar, M.D. & Engku Ali, E.R.A., (eds.), *op cit*, p. v.
[652] Irukwu, J., (1993), *op cit*, p. 3.

Takaful in Nigeria is practically based on the general understanding of *Takaful* as discussed at the beginning of the chapter which is supported by all the of the four main schools of thought. The provisions of the Nobel Qur'an and *Sunnah* of the Prophet (pbuh) are sacrosanct and are not subject to much controversy. All these add up to be the main sources of basic *Takaful* laws as applied in Nigeria. This is discussed further below.

3.13.1 Legal Basis of *Takaful* under the General Law

Basically, *Takaful*, in a way similar to conventional insurance, is a provision against loss or misfortune and a mechanism for sharing risk. Universally, insurance, whether conventional or otherwise, aims at providing protection, sense of security and comfort against misfortune. It is about protecting what is dear to someone as long as it is legal under the law. Insurance shields the insured and relieves him of the burden of worries. It translates into peace of mind and makes people safe and confident to make business decisions and take more progressive and ambitious business risks.[653] Furthermore, insurance confers financial independence (especially annuity), guarantees good standard of living and comfortable retirement for the assured. It also inculcates a culture of discipline and thrift in the individual and the larger society. Once a life policy is taken, the assured automatically creates some wealth, up to the value of the sum insured or the capital benefit. The level of savings through life assurance and pensions is an indication of wealth or economic development. The rate of insurance penetration and density has positive correlation with the rate of development and economic growth of a nation.[654]

[653] Adamu, A.I., *op cit*, p. 73.

[654] The importance of economic growth and development cannot be overstated. Income growth is essential for achieving economic, social and even political development. Countries that grow strongly and for sustained periods of time are able to reduce their poverty levels significantly, strengthen democratic and political stability, improve the quality of their natural environment, and even diminish the incidence of crime and violence. See Yusuf, T.O., (2012), Prospects of *Takaful*'s (Islamic insurance) Contributions to the Nigerian Economy, *Journal of Finance and Investment Analysis*, Vol. 1, No. 3, Science Press, p. 221. See also Barro, R.G., (1996), Democracy and Growth, *Journal of Economic Growth*, 1(1), pp. 1-27. See also Easterly, W., (1999), Life During Growth, *Journal of Economic Growth*, 4(3), pp. 239-276. See also Dollar, D. & Kraay, A., (2002), Growth is Good for the Poor, *Journal of Economic Growth*, 7(3), pp. 195-225.
See also Ahmad, R. & Auzzir, Z.A., *op cit*, p. 1, where they stated that ''a lot of literature and empirical evidence has shown that countries would have more stable long-run growth if supported by a better-developed financial system. One of the financial instruments that supports economic growth is insurance, a tool that is used to mitigate risk''.

Insurance serves as a medium for securing long term investment funds which could be channelled into capital markets for manufacturing, industrialization and other developmental projects. It facilitates international trade and serves a major source of foreign exchange earnings and cross border investments.[655] Islamic insurance or *Takaful*, as a complementary model to conventional insurance, provides an alternative product to the Nigerian insurance market because of its compliance with *Shariah* principles which is appealing to the greater majority of the population who are Muslims[656] and also non-Muslims who feel that the return of premium at the end of a transaction is an equitable business deal.

In recognition of the potential of *Takaful* towards enhancing an efficient and equitable allocation of resources by way of commerce and entrepreneurial activities at micro level of the society in Nigeria, the Insurance Regulatory Authority constituted a committee for the smooth integration of *Takaful* insurance into the legal and regulatory framework of the Nigerian insurance industry.[657]

As stated earlier, the regulatory framework for insurance has two different connotations. The first is the law of contract that deals with the relationship between the insured and the insurer. The second is the law that regulates the conduct of business of insurance and the entire regulatory machinery. The Insurance Core Principles (IAIS) provides:

> ''A sound regulatory and supervisory system is necessary for maintaining efficient, safe, fair and stable insurance markets for promoting growth and competition in the sector. Such markets benefit and protect policyholders.''[658]

[655] Yusuf, T. O., *op cit*, p. 222.
[656] Muslim communities in the business world have protested against conventional insurance in which the business transactions involved are not *Shari'ah*-compliant. Therefore an alternative to conventional insurance is needed and thus, Islamic scholars have introduced the doctrine of *Takaful*. See Ahmad, R. & Auzzir, Z.A., *op cit*, p. 1.
[657] NAICOM Regulatory Committee on *Takaful* Implementation and Integration.
[658] ICP, p. 12.

The provisions of core principles provide a globally accepted framework for regulation and supervision of the insurance sector. The rules establish the basis for evaluating insurance and the effectiveness of the supervisory systems and procedures. It is in this sense that this study deems it imperative to make a case for statutory underpinning or legislative safeguard to give the enabling legislation broader latitude to support and entrench the application and development of *Takaful* industry through liberalization in terms of standards, entry requirements, operational models, design and marketing structure for *Takaful* products which are, nonetheless, fully *Shari'ah* compliant.

The principal legislations for the insurance industry in Nigeria are four, namely:-

1. The Insurance Act, 2003, **(INSURANCE ACT)**[659]

2. *Takaful* Operational Guidelines, 2013[660]

3. The National Insurance Commission Act, 1997, **(NAICOM ACT)** and

4. The Companies and Allied Matters Act, 1990 **(CAMA)**

Some of these legislations have been discussed in the previous chapter but with particular reference to the application of conventional insurance in Nigeria. The specific reference to these legislations here is, however, not meant to undermine the strategic positions other legislations occupy in regulating certain aspects of the insurance business[661] or institutions.[662]

[659] The Insurance Act, 2013, Laws of the Federation of Nigeria, is the single most important legislation regulating the insurance industry in Nigeria. By virtue of its enactment, it has abolished all other previous legislative instruments regulating the insurance industry, with the exception of Marine Insurance Act, 1961, which is still applicable. Most of the provisions are the same with the previous legislations with few changes or alterations here and there to suit the contemporary age. Some provisions of the Act were discussed in chapter two of this study.

[660] The *Takaful* Operational Guidelines for Operators were released in March, 2013, as a result of the huge clamour by Muslims in Nigeria who constitute more than 70% of the population of 150 million, to find an alternative to conventional insurance practice which is not *Shari'ah*-compliant. Most Muslims have refused to partake in the insurance scheme due to the *Shari'ah* prohibitive features, thus compounding the problem of insurance deepening penetration in the insurance industry. There are so many controversies surrounding the release of the Guidelines as well as fundamental conflicts with some provisions of the Insurance Act, 2003 that has necessitated this study.

[661] E.g. Nigerian Council for Registered Insurance Brokers, Act 2003; Marine Insurance Act, 1961, Motor Vehicles (Third Party Insurance) Act, 1945.

[662] E.g. Chartered Insurance Act, No.22 of 1993; Pension Reform Act, 2004; Investment and Securities Act, 1999.

Under the Nigerian legal framework, for a contract of *Takaful* insurance to come into existence, certain essential requirements must be satisfied which are in tandem with the general Common law principles of insurance contracts but devoid of the anti-*Shariah* features. This means the subject matter of *Takaful* insurance may be any movable or immovable property, and in practice is always amply described in the insurance certificate or policy. One may, for example insure against the theft of his property or against the property being damaged by fire. Apart from physical objects, the subject matter of *Takaful* insurance may consist of an event, whose occurrence may expose the assured to liability against another person.[663]

Furthermore, since a contract of *Takaful* insurance operates within the general principles of law of contract, devoid of the anti-*Shari'ah* features, the *Takaful* contract may be made orally,[664] since there is no special form prescribed in law for making a contract of insurance. But nowadays, it is customary to embody the terms of the insurance contract in a written document because of the complexities of insurance contracts.[665]

Since a contract of *Takaful* insurance is a simple contract, it must satisfy the fundamental requirements for the making of such a contract. These include the mutuality of consent between the parties; the parties must have contractual capacity; the agreement must be supported by a consideration in order to ensure its enforceability; the parties must have intended to create a legally binding contract, and the object of the contract must not give rise to illegality.[666]

All insurance contracts are not only subjected to the general principles of the law of contract in Nigeria, but also certain special legal principles that are embodied in

[663] Yassin, N. & Ramly, J., (2011), *Takaful: A Study Guide*, IBFIM, Malaysia, p. 154.
[664] The only exception here under conventional insurance is that Marine Insurance must be in writing.
[665] Okany, M.C., *op cit*, p. 813.
[666] See Okay, A., *op cit*, pp. 317-318. See also Yassin, N. & Ramly, J., *op cit*, p. 154.

insurance contracts. In this context, these principles are also applicable to *Takaful* insurance contracts.[667] These are:

1. Utmost good faith

2. Insurable interest

3. Indemnity

4. Contribution

5. Subrogation

6. Proximate Cause

The Nigerian insurance legal framework approach to the application of utmost good faith takes a slightly modified stance. In modifying the Common Law principle of utmost good faith to suit the Nigerian environment, **Section 54(1) of the Insurance Act** shifted the burden of materiality of information from the insured or proposer to the insurer by requiring that all proposal forms should elicit such information considered by the insurer to be relevant.[668] This is in total contrast with the provisions of standard Common law insurance practice. One can understand the reason for deviation by the Nigerian insurance legal framework, because the courts have been inundated with cases of insurance companies taking advantage of unsuspecting insurance clients innocently seeking legal cover only to end up being short changed by the antics of dubious insurance companies who always capitalize on technical requirements to fleece unwary clients.

[667] Ismail, E., (2011), *Basic Takaful Broking Handbook: Course Manual for Basic Certificate Course in Takaful Broking (BCCTB)*, IBFIM, Malaysia, p. 77.
[668] This provision of the insurance Act, 2003, Laws of the Federation of Nigeria has been discussed at length in the second chapter of this study. The import of this provision on *Takaful* is highly controversial as to which law should be applied. See discussion in footnotes therein.

3.13.2 Legal Basis of *Takaful* Application under Insurance Act 2003

The Act is the foremost legislation that regulates insurance business in Nigeria. On application, specifically, the Act says:

> ''This Act applies to all insurance businesses and insurers, other than insurance business carried on or by insurers of the following description –
>
> (a) A friendly society that is an association of persons established with no share for the purposes of aiding its members or their dependants where such association does not employ any person whose main occupation –
>
> (i) Is the canvassing of other persons to become members of the association ;
>
> (ii) Is the collection of contributions or subscriptions towards the funds of the association from its members; or
>
> (b) a company or any other body (whether corporate or unincorporated) or person whose business is established outside Nigeria, engaged solely in reinsurance transactions with an insurer authorized or pursuant to the provisions of this Act to carry on any class of insurance business, but not otherwise however.''[669]

It is clearly evident in the provision cited above that there is no specific mention of *Takaful*. This study submits that this lack of legislative mention of *Takaful* or Islamic insurance creates a huge legal gap that will allow ambiguity and uncertainty to fester in the minds of stakeholders and the insuring populace. However, the regulatory authority, NAICOM, is quick to point out that there is an allusion to *Takaful* in the provision. It maintains that the Act takes care of *Takaful* insurance by inference. The study again

[669] Section 1 of the Insurance Act, 2003, Laws of the Federation of Nigeria (LFN)

submits that this is not good enough because *Takaful* is far too robust and important to be referred to by inference. The interpretation of the provision will have to be tested in court of competent jurisdiction to ascertain its veracity. This study hopes that the outcome will help make a case for legislative underpinning to resolve the issue.

A cursory look into the definition of the friendly society by the Section will tempt a conclusion that *Takaful* insurance falls within the variants of the businesses excluded from the regulation of the Act.[670] However, the robust commercial nature of modern *Takaful* operation demands that the operator should maintain a minimum paid up share capital and canvass for business to remain afloat in the competitive insurance market.[671]

Generally, the Act sets standard for registration, regulation, administration and control of the insurance business as well as establishes financial and prudential requirements for insurance institutions in Nigeria.

Section 86[672] vests in the National Insurance Commission of Nigeria (**NAICOM)** the responsibility for administration and enforcement of the provisions of the Act and authorizes it to carry out the requirements of the Act. This, in effect, places the responsibility for the regulation and enforcement of *Takaful* in the Commission[673]. It provides thus:

> ''Subject to the provisions of this Act, the National Insurance Commission (in this Act referred to as ''the Commission'') shall be responsible for

[670] The Section defines a 'friendly society'' as an association of persons established with no share for the purpose of aiding its members or their dependants where such association does not employ any person whose main occupation is;
(1) canvassing others to become members of the association;
(2) collection of contribution or subscription towards the funds of the association from its members.
See Section 1 Insurance Act, 2003 which presupposes that;-
(a) The Act recognizes the existence of some of insurance business or insurers other than those it regulates;
(b) That all insurance businesses not specifically mentioned in subsection (a) and (b) should be under regulatory remit of the Act.
[671] Adamu, A.I., (2013), *op cit*, p. 77.
[672] Insurance Act, 2003 LFN.
[673] Adamu, A.I., *op cit*, p. 78.

administration and enforcement of this Act and is hereby authorized to carry out the provisions of this Act.''[674]

It is submitted that this area of administration and enforcement outlined in the above provision has been the bane of insurance practice in Nigeria and is expected to impact negatively on *Takaful* once it is fully entrenched if adequate steps are not taken to put it in check. It is paramount for character of the law to be injected in enforcement provisions if the desired effect is to be achieved. The Insurance Act prescribes punishments for the violations of its provisions in either fines or imprisonment or both but is surprisingly silent on how the provisions should be enforced.[675]

These are some of the challenges facing the Nigerian insurance industry which this study hopes to address at the end of the day.

It is noteworthy that in Malaysia, the number one *Takaful* practicing nation in the world, insurance practice is regulated by the country's Central Bank or Bank Negara. This makes it much easier to supervise because insurance has now reached unprecedented level in liquidity volume and is central to ever expanding economic transformation.

Although still in its teething stage, it is without doubt that *Takaful* has been duly recognised as an integral part of the Nigerian insurance industry. Consequently, in an effort to integrate *Takaful* into the existing legal framework, the need arose to come up with operational guidelines to make some of the provisions of the Act accommodating in order to embrace *Takaful* insurance. In this regard, **Section 9 of the Act** which provides for minimum paid up capital was relaxed in the *Takaful* guidelines which

[674] Section 86 Insurance Act 2003.
[675] Mr Kola Adedeji, Managing Director, Niger Insurance Plc, stated in an interview that ''generally, the legislative framework for insurance practice in Nigeria is inadequate and ineffective. Often times we find the law making unenforceable provisions which though good on paper is almost impracticable without strong enforcement provisions. The law makes provision for NAICOM to enforce the insurance laws against insurance companies through the inspectorate division in the Commission but provides no means of enforcement against the public in general. The Commission has no power of arrest irrespective of the fact that there are sanctions provided in the law. How would arrest and legal action be taken to ensure sanctions are meted out to individuals in breach of the law?, he asked''. See Daily Trust Newspaper, 24th September, 2015, p. 34.

brought down the minimum paid up capital for *Takaful* insurers to N100 million.[676] This issue of accommodation by downward review of required paid up capital for *Takaful* insurers is, however, controversial and is subject to debate as the Commission's power under the Act relates only to upward review of the minimum paid up capital.[677] It remains contentious whether the power to increase the paid up capital would accommodate the power to decrease in the prescribed minimum share capital. The Insurance Act, 2003[678] provides, concerning the share capital, thus:-

> '' (1) No insurer shall carry on insurance business in Nigeria unless the insurer has and maintained, while carrying on that business, a paid-up share capital of the following amounts as the case may require, in the case of –
>
> (a) Life insurance business, not less than N150,000,000;
>
> (b) General insurance, not less than N200,000,000;
>
> (c) Composite insurance business, not less than N350,000,000; or
>
> (d) Reinsurance business, not less than N350,000,000
>
> (2) The paid-up share capital stipulated in subsection (1) of this section in the case of existing insurer –
>
> (a) Shall come into force on the expiration of a period of nine months from the date of commencement of this Act; and
>
> (b) May be subscribed to by the capitalisation of undistributed profits as approve by the Commission.

[676] This is the paid up capital requirement contained in the registration requirements for *Takaful* operation. The recent recapitalization of the insurance industry has jerked up the minimum paid up capital in the insurance industry to N3 billion for General Insurance Business and N5 billion for Life Insurance Business. Reinsurance stands at N25 billion. This high entry requirement is one of the highest in the world. Criticisms have followed this provision because most insurance industries of the world are now moving towards Risk-Based Capitalisation regime as opposed to a flat entry platform like that of the Nigerian insurance industry.
[677] Section 9(4) of the Insurance Act, 2003.
[678] Section 9(1) *Ibid.*

(3) The Commission shall –

(a) cancel the registration of any insurer or reinsurer that fails to satisfy the provisions of subsection (1) of this section as it relates to the category of operation of such insurer or reinsurer; and

(b) not later than thirty days after expiry of the period specified in subsection (2) of this section publish a list of all insurers and reinsurers that have complied with the provisions of this section.

(4) The Commission may increase from time to time the amount of minimum paid-up share capital stated in subsection (1).

Subsection (4) above is the controversial provision. The operational word here is ‘’increase’’ and not ‘’decrease’’. So where did this authority to decrease the share capital for *Takaful* insurers emanate from?

Section 10 of the Act[679] requires that an insurer/*Takaful* operator intending to commence business, to deposit the equivalent of 50% of the paid up capital with the Central Bank of Nigeria (CBN) as its statutory deposit. However, after registration, 80% of the deposit would be released to the insurer/*Takaful* operator. 10% will be maintained with CBN as minimum statutory deposit which shall attract interest at the minimum lending rate on every January of each year. It is submitted that this area of mandatory annual interest on the statutory deposit is one of possible areas of conflict with the fundamental principles of *Takaful* which prohibits interest (*Riba*)[680]. This goes against the principles of *Shari'ah* which will render the application of *Takaful* a nullity. This is one area of contention which this study has exposed and must be remedied in order for

[679] Insurance Act, 2003 LFN.
[680] Adamu, A.I., *op cit*, p. 79.

Takaful to take its rightful place and contribute its quota in the insurance industry and to the GDP of the country.

The Section provides thus:-

> '' (1) An insurer intending to commence insurance business in Nigeria after the commencement of this Act shall deposit the equivalent of fifty per cent of the paid-up share capital referred to in section 9 of this Act (in this Act referred to as the ''Statutory Deposit'') with the Central Bank.[681]
>
> (2) Upon registration as an insurer, eighty per cent of the statutory deposit shall be returned with interest not later than sixty days after registration.[682]
>
> (3) In the case of existing companies an equivalent of ten per cent of the minimum paid-up share capital stipulated in section 9 shall be deposited with the Central Bank.[683]
>
> (4) Any statutory deposit made under subsection (1) of this section shall attract interest at the minimum lending rate by the Central Bank on every 1 January of each year.[684]
>
> (5) Any withdrawal from the statutory deposit shall be made good within thirty days, failure of which shall constitute a ground for suspension from business and such suspension shall be published in the newspapers.[685]
>
> (6) Failure to deposit the statutory deposit shall constitute a ground for cancellation of the certificate of registration.[686]

[681] Section 10(1) Insurance Act 2003.
[682] Section 10(2) *Ibid*.
[683] Section 10(3) *Ibid*.
[684] Section 10(4) Insurance Act 2003.
[685] Section 10(5) Insurance Act 2003..
[686] Section 10(6) *Ibid.*

To create an enabling environment for registration and smooth take off of full-fledged *Takaful* insurance application in Nigeria, the Commission exercised its powers under **Section 101 of the Act**[687] and issued Guidelines in March, 2013, for *Takaful* insurance,[688] which have the objectives of:-

a) Providing minimum standards for the operation of Takaful Insurance in Nigeria;

b) Ensuring consumer protection in relation to Takaful insurance products;

c) Setting up general requirements for Takaful insurance;

d) Establishing duties and responsibilities of *Takaful* insurance operators and other insurance institutions in the market; and,

e) Setting conditions for the entry and exit of operators from *Takaful* business.

The guidelines prescribed general requirements for carrying out *Takaful* insurance in Nigeria, which include:-

1) Entry requirements: a limited liability or a subsidiary of the insurance company; minimum paid-up capital prescribed by the Commission.[689]

2) Class of business: two broad classes of family solidarity and General *Takaful*

3) Qualification requirements: the aims and operations of *Takaful* will not involve anything not approved by *Shari'ah*; establishment of a *Shari'ah* Advisory Committee to advise the operator.

[687] The provision of the Section states that the Commission may make rules and regulations generally for purposes of giving effect to the Insurance Act, 2003.
[688] Operational Guidelines 2013 (*Takaful* Insurance Operators) issued by the National Insurance Commission
[689] Registration requirements for *Takaful* Operators 2013, National Insurance Commission of Nigeria.

4) Grounds for cancellation of operator's authorization: pursuing aims or carrying operations which are not approved by *Shari'ah*; failure to carry on business after twelve months of registration.

The fact that the Guidelines have made it explicitly clear that the aims and operations of *Takaful* will not involve anything not approved by *Shari'ah* has not put to rest the raging controversy of interest on the paid-up share capital because of the superiority of the Act in the event of inconsistencies.[690] There has to be a proactive legislation or review of the provisions of the Act to marry it with the *Shari'ah*-compliant provisions contained in the Guidelines for *Takaful* operation in Nigeria. In the alternative, the provision contained in the Insurance Act will have to be tested in a court of competent jurisdiction to address the controversy decisively.

3.13.3 *Takaful* Application under the *Takaful* Operational Guidelines 2013[691]

The Guidelines for *Takaful* insurance provide guidance on elements that are specific to the operations of a *Takaful* insurance operator. These Guidelines are to be read in conjunction with other relevant legislations, guidelines and circulars as determined to be applicable to *Takaful* insurance operators by the Commission. The Guidelines represent primary regulatory framework with regards to *Takaful* insurance.[692]

The registration requirement for *Takaful* Operators in Nigeria is divided into four (4) parts which include:-

[690] See Section 100 of the Insurance Act, 2003 which provides that ''The provisions of this Act are without prejudice to the application of the Companies and Allied Matters Act, 1990 and any other enactment applicable to insurance institutions under the Act which are companies registered under that Act, so however that where any of the provisions of the Companies and Allied Matters Act, 1990 and other enactment is inconsistent with any provisions of this Act, the provisions of this Act shall prevail to the extent of that inconsistency. (Emphasis mine).

[691] Section 1.2 of *Takaful* Operational Guidelines states – ''A part of NAICOM's on-going pursuit to increase insurance penetration in Nigeria and increase the contribution of insurance to the National GDP, the need for *Takaful* insurance was identified following detailed research. *Takaful* insurance is a form of insurance that incorporates elements of mutuality and ethical finance considerations and is open to all people regardless of faith and background. These Guidelines are issued to provide regulatory guidance for *Takaful* insurance in the industry with the desire of enhancing financial inclusion in Nigeria and to ensure *Takaful* insurance providers are not disadvantaged''.

[692] Section 1.3 *Takaful* Operational Guidelines, 2013.

(1) The corporate status which implies that the applicant must be a limited liability company registered under the Companies and Allied Matters Act (CAMA), 1990.[693] The company must have as part of its name such words or terminologies which connote *Takaful* operation and the Article of Association of the company shall make provision for the establishment of an Advisory Council of Experts (ACE)[694] among others. The second part is the application requirements which involve the submission of completed application form, submission of business plan, operational system manuals, notice of location of principal office or registered office of the company,[695] among others, all to be accompanied with all relevant documents for registration. Parts three and four of the registration requirements deal with corporate governance issues and procedures for product approval respectively.[696]

The Operational Guidelines, 2013 for *Takaful* Insurance Operators outline and define the framework within which *Takaful* Insurance Operators are to carry out *Takaful* Insurance business. The objectives of the Guidelines are as follows[697]:-

(a) Establish duties and responsibilities of *Takaful* Insurance Operators and other institutions

(b) Set requirements and minimum standards for operation and disclosure that aim to protect the interests of consumers

(c) Provide a framework for the establishment and growth of *Takaful* Insurance business that is efficient and leads to financially sound and sustainable *Takaful* Insurance funds.

[693] Section 3.1, *Ibid*.
[694] Section 3.6, *Ibid.* The section states that '' The *Takaful* Insurance Operator before starting *Takaful* Insurance operations shall have in place an Advisory Council of Experts (ACE) to ensure the operations are in line with best practice. Any alternative approach to the establishment of the ACE must be approved by the Commission as per Section 3.11.
[695] Section 3.2, *Ibid.*
[696] See Sections 3.1 and 4.1 of *Takaful* Operational Guidelines 2013.
[697] See Section 1.5, *Ibid.*

The Guidelines regulate only Commercial *Takaful* insurance business conducted in Nigeria and cover the operational processes relating to *Takaful* Insurance Operators[698]. These include:-

(1) Establishment of *Takaful* Insurance operating models

(2) Specific governance standards for *Takaful* Insurance Operators

(3) *Takaful* Insurance fund management methods

(4) Management of participants (policyholders)

(5) Operators' specific operational requirements

(6) Capital requirements for a *Takaful* Insurance Operator

(7) Reporting requirements for *Takaful* Insurance Operators.

The Guidelines apply to *Takaful* Insurance Operators including (Micro-*Takaful* Insurance) that are operating exclusively as *Takaful* Insurance providers (''stand-alone operation'') and to *Takaful* Insurance business being provided by a conventional insurance institution alongside existing conventional insurance business (''window operators''). The Guideline is limited in the consideration of Re*Takaful* Insurance to the requirements of a *Takaful* Insurance Operator as set out in paragraph 6.12. Additional requirements may be set by the Commission from time to time as deemed fit for Micro-*Takaful* Insurance providers.

According to the Guidelines, the concept of *Takaful* Insurance is a form of insurance that is compatible with the principles of *Shari'a.h*[699] Market survey undertaken by the Commission prior to the issuance of these Guidelines, indicated a significant religiously based objection to conventional insurance. A number of financial principles inspired by

[698] See Section 1.7, *Takaful* Operational Guidelines 2013.
[699] See Section 1.11 of *Takaful* Operational Guidelines, 2013.

Shari'ah are shared by other Abrahamic faith. *Takaful* Insurance is in consonance with elements of mutual insurance, ethical financial management and is also accountable to all insuring public regardless of faith.[700]

The Guidelines further lists the key elements of a *Takaful* Insurance scheme which include among others, the following:-

(a) Mutual guarantee – all policyholders agreeing for the pooled funds to be used for assistance in specified circumstances of loss;

(b) Ownership of fund – the participants are the main owners of the *Takaful* Insurance fund';

(c) Management of the *Takaful* Insurance fund – the management role is performed by the *Takaful* Insurance Operator in consonance with international best practices';

(d) Investment conditions – any investment activity performed using the participants' contributions must be in line with governing principles of *Takaful* insurance 9e.g. avoiding investment in select unlawful industries that are deemed harmful to society and avoiding interest.

The controversial sections of the Guidelines that appear to be in conflict with other regulatory instruments on insurance have been dealt with in this chapter under the legal basis of application of *Takaful* under the Insurance Act, 2003 (3.13.2).

[700] The Guidelines further provide that *Takaful* Insurance is based on two principles:
(i) *Tabarru'* (donation/contribution) – is a donation covenant where all participants agree to mutually support each other and is the basis of participants' contributions into *Takaful* Insurance Fund.
(ii) *Ta'awun* (cooperation) – is the established Islamic concept of mutual assistance and is the basis on which participants willingly agree for the *Takaful* Insurance Fund to be used for the mutual benefit of all participants to meet eligible claims.

3.13.4 Legal Basis of *Takaful* Application under the National Insurance Commission Act (NAICOM)[701] 1997

The Act establishes the Commission as a body empowered to administer, regulate, supervise and control insurance businesses and activities in Nigeria. **Section 7 of the Act** empowers the Commission to set standards for the conduct of insurance business in Nigeria. The Commission is also empowered to carry out regulatory activities in form of inspection, actuarial investigation and intervention with a view to ensuring control and compliance with the requirements of the law. On the strength of this, the Commission has powers to scrutinize annual accounts and returns to ensure that the insurer maintains statutory reserves and margin of solvency required by the Insurance Act.[702]

In exercise of the powers under the Act,[703] the Commission constituted a committee to come up with registration requirements for *Takaful* insurance in Nigeria. The committee submitted its report[704] and recommended the following:-

a) Adoption of registration requirements similar to that of conventional insurance with some amendments to meet *Takaful* Guidelines;

b) Initial paid-up capital of N100 million each for general *Takaful* and Family *Takaful* operators;

c) All existing companies offering '*Takaful* window services' should have additional paid-up capital which shall be ring-fenced from the existing capital of the conventional insurance business;

[701] Section 6 of the NAICOM Act provides that ''the principal objective of the Commission shall be to ensure the effective administration, supervision, regulation and control of insurance business in Nigeria. One of the major criticisms of the Commission is that it is too much into supervision and has virtually left the development of insurance in the hands of insurers, hence the virtual stagnation of the industry.
[702] Adamu, A.I., *op cit*.
[703] Section 49(1)(b) and Section 64 of NAICOM Act, 1997.
[704] Report of the Committee on Registration of *Takaful* Presented to Top Management Meeting of NAICOM in February, 2013, Abuja, Nigeria.

d) The adoption of global trend for separate licenses for General *Takaful* or Family *Takaful* operators;

e) Establishment of distinct *Takaful* Advisory Council for the Commission to meet the specific needs of *Takaful* operations;

f) Revisit window operations because of its complexities in funds segregation etc.

The legal basis of *Takaful* application in Nigeria under the NAICOM Act is further enshrined in the fundamental public policy objectives set for the Commission in the Guidelines which include the following:-

1) To ensure that the business of *Takaful* is conducted in accordance with the *Shariah* and sound insurance principles;

2) to ensure that all *Takaful* operations are managed in an efficient and responsible manner by qualified officers of integrity;

3) to ensure that all *Takaful* companies are financially viable and adequately capitalized and capable of discharging their financial responsibilities; and,

4) To ensure the protection of policyholders and the insuring public generally, from weak and unscrupulous insurance/*Takaful* practitioners who may have gone into the business with ulterior motives.[705]

3.13.5 Legal Basis of *Takaful* Application under the Companies and Allied Matters Act (CAMA) 1990

With the exception of statutory corporations such as African Insurance Corporation (Africa Re) all registered insurance companies in Nigeria are subject to the provisions of the Companies and Allied Matters Act, 1990 (CAMA). Section 3(a) of the Insurance

[705] Adamu, A.I., *op cit*, p. 83.

Act, 2003 requires a company to be duly incorporated under the CAMA as condition precedent for registration as an insurer. The provision, however, excludes statutory corporations.[706] The Act requires an applicant for business operations to be incorporated as a limited liability company.[707]

Within the provisions of CAMA, a company can either be incorporated as a company limited by shares or by guarantee.[708] Although the provision of Section 3 of the Insurance Act only made mention of incorporation of a company, the requirements of Section 9 of the Act has by implication established that an applicant for *Takaful* operations must be a limited liability company. Furthermore, the guidelines have made specific provisions that:

> ''no person shall carry on *Takaful* business in Nigeria unless it is a limited liability company or a subsidiary of insurance company having a paid up capital prescribed by the Commission.''[709]

Despite the requirements for incorporation, the provisions of CAMA regulate activities of *Takaful* operators from incorporation to winding up just like it is with other corporate entities. The significant role played by CAMA is in the area of returns, for instance, the *Takaful* insurance company is required by CAMA, before it commences business, to submit to the Corporate Affairs Commission (CAC), a statement of returns in a prescribed manner, on the first Monday in February and on the first Tuesday in August of every year during which it carries on business.[710] The provision therefore envisages that all *Takaful* operators will furnish the Corporate Affairs Commission with the statement of returns containing the following information:-

i) The amount of nominal share capital;

[706] Section 3(b) Insurance Act, 2003.
[707] Adamu, A.I., *op cit*, p. 84.
[708] Section 21 of Companies and Allied Matters Act (CAMA), 1990.
[709] Section 2, 1(i) & (ii) Guidelines for *Takaful* Insurance Issued by the National Insurance Commission (NAICOM).
[710] Section 553 of Companies and Allied Matters Act, 1990.

ii) The issued share capital and the proportion thereof called;

iii) It's proven and estimated liabilities;

iv) It's assets including cash at the bank;

v) The insurer's other securities.

Another important area where the provisions of CAMA feature in the take-off of *Takaful* is the filing of its paid-up capital, registered office address, particulars of Directors and statutory meetings. Section 211 of CAMA requires every public company to hold a general meeting of its members within six months of its incorporation. Therefore, by extension, where the *Takaful* operator is a public company within the context of the law, compliance with this provision is mandatory. The provisions of CAMA also impact on the choice of name for *Takaful* operators in order to prohibit the use of word like 'cooperative' which if used will have to be subjected to the requirements of Section 30 of CAMA.

However, in spite of the role of CAMA in the affairs of companies, Section 100 of the Insurance Act subjects the application of CAMA provisions or requirements to be in conformity with the requirements of the Insurance Act. The import of this requirement is demonstrated in priority order for the settlement of debts owed by insurance/*Takaful* operators.[711] Conversely, the Section requires that filing of the winding up petition of the insurer/*Takaful* operator, shall be as if is presented under CAMA.[712] These conflicts of authority do not bode well for the smooth and effective application of insurance and *Takaful* insurance in particular because of its teething problems and the challenges it is facing at this moment. These contradictions erode the confidence and trust of the insured and the would-be insured thereby compounding the deepening penetration

[711] Section 32 (4) Insurance Act, 2003.
[712] Section 32 (1)(a) and (2) of the Insurance Act, 2003.

difficulties the insurance industry is currently grappled with. There must be a harmonisation of legislations as is done in most advanced jurisdictions. Sadly, though the law Reform Commission of Nigeria has been virtually in perpetual slumber only stirring up occasionally to make cosmetic reforms in less critical matters. It is a thing of immense curiosity as to why a topical issue like this has not been a subject of proactive litigation. This ought to have been tested in the law courts long ago. A declaratory pronouncement would have sufficed in resting the issue.

3.13.6 Legal Basis of *Takaful* Application under the Investment and Securities Act, (ISA) 2007

The Investment and Securities Act (ISA) 2007, establishes the Securities and Exchange Commission (SEC) as the apex regulatory authority for capital market operations in Nigeria. The Act provides regulatory framework for capital market, protection of investors, maintaining fair, efficient and transparent market and prevention of systemic risks and other related matters. Although the Insurance Act, as the principal regulatory instrument of insurance business in Nigeria has not made specific mention of Investments and Securities Act (ISA), the role of ISA in the operations of key areas in the financial sector cannot be discountenanced. Section 13 of the Investments and Securities Act empowers the Securities and Exchange Commission, among other things, to do the following:-

(i) Regulate investments and securities business in Nigeria;[713]

(ii) Review, approve and regulate mergers, acquisitions, takeovers and all forms of business combinations and affected transactions of all companies.[714]

[713] Section 13 (a) Investments and Securities Act, 2007.
[714] *Ibid*, Section 13(p)

The fundamental requirement of *Takaful* operation is that it must be *Shari'ah* compliant. Therefore, *Takaful* investment must be tailored to suit its peculiarities and avoid the conventional interest-paying bonds and equities. This presupposes that the assets risk profile is different from that of conventional insurance and in this regard the role of the Securities and Exchange Commission cannot be overemphasised. In pursuance of this responsibility, the Securities and Exchange Commission issued a guideline on non-interest investment portfolio in support of the peculiarities of *Takaful* insurance and Islamic banking in Nigeria.[715]

Another area of significant contribution of the Investments and Securities Act in the operations of *Takaful* is in amalgamation and other businesses arrangement. The financial inclusiveness and integration has become a key factor in financial sector consolidation and re-engineering. This makes the Investments and Securities Act's role in the application of *Takaful* crucial.

3.14 CONCLUSION

This chapter, by implication, is critical to the study. It defined *Takaful* and its attributes and discussed the origins, essence, fundamental features and other cardinal components of the concept all within the confines of general law of insurance and specific regulatory framework. A descriptive analysis of *Takaful* was imperative to lay the foundation for the discussing that ensued on the general and regulatory framework in order to fully appreciate the magnitude of *Takaful* application and its projected impact. *Takaful*, like conventional insurance is based on the principles of insurable interest, indemnity, subrogation and utmost good faith. Insurable interest ensures that the insured's claims succeed if he has sufficient interest in the subject matter on which insurance was sought. Indemnity implies that the claim is only to the extent of the actual financial loss to the

[715] Adamu, A.I., *op cit*, p. 87.

insured. Subrogation entitles the insurer to claim from a third party and utmost good faith is required for the disclosure of all material facts, a condition highly commended by Islam.

Bearing in mind that manipulation and exploitation are abhorred in Islam, *Takaful* participants, like in the case of conventional insurance policyholders, deserve more protection not only from the insurance regulatory bodies but from financial regulatory authorities like the Securities and Exchange Commission and Financial Reporting Council.

The operational Guidelines issued by the National Insurance Commission of Nigeria (NAICOM) recognise the operational models of *Wakalah, Mudharabah* and the Hybrid.[716] However, **Section 2.5** of the Guidelines requires operators opting to implement other than the three mentioned models to seek the Commission's approval. This kind of flexibility is highly recommended as *Takaful* seeks to be permanently engrained in the Nigerian insurance landscape. The Guidelines were made to be the primary regulatory framework with regards to the application of *Takaful* insurance in the midst of conflicting laws and regulations.

Suffice it to say, the chapter dwelt on the fact that the regulatory framework is in place but is not clear and comprehensive enough to facilitate the smooth integration of *Takaful* in the Nigerian insurance industry. The regulatory discrepancies that abound in the Guidelines and the Insurance Act are serious enough to derail the application of *Takaful* in Nigeria. However, this study submits that a statutory legislation harmonizing these regulatory conflicts will go farther in clearing all ambiguities and enhancing regulatory clarity – conditions that are critical in building trust and confidence in the insurance industry. It is also heart-warming to note that all regulatory agencies are

[716] Section 2.2 Operational Guidelines for *Takaful* Insurance Operators, 2013.

taking steps to meet with global demands for new openings and innovations in the quest to bolster the spread and reach of *Takaful* world-wide. It is on this premise that 'non-interest' yielding products and investments are being approved amidst regulatory certainty by the key financial sectors and regulatory agencies in the country.

Top of it all, the rising demand for ethical effusion in business requires effectiveness and efficiency of the internal control structures in the area of corporate governance and risk management practices expected from *Takaful* operators in order to make a difference. Therefore in spite of the leverage and receptive legal framework in the country, it is incumbent on the regulatory authorities to put in place such measures that will ensure regulatory certainty and operational efficiency of *Takaful* operators to help them explore their potential in facilitating the application of this alternative form of insurance.

CHAPTER 4: CONVENTIONAL INSURANCE AND *TAKAFUL* – A COMPARATIVE ANALYSIS OF CONCEPTS AND LEGAL FRAMEWORKS

4.0. INTRODUCTION

Insurance, whether conventional or Islamic, seeks to mitigate loss.[717] Whatever comparisons that are undertaken are meant to portray underlining attributes of commonality in the varied insurance practices that culminate in a unity of outcome at the end of the transactions. The term insurance, in its real sense, is community pooling, to alleviate the burden of the individual, lest it should be ruinous to him. The simplest and most generous conception of insurance is a provision made by a group of persons, each singly in danger of some loss, the incidence of which cannot be foreseen, that when such loss shall occur to any of them it shall be distributed over the whole group.[718]

The aim of any type of insurance is, thus, to make provision against the dangers which beset human life and dealings. It is, in fact, the danger of loss that makes men seriously think of some safety device to avoid it. These devices vary according to the degree of the losses.[719]

The bottom line of conventional insurance is about assumption of risk in exchange for premium. This is in sharp contrast with Islamic insurance which not only mitigates loss but goes farther in spreading mutual support among the policy holders.[720] The Islamic banking system came into being because of the presence of *Riba* in the conventional banking system. In the same light, Muslims are prohibited from transacting in the

[717] Insurance is basically a scheme whereby the insurer, in consideration of a price known as the premium agrees to indemnify or pay a sum of money to the insured upon the happening of a loss or misfortune. Through insurance, a large number of people make payments into pool of funds out of which only those who sustain financial losses or misfortune obtain compensation. Insurance is thus an organized scheme of distributing economic risks of individuals over a large number of persons by way of fixed costs predicted and assessed by insurers. See Raymond S.U. (2014), The Fundamental Principles of Insurance Law: A Critical Analysis of The Nigerian Context (Unpublished LL.M Thesis), University of Maiduguri, p.33.

[718] Muslehuddin, M. (2012), Insurance and Islamic Law, Adam Publishers and Distributors, New Delhi-2 India, p. 3.

[719] *Ibid.*

[720] *Takaful* companies take those aspects of conventional insurance that are not considered Haram in *Shari'ah* law and adjust them so that they can fulfil the conventional role of insurance whilst at the same time being in accordance with Islamic law. See also Rashid, S.K., (1992), ''Insurance and Muslims'', paper presented at IIUM Conference on October 13, 1992, quoting Siddiqi, (1985), *Insurance in an Islamic Economy*. See also Vernados, A.M., (2012), *Islamic Banking & Finance in South East Asia: Its Development and Future*, 3rd Edition, Asia-pacific Business Series – Vol. 6, World Scientific, p. 64.

conventional insurance system since conventional insurance does not conform to the *Shari'ah* principles as it embodies the three elements of *Gharar, Maysir* and *Riba.*[721]

Gharar is the element of ''uncertainty'' that exists in conventional life insurance policies and general insurance policies. The ''uncertainty'' factor is the main feature in the contract or *Mu'qud'alaih,* while in Islam this point must be something which is clear and certain. Uncertainty is present in conventional insurance because the value and timing of compensation cannot be determined and known at the time the contract is made. For example, in conventional insurance, the policyholder agrees to pay a premium to the insurance company, and in return the company agrees to pay compensation in the event of a loss or catastrophe. However, the policyholder is not notified of the method, source or the amount of money that the company would pay him.[722] Under the Islamic concept, all parties to the contract need to know exactly how much they must contribute and how much compensation they will receive. In addition, *Gharar* also exists when injustice or bias arises in the agreement made by both parties. This situation occurs in both life and general policies of the conventional insurance system. For example, life insurance policyholders would lose their premiums if they terminate their participating policies before they are eligible for the cash surrender value. Similarly, for general policyholders, the insurance company would be at an advantage in the event of a policy cancellation within a short term period.[723]

Maysir or gambling is an extension of the ''uncertainty'' concept. For example, a person buys a life insurance policy with the hope that his family or beneficiaries would receive a certain amount of money upon his death. The policy undertaker, however, has knowledge neither of the source of the money that would be paid to his beneficiaries nor of how it would be obtained. The element of *Riba* exists in the conventional insurance

[721] Haron, S. & Azmi Wan, W. N., (2009), *Islamic Finance and Banking System: Philosophies, Principles & Practices,* McGraw-Hill Education p. 424.
[722] *Ibid.*
[723] *Ibid.*

system because the insurance company guarantees to pay fixed returns on the money contributed by the policyholder.[724]

Given the presence of these prohibitive elements in the conventional insurance system, Muslim *Ummah*, particularly those involved in business are truly in need of a system which is *Shari'ah*-compliant to cover them from losses incurred due to unforeseen disasters, catastrophes or tragedies. According to Muslim intellectuals, this concept of mutual help and cooperation is indeed encouraged in Islam.[725]

It needs to be stated clearly that conventional insurance and *Takaful* are the same yet different. Conventional insurance is a very important component in the emergence and continued existence of *Takaful*. Dato' Abdul Hamid Bin Haji Mohamad[726] succinctly puts it this way:

> ''What strikes me is that Islamic banking, insurance and finance are actually Islamized banking, insurance and finance. The products are products of conventional banking, insurance and finance but ''Islamized'' by removing the features prohibited by *Shari'ah* and applying *Shari'ah* principles to achieve the same or similar effects. That Islamic banking, insurance and finance develop that way is a matter of practicality: that it is the only practical way to do so under the existing circumstances.''[727]

He further asserted:

> ''The other point I observe is that the creation of an Islamic product and the determination of the *Shari'ah*-compliance of a product is a much more difficult exercise than determining the legal status under Islamic law as in other matters. It is not just a matter of knowing the relevant verses of the *Al-Qur'an* or *Hadiths*

[724] Haron, S. & Azmi Wan, W. N., *op cit.*
[725] *Ibid.*
[726] Former Chief Justice, Federal Court of Malaysia.
[727] Bakar, M.D. & Ali, E.R.A.E., *op cit,* p. v.

or the ability to read *Fiqh* books in Arabic. What is more difficult is to understand the intricacies of the product before the relevant law (*Shari'ah*) can be applied. Applying the right law to the wrongly-perceived facts will lead to a wrong ruling. Knowledge of the mechanism of the products is of utmost importance. That is where the contribution by the experts in conventional banking, insurance and finance is essential, because, the field is too vast for one person to master.''[728]

Chapters two and three discussed the concepts and application of conventional insurance and *Takaful* respectively under the Nigerian legal system. This chapter brings the two institutions side by side in a contextual and analytical platform to showcase their marked similarities and differences in order to fully grasp the parameters and depth of regulatory conflicts in the enabling instruments that are threatening to derail the successful application of *Takaful* in the Nigerian insurance industry.

4.1 JURISPRUDENTIAL[729] DISTINCTIONS

Under conventional insurance, there is a conflict of opinion as to the definition of law in general. The jurists approach it from different angles of vision. According to the Teleological school, 'law is a product of human reason and is intimately related to the notion of purpose,[730] so the question arises: what is the supreme end of law? Most of the philosophers regard justice as the supreme end and make a distinction between natural and conventional justice which leads to a great controversy and a long metaphysical

[728] Bakar, M.D. & Ali, E.R.A.E., *op cit*, p. v. The above assertion in the quote sums up the basis for understanding the differences and similarities between the two very important systems of insurance. Since the conventional insurance cannot serve the Islamic *ummah*, *Takaful* becomes the alternative but it must be borne in mind that conventional insurance is still very much a part and parcel of *Takaful* and will continue to be so because of the much needed expertise.

[729] Jurisprudence is the science, study and theory of law. It includes principles behind the law that make the law. Scholars of jurisprudence, also known as jurists or legal theorists (including legal philosophers and social theorists of law), hope to obtain a deeper understanding of the nature of law, of legal reasoning, legal systems and of legal institutions. Modern jurisprudence began in the 18th century and was focused on the first principles of the natural law, civil law and the law of nations. General jurisprudence can be divided into categories both by the type of questions scholars seek to answer and by the theories of jurisprudence, or schools of thought, regarding how those questions are best answered. See Wikipedia Encyclopaedia. Under Islamic law, jurisprudence is known as *Usul al Fiqh* or the science of law. It is the study or critical analysis of the origins, sources, and principles upon which Islamic jurisprudence is based.

[730] Paton, G.W., (1951), *Jurisprudence*, Oxford, p. 3.

discussion.[731] Kelsen in his attempt to free law from the metaphysical mist advocates a separation of jurisprudence from natural science which deals with cause and effect. According to him the science of law is the study of the nature of norms set up by the law. Ethics and social philosophy are thus far from law while Pound emphasizes the sociology of law since it is deeply connected with the needs of humanity.[732] Savigny of the Historical school is of the opinion that the source of law is the custom which lies deeply embedded in the minds of men. While the Austinian school holds that the law is the command of the Sovereign and that jurisprudence, having nothing to do with the goodness or badness of law, must be distinguished from legislation which is based upon the principle of utility, that is, the greatest good of the greatest number. This is an accepted principle of the modern world and a view that finds expression in Bentham's utilitarianism which represents 'a reaction against the metaphysical and abstract character of eighteenth century political and legal philosophy.[733]

Bentham's work is a violent attack upon the conception of natural law and the essence of his philosophy is that

> ''Nature has placed man under the empire of pleasure and pain. We owe to them all our ideas; we refer to them all our judgements, and all the determinations of our life. He who pretends to withdraw himself from this subjection knows not what he says. His only object is to seek pleasure and to shun pain. These eternal and irresistible sentiments ought to be the great study of the moralist and the legislator. The principle of utility subjects everything to these two motives.''[734]

[731] Muslehuddin, M., *op cit*, p.57.
[732] *Ibid.*
[733] Friedman, W., (1953), *Legal Theory*, London, p. 211.
[734] Bentham, J., (1931), *The Theory of Legislation*, London, p. 2.

Good and evil are, thus, interpreted in terms of pleasure and pain. This sensualistic evaluation of life does not accord with the ideology of Islam which is a harmonious blend of the temporal with the spiritual and whose aim is to win the approval of God. Human actions are, therefore, classified, under Islamic law, into certain categories so as to indicate what to do and what to avoid in order to pass the reckoning on the Day of Judgement.[735] The *Shari'ah* or Islamic law is an ideal code of behaviour.

> ''To the Muslim, there is indeed an ethical quality in every human action, characterized by *Qubh* (ugliness, unsuitability) on the one hand or *Husn* (beauty, suitability) on the other. But this ethical quality is not such as can be perceived by human reason; instead, man is completely dependent in this matter on divine revelation. Thus all human actions are subsumed, according to a widely accepted classification, under five categories: as commanded, recommended, left legally indifferent, reprehended, or else prohibited by Almighty God. And it is only in regard to the middle category (i.e. those things which are left legally indifferent) that there is in theory any scope for human legislation.''[736]

Islamic law does not recognise the liberty of legislation, for it would be incompatible with the ethical control of human actions and, ultimately, of society.

> ''Law, therefore, does not grow out of, and is not moulded by society as is the case with Western systems. Human thought, unaided, cannot discern the true values and standards of conduct; such knowledge can only be attained through divine revelation, and acts are good or evil exclusively because God has attributed this quality to them. In the Islamic concept, law precedes and moulds

[735] Muslehuddin, M., *op cit*, p. 58.
[736] Anderson, J.N.D., (1959), London, *Islamic Law in the Modern World*, p. 3.

society; to its eternally valid dictates the structure of State and Society must ideally conform.''[737]

In order to secure order in the community Islamic law charges man with dual responsibility. One is in relation to God and the other in relation to society which 'results in a law of duties[738] rather than of rights, of moral obligation binding on the individual, from which no earthly authority can relieve him, and which he disobeys at the peril of his future life.'[739] And, indeed, it is the fear of punishment in the Hereafter which has been successful in providing a deterrent against evil, more effective than punitive legislation of the severest type, provided , of course, that the faith is real and not a mere formality.[740]

'Verily, the Qur'an is a guidance unto those who fear God,[741] and history is replete with biographies of men who led the cleanest, purest and noblest lives mainly due to their fear of God and of reckoning on the day of judgement. O ye who believe! 'Fear God as He should be feared,'[742] 'And fear God that ye may prosper,'[743] is the voice which reverberates in the Qur'an.

The prosperity of society depends not so much upon the rigours of law as upon righteousness inspired by the fear of God i.e. *Taqwa*. And, therefore, *Shari'ah* is a code of moral conduct, *Taqwa* being the standard for the judgement of human actions:

''O mankind! Surely, We have created you male and female, and made you nations and tribes that you may identify each other; surely, the noblest of you in the sight of God is he that fears God most.''[744]

[737] Coulson, N.J., (1964), *A History of Islamic Law*, Edinburgh, p. 85.
[738] Hurgronje, Selected Works (eds. Bousquet and Schacht), (1957), Lieden, p. 52.
[739] Jackson, Foreword to *Law in the Middle East (*eds. Khadduri and Liebesny), *op cit*, p. vii.
[740] Muslehuddin, M. *op cit*, p. 59.
[741] Noble Qur'an Chapter 2 verse 2.
[742] Noble Qur'an Chapter 3 verse 102.
[743] *Ibid* Chapter 3 verse 300.
[744] *Ibid* Chapter 49 verse 13.

The very idea that God 'knows what the soul of man whispereth to him' and that He is 'closer to him than his jugular vein'[745] and that 'three persons speak not privately together, but He is their fourth, nor five, but He their sixth, nor fewer, nor more, but wherever they be He is with them.'[746] And that 'whether he makes known what is in his mind or hide it, He will bring him to account for it,'[747] is enough to strike terror in the heart of a God fearing Muslim and make him abstain from evil thinking, let alone evil doing.[748]

Unlike the secular laws of the modern world which are rationalistic and, therefore, liable to err, which depend for their existence upon the vagaries of public opinion and which alter with every change in society, the divine law of Islam

> ''Finds its chief source in the will of Allaah as revealed to the Prophet Muhammad pbuh. It contemplates one community of the faithful, though they may be of various tribes and in widely separated locations. Religion, not nationalism or geography is the proper cohesive force. The state itself is subordinate to the Qur'an, which leaves little room for additional legislation, none for criticism or dissent. This world is viewed as but the vestibule to another and a better one for the faithful, and the Qur'an lays down rules of behaviour towards others and towards society to assure a safe transition. It is not possible to separate political or juristic theories from the teachings of the Prophet pbuh, which establish rules of conduct concerning religious, domestic, social and political life.''[749]

The peculiarity of Islamic law is that it stands for reforming society by way of persuasion rather than coercion, so it remains content with prescribing such

[745] Noble Qur'an Chapter 50 verse 16.
[746] *Ibid* Chapter 58 verse 7.
[747] *Ibid* Chapter 2 verse 284.
[748] Muslehuddin M., *op cit*, p.60.
[749] Jackson, *op cit*, pp. vi, vii.

punishments only as are most needed to stop crimes of grave nature and create thereby an ordered society. It is for this reason that exemplary punishment was meted out for murder, physical injury, fornication, adultery, theft highway robbery, false accusation or calumny against chastity and drinking of wine, while usury, gambling and the like were left to be dealt with in the Hereafter because of their bearing upon transactions rather than upon the establishment of peace and order.[750] Reform by persuasion and exhortation being the principal aim of Islam, it allows time for penitence and to make amendments in one's life. Islamic law has a twofold object - spiritual benefit and social good. Its policy is, therefore, to encourage obedience by offer of reward, and to discourage disobedience by imposition of penalties. Penalties may be imposed in this world or in the next, or in both, but reward (*Thawab*) is given only in future life.[751]

> ''Law, in classical Islamic theory, is the revealed will of God, a divinely ordained system preceding and not preceded by the Muslim state, controlling and not controlled by Muslim society.[752]

According to Schacht,

> ''the sacred law of Islam is an all-embracing body of religious duties, the totality of Allaah's commands that regulate the life of every Muslim in all its aspects it comprises on an equal footing ordinances regarding worship and ritual, as well as political and (in narrow sense) legal rules.[753]

In Islamic concept, the *Shari'ah* embodies will of God who is the sovereign and source of law and to whom is due the obedience of man: 'His is the sovereign of the Heavens and the Earth and unto Him (all) things are brought back.'[754] 'To God belongeth the

[750] Muslehuddin, M., *op cit*, p. 61.
[751] Rahim, A., (1963), *Muhammadan Jurisprudence*, Beirut, pp. 58-59.
[752] Schacht, J., (1953), *An Introduction to Islamic Law*, Oxford, p. 1.
[753] *Ibid.*
[754] Noble Qur'an, Chapter 57 verse 5.

domain of the Heavens and the Earth and God hath power over all things.'[755] Since He is not only Omnipotent but also Omniscient, human actions are judged according to motive (*Niya*).[756] This being an important feature of the *Shari'ah* the believer is required to observe it with 'sincerity and good faith.'[757]

The *Shari'ah* has the character of a religious obligation to be fulfilled by the believer. 'The law of God remains the law of God even though there is no one to enforce it.[758] The believers, even if they reside outside the territory of Islam, are bound by the law, for the law was revealed to bind the believers as individuals wherever they may be. 'The law takes into consideration primarily the common interests of the community and its ethical standard, the personal interests of the individual believer are protected only in so far as they conform to the common interests if Islam. Not infrequently the interests of the individual were sacrificed for the sake of protecting the common interests of the community.'[759]

The assessment of all human acts and transactions according to its own precepts of good and evil is the central feature of Islamic law which guarantees its unity.[760]

4.2 SIMILARITIES AND DIFFERENCES IN LEGAL SOURCES AND GENERAL PRINCIPLES

The legal sources of conventional insurance have been dealt with comprehensively in the second chapter of this thesis while those of *Takaful* were discussed in the third chapter. Suffice it to say, a side by side comparison is apt at this juncture in order to drive home the point that in as much as the two insurance systems are diametrically different, they do, however, complement each other in many spheres of risk coverage.

[755] Noble Qur'an, Chapter 3 verse 189.
[756] Bukhari, Sahih, Vol. 1, p. 2.
[757] Khadduri, M., (1960), *War and Peace in the Law of Islam*, Baltimore, p. 26.
[758] Fitzgerald, S.G.V. (1955), Nature and Sources of the *Shari'ah*, in *Law in the Middle East*, (eds, Khadduri, M., & Liebesny, H.J., Washington, p. 85.
[759] Khadduri, *op cit*, p. 26.
[760] Schacht, *op cit*, p. 200.

There is enough room for both to exist side by side and become an essential basis of modern life in mitigating the consequences of loss.

The primary legal sources of conventional insurance are the legislations and principles evolved from English Common law and doctrine of equity.[761] The concept of this type of insurance is purely a profit making undertaking that has no regard for ethical considerations. In this regard, Muslim scholars differ in their approach on the permissibility (*Halal*) or prohibition (*Haram*) of conventional insurance.[762] According to Imam Ibn Taimiyyah[763] **'**each contract whose consequences are held in ignorance includes aleatory**,** therefore, the contract of insurance is void *ab initio* in *Shari'ah.* While another view held is that, since there is no injunction (*Nass*) against conventional insurance, it should be allowed (*Mubah*) unless there is clear evidence prohibiting it.[764]

The message of Islam is meant for all mankind and it touches all spheres of life. It is not only restricted to rituals and spiritual obligations, but encompasses politics and economic well-being of mankind. The Qur'an underscored the completeness of Islam as a way of life when Allaah SWT said,

[761] In Nigeria, the received English law as a source of Nigerian law has its origins in common law, doctrines of equity, statutes and subsidiary legislation. It has been introduced into Nigerian law by Nigerian legislation. The history of the reception dates back to 1863 when Ordinance No. 3 of that year introduced English law into the colony of Lagos. The received English law as a source of Nigerian law excludes English law received by being enacted or re-enacted as Nigerian legislation. The latter type of received English law is not a source of Nigerian law. It is the resulting Nigerian legislation that is a source of the law. See the Defamation Act 1952 (15 & 16 Geo. 6 & 1 Eliz. 2, c. 66) whose provisions were re-enacted as part of the Defamation Law (W.R.N. Laws 1959, Cap 33).

[762] Adamu. A. I., *op cit*, p. 106.

[763] Imam Ahmad Ibn Taimiyyah.

[764] Throughout the history of Islamic law, there has been disagreement among the scholars as to whether the conventional insurance contract is prohibited or not. The centre of the disagreement is based mainly on two grounds, that is, whether it pertains to the kind of contracts involving *Gharar*, or if it involves *Riba.* Generally, these views can be categorized into three groups, namely, those who view the contract as prohibited; those who view it as permitted; and those who view that some of the contracts are permitted while others are prohibited. See Ahmad, H., (2000), Evolution of Islamic Banking and Insurance as a System Rooted in Ethics, New York, *Takaful* Forum, April 26. He contends that ''the modernist view tends to be more liberal in the sense that the prohibition of *Gharar* is qualified according to current circumstances and conditions than the traditionalist view, which is a distillation of the classical jurisprudence on the subject''. See also Yassin, N. & Ramly, J., (2011), *Takaful: A Study Guide*, IBFIM, p. 81 where they said ''the scholars who are of the opinion that conventional insurance is permissible said that insurance is a modern contract and there is no injunction (*Nass*) regarding it. If there is no injunction, then it is allowed (*Mubah*). They based their argument on the established legal maxim that ''the original legal position on any matter is permissibility until there is evidence prohibiting it''. This legal maxim is based on the Noble Qur'an where some of the related verses are as follows: ''And He has subjected to you, as from Him, all that is in heavens and on earth: behold, in that are Signs indeed for those who reflect''. (Al- Jathiyah: 13). These scholars further claim that insurance is a contract that brings 'Maslahah' (public interest) to the insured. Without insurance for example, one's next of kin will suffer a huge financial burden after his death. The scholars further said that custom (*Uruf*) establishes the practicality of insurance''.

''This day I have perfected your religion for you, complete My blessings on you and endorse Islam as a way of life for you.''[765]

Takaful insurance derives its origins from the Noble Qur'an and *Sunnah* (sayings and actions) of Prophet Muhammad pbuh. The implication here is that all the principles of *Takaful* insurance must be in conformity with the general requirements of *Shari'ah*. This is in sharp contrast with what obtains with conventional insurance.

The peculiarity of *Takaful* insurance lies in its two-tier structure. The operator is remunerated for services rendered ranging from the running of the operations of the insurer to the management of the policyholders' funds. In principle, the *Takaful* operator is not exposed to any underwriting risks.[766] In contrast, under conventional insurance, premiums paid by the policyholders accumulate in funds from which benefits and claims would be settled. The difference between the premium and claims paid constitutes profit which goes to the shareholders (operators) fund under *Takaful.*[767]

With regards to the principles of contract, both *Takaful* and conventional insurance are subjected to fundamental principles of insurance contract. These include utmost good faith, insurable interest, indemnity, subrogation, contribution and proximate clause. These are special legal principles that are embodied in all contracts of insurance details of which have been discussed in previous chapters of this thesis. By way of recap, though, under *Takaful*, the requirement of insurable interest presupposes the legal right to provide cover arising from legitimate financial interest which the participant has in the subject matter of *Takaful.* In contrast, the insurable interest under conventional

[765] Noble Qur'an, Chapter 5 verse 3. In Islam, whatever fate befalls an individual is according to the established will of Allaah and a true Muslim must conform to the dictates of *Shari'ah*. The primary source of the *Shari'ah* is the Noble Qur'an which exhorts all Muslims to accept all misfortune as predestined but at the same time one is allowed to endure patiently and to make contingencies where necessary. Muslims are encouraged to take necessary steps to minimize losses from unfortunate circumstances. A good example is when the Prophet pbuh told a Bedouin Arab to tie his camel before entrusting it to the care of Allaah.

[766] Adamu, A. I., *op cit* p. 107.
[767] *Ibid.*

insurance is the legal right of the insured to benefit from preservation of the subject matter or be jeopardized by its destruction or loss.[768]

On the principle of utmost good faith, both the *Takaful* operator and participants are to sufficiently disclose material facts and any other circumstance that could invalidate the contract. Allaah SWT enjoins the parties to the transaction in the following verse, thus:

> ''O' you who believe! Eat not up your property among yourselves in vanities. But let there be amongst you traffic and trade by mutual good will; nor kill or destroy yourselves; for verily Allaah hath been to you the Most Merciful.''[769]

In the same way, the principle of utmost good faith is a major requirement for the validity of conventional insurance contract under the Insurance Act.[770] Utmost good faith is a Common law principle which is applicable in Nigeria. However, what remains imperative here and is worth noting, is that the Nigerian insurance Act, 2003, is not only regulatory in nature but has gone ahead to incorporate quite a number of these insurance principles in its provisions. The import of this is that these insurance principles are of cardinal importance which requires strict compliance otherwise the contract becomes null and void. It, however, appears that the requirement for disclosure of material facts is absolute and binding under *Takaful* than under conventional insurance because the provisions of the Insurance Act, 2003 have swayed so much in protecting the insured[771] by placing the onus on the insurer to elicit material facts from the insured through purposeful questioning.

It is submitted that a point of departure between the two insurance systems is that while the principle of *Tabarru'* (donation) is a fundamental element of *Takaful*, the concept

[768] Adamu, A. I., *op cit* p. 107.
[769] Noble Qur'an, Chapter 4 verse 29
[770] Section 54 (1) Insurance Act 2003.
[771] Section 54 (1) & (3) Insurance Act 2003. The Act says ''where an insurer requires an insured to complete a proposal form or other application form for insurance, the form shall be drawn up in such a manner as to elicit such information as the insurer considers material in accepting the application for insurance of the risk and any information not specifically requested shall be deemed not to be material''. It further provides that '' a disclosure or representation made by the insured to the insurance agent shall be deemed to be a disclosure or representation to the insurer provided the agent is acting within his authority''.

has no bearing in conventional insurance. The principle of *Tabarru'* represents an agreement for shared responsibility and shared guarantee that the contribution collected is to be used for the purpose of assisting fellow participants in accordance with *Shari'ah* principles. In contrast, conventional insurance is an agreement between the insurer and the insured which is independent from any relationship with other insured persons, therefore, the element of mutual support and brotherhood which form the basis of *Takaful* are lacking.

4.2.1 Common Attributes in both Insurance Systems as Risk Hedgers[772]

Universally, the essence of insurance is to transfer of hedge risks. The idea of insurance as a medium for risk transfer is to provide protection to individuals or businesses against specified contingencies. Therefore, the bottom line of both *Takaful* and conventional insurance as a means of finding succour to those afflicted by misfortune is the same in both systems of insurance. The essence of insurance is succinctly expressed by Professor Irukwu as follows:-

> ''We live in a world dominated by numerous risks and uncertainties, which we encounter in practically all aspects of our lives. Unfortunately, no amount of human ingenuity has been able to eliminate these risks. Since these risks cannot be eliminated, all we can do as rational and intelligent beings is to device effective and efficient methods of managing and controlling these risks.''[773]

The learned author further asserted that:-

[772] ''Hedging is analogous to taking out an insurance policy. If you own a home in a flood-prone area, you will want to protect that asset from the risk of flooding – to hedge it, in other words – by taking out flood insurance. There is a risk-reward tradeoff inherent in hedging; while it reduces potential risk, it also chips away at potential gains. Put simply, hedging isn't free. In the case of the flood insurance policy, the monthly payments add up, and if the flood never comes, the policyholder receives no payout. Still most people would choose to take that predictable, circumscribed loss rather than suddenly lose the roof over their head. A perfect hedge is one that eliminates all risk in a position or portfolio. In other words, the hedge is 100% inversely correlated to the vulnerable asset. This is more an ideal than a reality on the ground and even the hypothetical perfect hedge is not without cost''. See www.investopedia.com/terms/h/hedge.asp.

[773] Irukwu, J.O., *op cit*, p. 1.

> ''Insurance is universally recognised as a major response to risk problems. As a risk management tool, or to be more specific, as a risk distribution tool, it is the most ingenious creation of human mind. It managed to survive for well over two thousand years because it rests on solid and durable principles and laws that are universally recognised and enforced by the courts of most civilized countries.''[774]

The major point of departure between the two types of insurance is that *Takaful* is an ethics-based system founded on brotherhood, mutual support and voluntary contribution of money to support a common goal of providing mutual financial aid to members in distress. Whereas the underlining interest of conventional insurance is to enhance freedom of trade from the point of view of capitalism stripped of ethical considerations.

Furthermore, under *Takaful,* the participants own the *Takaful* funds and it is managed by the operator. The participants give up individual rights to gain collective rights over contribution and benefits. Whereas, with conventional insurance, it is solely a buying and selling contract, in which policies are sold and the policyholders are the buyers. The policyholders pay premium to the insurance company but with *Takaful* it is the opposite because the participants make contributions to the scheme.[775]

The issue of interest or *Riba, Gharar* or uncertainty and gambling or *Maysir* are so central to the survival of conventional insurance, whereas, it is the converse under *Takaful*. This has been the main dichotomy between conventional insurance and *Takaful.*

For general *Takaful,* the account is known as *Tabarru'* (PSA), which means donation. Under life *Takaful*, there are two accounts namely, PA or participant's account, which is

[774] Irukwu, J.O., *op cit*, p. 1.
[775] Ismail. E., *op cit*, p. 31. See also Yassin N. & Ramly, J., (2011), *Takaful: A Study Guide*, IBFIM, p. 121, ''in conventional insurance, the insured pays premium for the policy whereas in *Takaful* the participant contributes fund consisting of *Tabarru'* and investment fund''. Again, '' premium paid by policyholder is considered as income to the insurance company whereas under *Takaful* there is full isolation between the *Takaful* fund and shareholders' funds''.

treated in line with the principles of *Mudharabah*; while the other account is PSA, which is treated on the basis of *Tabarru'*, *Wakalah* or *Waqf*. As for conventional insurance, for general insurance, the paid premium is credited into the account, which is generally known as General Insurance Account. Similarly, in life assurance policy, the collected premiums are credited into the account known as Life Insurance Account or Fund.[776]

4.2.2 The Essential Elements of Contract in both Systems

Basically, the significant features of conventional insurance are also applicable to *Takaful* in the sense that the essential elements of a valid contract must all be present for that contract to be enforceable. In addition, there are some peculiar attributes of insurance contract that must be complied with in order to enjoy the protection of law.[777]

The essential elements of a valid contract under the English Common law include: offer, acceptance, legality, consideration, intention to create legal relations, capacity, object, time, etc. These elements are so critical to the existence of a valid contract that any omission renders the contract a nullity. It is virtually the same thing under Islamic contracts. Islamic finance (which includes *Takaful*) – like any commercial transaction – is built on contracts that express the mutual intention of the parties and establishes their rights and obligations. The term for Islamic contract is *Aqad* literally meaning a 'tie or a knot binding two parties together.'[778] The crucial factor in Islamic finance is *Shari'ah*, i.e. the contracts have to follow the basic tenets and prohibitions of the *Shari'ah* in order to be valid. An Islamic contract, just as stated in conventional contract, must fulfil the following requirements to be valid.

[776] Ismail, E., *op cit*, p. 31.
[777] These peculiar fundamental elements include: insurable interest, utmost good faith, subrogation, indemnity, proximate cause, etc.
[778] Frenz, T. & Soualhi, Y., *op cit*, p. 61.

(a) There must be an offer (*Ijab*) by the offeror and an acceptance (*Qabul*) by the offeree: The acceptance refers to the original offer, but without qualification, as that would make it a counter offer. It can be done verbally, in writing or by conduct. The contract should be accepted in the same session. For Islamic finance contracts, legal documentation of contracts is required to reflect the nature of the asset, the price, the mode of delivery, signature of both parties, etc.[779]

(b) The parties to a contract can be individuals, groups or legal entities, if they have the legal capacity to enter into the contract. This would for instance exclude minors or a person of unsound mind.[780]

(c) The object of the contract refers to the subject matter, for example an asset, a service, money, capital, liability, rights or usufruct. The subject matter of the contract must be lawful under the *Shari'ah* and excludes for instance haram goods such as alcohol or pork or unlawful activities like gambling or conventional insurance.[781]

By extension, this means the pillars of a *Takaful* contract are made up of the following elements:

(d) The parties to the *Takaful* contract: *Takaful* operator and participant

(e) Offer and acceptance: *Takaful* policy

(f) Subject matter: Risk coverage.

Basically, the forms of contract in both conventional insurance and *Takaful* are the same except for a few details that border on the subject matter of the contract. Where an Islamic contract fulfils the requirements listed above it is considered as valid (*Sahih*) or otherwise as void or invalid (*Batil*), meaning that it has no legal effect. An example of a

[779] Tobias, F. & Soualhi, Y., (2010), *Takaful and ReTakaful: Advanced Principles & Practices,* IBFIM, p. 87.
[780] *Ibid.*
[781] *Ibid.*

void or invalid contract would be a loan (*Qard*) contract where interest is charged on late payment.[782]

In spite of the striking similarities in the legal requirements to be satisfied before a valid contract of insurance can be said to be in existence, the two forms of insurance are fundamentally different and distinctive in their approach to these essential elements fulfilment. For instance, *Takaful* participants contribute to *Takaful* funds on the basis of reciprocal or mutual donation (*Tabarru'*) instead of commercial or sale of the insurance cover. Therefore, *Takaful* must have some other essential features which entail unilateral or charitable contract based on the principle that participants guarantee each other.

Furthermore, while the legality of conventional insurance depends strictly on conforming to the essential elements and fundamental principles of insurance, the *Takaful* insurer must strictly adhere and comply with *Shari'ah* principles in all their ramifications. As an ethics-based insurance platform, the relationship between the participants and operators is based on *Ta'awun* principle and that surplus underwriting shall be distributed among participants who have not suffered loss, etc. In contrast, the conventional insurance platform is a purely profit-oriented venture whereby the insured is not entitled to anything in the event that he has no admissible claim during the term of the policy.[783]

4.2.3 *Shari'ah* Compliant Requirement

The primary objective of a conventional insurer is the maximization of profit to boost shareholders holdings. In contrast, the concept of *Takaful* is based on *Ta'awun'*

[782] Frenz, T. & Soualhi, Y., *op cit* p. 62. In spite of the striking similarities in the legal requirements to be satisfied before a valid contract of insurance can be said to be in existence, the two forms of insurance are fundamentally different and distinctive in their approach to these essential elements fulfilment. For instance, *Takaful* participants contribute to *Takaful* funds on the basis of reciprocal or mutual donation (*Tabarru'*) instead of commercial or sale of the insurance cover. Therefore, *Takaful* must have some other essential features which entail unilateral or charitable contract based on the principle that participants guarantee each other

[783] Adamu, A.I., *op cit*, p. 111.

(brotherhood), therefore, any element in its operations must be subjected to strict *Shari'ah* compliance test. Islam has a clear set of rules or general principles governing the terms and conditions of doing business. So long as the boundaries set are not violated, the business should be permissible and valid. The original legal position of any matter is permissible until there is evidence prohibiting it.[784] The Prophet pbuh clearly stated in a *Hadith* that:

> ''….Muslims are bound by contracts, except contracts which prohibit what is permitted or permit the prohibited.''[785]

If, however, the objectionable elements are only incidental as in the case of insurance, Islam has provided the means to remove such elements. On the other hand if the contravention goes to the basic principles of Islam, then it should be totally rejected. However, it should be noted that there is no explicit injunction against conventional insurance either in the Al-Qur'an (first source of *Shari'ah*) or *Sunnah* or Hadith (prophetic traditions and the second source of *Shari'ah*) which some Muslim scholars viewed as permissible, subject to certain modifications.[786]

> ''The earliest opinion on the non-compliance of marine insurance contract to the *Shari'ah* was noted in the 19th century from a well-known Hanafi jurist named Syed Ibn Abideen. This view was echoed a century later in Malaysia, whereby Muslim scholars debated on the same issue in the 1970s. The National Fatwa Committee of the Malaysian Islamic Affairs Council made similar conclusion regarding the non-compliance of conventional insurance under the *Shari'ah*. In other events, the First International Conference on Islamic Economics held in Makkah, in 1976, and the *Fiqh* Academy of the Organization of Islamic

[784] Ismail, A., (2002), *Islamic Risk, Asset Management and Wealth Distribution*, Lecture Series for Persatuan Remisier Bumiputra, Malaysia.
[785] Directory of Islamic Insurance, 1999.
[786] Rahman, Z.A., & Redzuan, H., *op cit*, p. 20.

> Conference (OIC) meeting in 1985 also made the same resolution; both life and non-life insurance as practiced conventionally do not comply to the Islamic principles as laid down by the *Shari'ah.''*[787]

The *Fatwa* (legal opinion) issued by Muslim scholars argued that three elements are present in the current form of conventional insurance that are not permissible. These elements are *Gharar* (uncertainty), *Maysir* (gambling) and *Riba* (usury).[788] They are prohibited because their presence could lead to exploitation and injustice. In the Noble Qur'an, Allaah SWT states:

> ''…. Do not devour one another's property by unlawful ways; instead do business amongst you by mutual consent.''[789]

It should be noted that any social device to help individuals in financial hardship is not contradictory to Islamic tenets. *Shari'ah* is concerned with human welfare, justice and equity. *Maslahah* or public interest has always been the utmost priority in Islam. An arrangement similar to conventional insurance, which is *Takaful*, should be encouraged in the society because it promotes cooperation, shared responsibility, mutual protection, solidarity and self-sustaining virtues. Muslim jurists have acknowledged that the benefits of insurance far outweigh the defects, therefore, clearly exceeds its disadvantages and unfairness. An insurance system that addresses the problems of *Gharar*, *Maysir* and *Riba*, as embodied in *Takaful*, is much desired by the Muslim community.[790]

The undesirability of conventional insurance, according to the Muslim, is firmly entrenched in the conventional perspective of wealth accumulation. While Islam encouraged ownership of assets, it is noted, similarly in conventional way of

[787] Yusof, M.F., (1996), *Takaful Sistem Insurans Islam*, Kuala Lumpur, Utusan Publications and Distributors. Also see Rashid, S.K., (2005), A Religio-Legal Experiment in Malaysia, *Religion and Law Review*, 2(1): 16-40.
[788] Khorshid, A., (2004), *Islamic Insurance: A Modern Approach to Islamic Banking*, Routledge Curzon, London.
[789] Noble Qur'an, Chapter 4 verse 29.
[790] Rahman, Z.A., & Redzuan, H., *op cit*, p. 21.

accumulating wealth, or in the field of economics, where pure capitalism is advocated, it provided that sources of assets rightfully belong to the individual and the private sector. Acquiring wealth and freedom to enter into legal contract allows individuals or a business organization to accumulate, control, utilize and dispose the economic source by whichever means deemed fit.[791] In the practice of this system, also known as *laissez-faire*, human beings are prone towards greed and selfishness for the sake of maximizing income, and accumulate as much wealth as possible without taking into account the interest or welfare of others. On the other extreme end is the economic system practiced by the communists, where assets or wealth are owned by the state and decision on how income should be generated from the economic source is made by the government of the day. Individuals are not given the power or rights to own assets, although there has been a remarkable in recent times where socialist economies have allowed for individual ownership of assets within certain limits and conditions. It could be seen that from both ideologies, they are equally flawed and extreme in nature and go against the requirements set by *Shari'ah*, which provides for the rights of the individual, private institution and the responsibility of the state to determine that wealth accumulation is carried out in a just and ideal manner. On reflection, the practice to generate income and economic development of most countries around the world falls between these two extreme ideologies. Islamic method differs from both.[792]

4.2.4 Business Models and Operational Structures

Conventional insurance is based on an exchange of premium payments now for claimable future indemnities. Such an exchange would not be valid under *Shari'ah* due to the presence of uncertainty (*Gharar*) in the value of the future indemnities. To circumvent this obstacle of uncertainty, *Takaful* introduced the concept of donation

[791] McConnell, C,R., (1984), *Economics: Principles, Problems and Policies*, McGraw-Hill Book Company, US, pp. 26-29.
[792] Rahman, Z.A., & Redzuan, H., *op cit*, p. 93.

(*Tabarru'*), which is a voluntary individual contribution to a risk pool out of which indemnities are paid out to other contributors.[793]

It is worth mentioning that *Takaful* is virtually the same thing as conventional insurance in its pristine form. There is a great disparity between conventional insurance in its earliest forms and conventional insurance as it developed in the course of time. In its inception it is a mutual institution to meet the actual loss when it occurs but in its development it is a device to cover the chances of loss, i.e. risks which are abstract and indeterminate.[794] Its history may be traced back to remote antiquity thousands of years before Christ. Mutual assistance was its primary objective. This spirit of mutual help, based as it is upon the golden principle of **'**bear ye one another's burdens**'**, has always been looked upon as a virtue in itself and, therefore, acceptable to Islam.[795] But with the passage of time and as the capitalist adventure gained ground there evolved a contract of conventional insurance, personal in character, whereby, instead of losses, risks or chances of loss are insured. The insurer agrees to undertake risk in consideration of a sum called the premium. This is but speculation and seems to have originated in the marine loans of the type known in ancient Greece as early as the fourth century before the Christian era.[796] Thus, the modern contract of conventional insurance stripped of the virtue of mutuality, stands, today, as an offshoot of capitalist enterprise.[797]

Furthermore, as a science, the modern contract of insurance is based upon the principles of probability and the law of large numbers whereby risks are converted into a fixed cost. This is done by combining large numbers of risks and applying the principles of probability to the mass of data relating to them.[798] Exact mathematical measurement being impossible, the risk is determined by the chance of loss as estimated from past

[793] Adamu, A.I., *op cit*, p. 113.
[794] Muslehuddin, M., *op cit*, p. x.
[795] *Ibid.*
[796] *Ibid.*
[797] *Ibid.*
[798] Allen, F.T., (1936), *General Principles of Insurance*, New York, p. 10.

experience. This yields no accurate results and ends in uncertainty of compensation (subject-matter).[799] These and other reasons stated earlier render the modern contract of conventional insurance invalid under Islamic Law which is permeated by religious and ethical considerations: each institution, transaction, or obligation is measured by the standards of religious and moral rules, such as the prohibition of interest, the prohibition of uncertainty, the concern for equality of the two parties, the concern for the just mean or average (*Mithl*).[800]

Insurance, in its real sense, is community pooling, to alleviate the burden of the individual, lest it should be ruinous to him:

> ''The simplest and most general conception of insurance is a provision made by a group of persons, each singly in danger of some loss, the incidence of which cannot be foreseen, that when such loss shall occur to any of them it shall be distributed over the whole group.''[801]

The aim of all insurance is, thus, to make provision against the dangers which beset human life and dealings.[802] It is, in fact, the danger of loss which makes men seriously think of some safety devices to avoid it. These devices vary according to the degree of the losses. If the loss is foreseeable it may be avoided by adopting preventive measures, and in case it is small the individual may assume it himself, but the difficulty arises when it is unforeseen and large as it can neither be prevented nor assumed. Hence **'**loss prevention**'** or **'**loss assumption' has a very limited application[803] and cannot cope with the losses that are heavy, ruinous and unforeseen. On such occasions the individual is completely destroyed if the assistance of the community or group is not forthcoming. For the community as a whole such a loss will be negligible but the individual will be

[799] Muslehuddin, M., *op cit*, p. xi.
[800] *Ibid.*
[801] *Ibid*, p. 3.
[802] Morgan, T.W., (Ed.), (1933), *Porter's Laws of Insurance,* London, p. 1.
[803] Allen, F.T., *op cit*, p. 3.

totally ruined if exposed to it singly.[804] This is the theoretical background of conventional insurance which has been devised to meet a loss unknown in time and in amount.[805]

It is evidently clear that whatever business model of insurance that is in existence today largely depends on the theoretical composition of that particular system that has characterized its evolution through the years. Conventional insurance has undergone so much transformation since its inception while *Takaful* has had the privilege of remaining consistent because of the nature of the Qur'an and *Sunnah* that have been so preserved.

The basic structure of *Takaful* insurance is determined by the *Takaful* operator from the choices available within a given jurisdiction which demonstrates the flexibility of the system as long as the contract is *Shari'ah* compliant. Guidelines on *Takaful* insurance in Nigeria[806] recognise three models of *Takaful* operation which are as follows:-

1. *Takaful* Insurance based on *Mudharabah* (profit sharing) contract; in this model, the *Takaful* operator assumes the role of a *Mudharib* (entrepreneurial partner) and the participants as the owners of the capital. The key aspect of this model under the Guidelines is that the operator manages the investment and underwriting activities. The *Takaful* insurer is entitled to a percentage share of investment gains and operating surplus while the financial loss will be borne by the *Takaful* participants. Details of this model are discussed in the previous chapter of this study.

2. *Takaful* insurance based on *Wakalah* (agency). In this model, the operator assumes the role of a *Wakil* (agent) acting on behalf of the participants in return for a fee. The key elements of this model under the Guidelines are that the operator manages

[804] Muslehuddin, M., *op cit*, p. 3.
[805] Barou, H., (1936), *Cooperative Insurance*, London, p. 11.
[806] Section 2 (2) of the Guidelines on *Takaful* Insurance – Operating Models.

investment and underwriting activities of the venture. He is remunerated by being paid agency fees as set out in the agreement. He is also entitled to a performance fee.

3. *Takaful* insurance based on hybrid *Wakalah-Mudharabah* contract. In this model, (*Wakalah*) agency contract is placed between the operator and participants for the management of underwriting activities and a (*Mudharabah*) profit sharing contract is entered between them for investment activities.[807]

Details of all the models discussed above are found in the previous chapter of this study with an analysis for the preferred model. Beside the recognised models, The Guidelines also categorized *Takaful* into two classes of Family *Takaful* and General *Takaful*[808]. The Family *Takaful* is described as typically a long term arrangement between the *Takaful* operator and participants which provides the policyholders with financial relief in case of bereavement, critical illness or disability. General *Takaful* on the other hand is typically a short term agreement between the operator and participants providing financial contribution for special losses such as theft or damage but excluding cover under Family *Takaful*.

In contrast, the Insurance Act[809] recognises three models of conventional insurance in Nigeria.[810] This can be classified as;

1. Insurer and insurance business regulated by the Act

2. Friendly society and

3. Other forms of insurers that fall within the description given in Section 1 (a) & (b) of the Act.

[807] Adamu, A.I., *op cit*, p. 114.
[808] Section 2 (1) Guidelines on *Takaful* 2013.
[809] Insurance Act 2003.
[810] *Ibid*, Section 1.

However, the Act created two classes of insurance namely Life insurance business and General insurance business with further sub classes to reflect the distinct nature of this line of business. The Act also provided for a combination of Life and General business classified as Composite insurer.[811]

A distinguishing feature in relation to the models found in both systems of insurance under the Act and the Guidelines is found in the permissibility of carrying out distinct classes of insurance. While a life insurer can composite certificate to underwrite General business under the Insurance Act, a General *Takaful* insurer is not allowed under the Guidelines to underwrite Family *Takaful* business. Further distinction is that the enabling legal framework for *Takaful* has provided options to the operators in respect of multiple models e.g. *Wakalah, Mudharabah* and Hybrid *Wakalah-Mudharabah* models. However, in contrast, the only option available to the conventional insurer under the Insurance Act is the only model that is regulated by the Act. This therefore, suggests that both *Takaful* operators and participants are given more options and more room than their counterparts under conventional insurance.

Another area of distinction is that irrespective of the business model, *Takaful* business differs from conventional insurance in their operational structure. This is clearly seen in the case of contractual exclusion of the risk transfer from the participant to the *Takaful* operator. While conventional insurance policyholders buy a risk cover and transfer the premium as consideration for the contract, the *Takaful* participant remains the owner of

[811] Section 2(1) Insurance Act 2003. See also Section 2(6) of the Act which provides that ''If the National Insurance Commission (in this Act referred to as the ''Commission'') is satisfied that an insurer –
(a) has conducted his business in accordance with sound insurance principles; and
(b) has complied with the provisions of this Act, it shall in writing permit the insurer to conduct any class of insurance business in addition to those covered by his certificate of registration''.
Compare the above position with that of the new Islamic Financial Services Act of Malaysia, 2013 which introduced separate licenses for Family *Takaful* and General *Takaful* business. While the 1984 *Takaful* Act allowed *Takaful* Operators to carry on both businesses under the same company, a *Takaful* Operator now needs to have two separate companies to carry out the Family *Takaful* business and General *Takaful* business. See Section 16 (1) Islamic Financial Services Act, 2013 which provides that a licensed *Takaful* Operator, other than a licensed professional *Takaful* Operator, shall not carry out both, Family *Takaful* business and General *Takaful* business. The rationale for the separation is not stated in the Act but it probably has to do with different risks and appetite that requires separate focus and treatment. The combination of both businesses under one umbrella may lead to manipulation and injustice to either of the business models. See Abd Hamid, M.H. & Hassan R., (2014), Islamic Financial Services Act 2013: A Preliminary Note On Its Impact On *Takaful* Industry, 2. *Malaysian Law Journal*, p. lxxv.
See also Adamu, A.I., *op cit*, p. 115.

the Participants' *Takaful* fund. In *Takaful,* it is not the insurance company but the participants themselves who provide the mutual risk cover out of the *Takaful* fund. The *Takaful* operator only manages the underwriting and investment on behalf of the participants. The underwriting surplus and investment profits belong to the *Takaful* participants. They also bear deficits and losses except for cases of misconduct and negligence on the part of the *Takaful* operator.[812]

In practice, however, *Takaful* operators are bound to provide interest free loans (*Qard Hasan*) if the underwriting leads to a deficit in the Participants' *Takaful* Fund. The loan is recovered from future underwriting surpluses which therefore demand for sufficient shareholders' funds. This is similar to the case of conventional insurance where the insurer is required by law to at all times maintain solvency margin which shall not be less than 15 per cent of the gross premium income or a minimum paid up capital, whichever is greater.[813]

It should be noted also that there are two features that distinguish *Takaful* companies from conventional and other Islamic companies alike; a *Shari'ah* board and the separation of the two funds, the participants' and shareholders' funds. The latter feature is a consequence of *Shari'ah* requirements and is meant to both express and guarantee that two main functions take place within the community of participants only: the carrying of the risks (risk sharing) and the transformation of the risk with minimisation of relative volatility costs (pooling).[814]

What is further present in *Takaful* (and Islam in general) are moral values and ethics – business is meant to be conducted openly in accordance with utmost good faith, honesty, full disclosure, truthfulness and fairness in all dealings. The same is certainly

[812] Archer, S. & Abdel Karim, R., (2009), Conceptual, Legal and Institutional Issues Confronting *Takaful*. *Takaful* Islamic Insurance, p. 11.
[813] Section 24 (2) Insurance Act 2003.
[814] Frenz, T. & Soualhi, Y., *op cit*, p. 149.

expected of conventional insurance operations, but the aim of *Takaful* is to operate on more ethical principles.[815]

4.2.5 Investment Portfolio

As earlier stated in the study, conventional insurance is not strictly subject to ethical considerations as found in *Takaful.* Investment issues for the insurer under the Insurance Act are regulated under Section 25 of the law.[816] The section requires the insurer to invest and hold invested in Nigeria assets equivalent to not less than the amount of policyholders' fund in such accounts of the insurer. The section also provides restrictions on the type of investment in properties and securities allowed.[817] The law also restricts investment of the life insurer in real property to 35 per cent while a general insurance to 25 per cent of its assets. Investments are carried out in line with capitalist ideology.

Conversely, the objective of Islamic economy is to create an exploitation-free society, promote welfare of the people which encompasses safeguarding their faith, lives and property. By safeguarding these elements, *Takaful* serves public interest and occupies a strategic position in the global economic system. The contribution of *Takaful* to the global economy is a major indicator of the potentiality of the industry and points to the

[815] Frenz, T. & Soualhi, Y., *op cit,* p. 124. ''Whatever the legal structure of a *Takaful* operation might be, the most important aspect is full *Shari'ah* compliance at all times:(i) This requires a *Shari'ah* Advisory Board (SAB) of between three to five *Shari'ah* scholars. If a *Takaful* operator has regional ambitions, it is advisable for the members to come from the target markets to underline credibility. Scholars should ideally already have conventional insurance/*Takaful* experience to avoid possible miscommunication in discussions with business people. This is of a particular importance because the SAB members have to certify the *Shari'ah* compliance.(ii) Although the relationship between the SAB and the management is usually one of deep trust and integrity, it does not obviate the requirement to lay down clear and written guidelines for the scope and responsibilities of the SAB. They would for instance define how often the board should meet or provide for the right of an unannounced on-site inspection/audit.(iii) Compliance covers all aspects of the operation – the *Takaful* model, products, surplus sharing and fee structures, Islamic investments, contract wording, marketing material etc. Most of these provisions are also commonly found with conventional insurance except those having to do with Islamic prohibitions.

[816] The Section provides that '' An insurer shall at all times in respect of the insurance transacted by it in Nigeria, invest and hold invested in Nigeria assets equivalent to not less than the amount of policyholders' funds in such insurance business as shown in the balance sheet and the revenue accounts of the insurer.

[817] Section 25 (2) Insurance Act 2003.

socio-economic advantages of ethics-based systems that guarantee equity, justice and fair play.[818]

An exploitation-free society is in dire need of capital formation. *Takaful* facilitates capital formation through individual households by encouraging personal savings. These collective savings when invested trigger further utilization of the resources and greater employment generation opportunities.[819]

Another fundamental principle of Islamic economic system is the need for equitable distribution of wealth. Islam encourages people to be selfless helpers of one another which *Takaful* upholds by way of mutual cooperation and joint guarantee.[820]

The basic requirement of investment in *Takaful* is its compliance with *Shari'ah* principles. This presupposes that the investment must be free from any form of *Riba* (interest), gambling (*Maysir*) or uncertainty (*Gharar*). In line with this requirement, the Guidelines require the *Takaful* operator to establish investment policies for the Participants' Risk Fund (PRF) and Participants' Investment Fund (PIF).[821] The requisite investment policies shall include:

[818] Fortunately, in the past decades, several interesting lines of research have begun to map the specific contribution of Islamic insurance (*Takaful*) to the economic growth process as well as to the wellbeing of the poor. See Billah, M.M. (2001), Principles and Practices of *Takaful* and Insurance Compared, Malaysia, GECD Printing, Sdn Bhd. See also Iqbal, M. & Molyneux, (2005), Thirty Years of Islamic Banking History. Performance and Prospects, Palgrave. See Abdur Rahman Z. et al, (2008), Family *Takaful*: Its Role in Social Economic Development and as a Savings and Investment Instrument in Malaysia – An Extension, *Shari'ah Journal*, 16(1), pp. 89-105. The evidence suggests that Islamic insurance contributes materially to economic growth by improving the investment climate and promoting a more efficient mix of activities than would be undertaken in the absence of risk management instruments. (For example see Fisher, O. & Taylor, D.Y. (2000), Prospects for Evolution of *Takaful* in the 21st Century, available at www.takaful.com.sa/m4sub3.asp.openaccess.htm. See also Brainard, L., (2008), What is the Role of Insurance in Economic Development?, Zurich Government and Industry Affairs Thought Leadership Series, available at www.zurich.com.openaccess.htm. See also Redzuan, H, et al (2009), Economic Determinants of Family *Takaful* Consumption: Evidence from Malaysia, *International Review of Business Research Papers*, 5(5), pp. 193-211. This contribution is magnified by the complementary development of the Islamic banking and other financial systems. And like the rest of the world market, Nigeria has recently introduced the non-interest banking to engender financial inclusion of the unbanked majority in the polity. JAIZ Bank was granted license in September, 2015. See Emejo, J.S., (2011), Only Court of Law Can Stop Islamic Banking, *ThisDay* Newspaper (online), 4th July.

[819] Adamu, A.I., *op cit*, p 118.

[820] *Ibid.*

[821] See Section 4(2)(a) & (b) of Takaful Operational Guidelines, 2013.

(a) The *Takaful* operator must seek to manage funds aligned with *Shari'ah* compliant methodology as practiced internationally and approved by its Advisory Committee of Experts (ACE).[822]

(b) The investment policies must be approved by the ACE and the Commission and the operator shall ensure utmost diligence when selecting where the funds are to be invested in order to maintain the strict compliance with the *Shari'ah* standard.[823]

In contrast, investment under conventional insurance is devoid of any ethical standards. It is driven by pure profit maximization considerations. The Insurance Act regulates investment issues under conventional insurance but these are a far cry from what obtains under *Takaful* Guidelines in Nigeria.

On the international scene, the success of the *Takaful* industry is directly linked to the asset management capabilities of the Islamic finance industry. Few Muslim buyers would accept lower returns for the sake of religion. In reality, Muslim individuals purchase insurance for children's education, retirement, unexpected medical expenses and financial protection against the death of the breadwinner. This indicates the importance of investment performance in purchasing insurance cover.[824]

The funds of the shareholders and the policyholders have to be invested in *Shari'ah*-compliant and profitable manner. The more successful the asset management proposition is, the stronger the *Takaful* proposition will be.[825]

[822] Section 4(4)(a) of *Takaful* Operational Guidelines, 2013. Where income is generated from non-*Shari'ah* compliant or partial investments, a process of purification of the income must take place by giving the percentage of the income generated to charitable institutions. This approach must be ratified by the operator's ACE and approved by the National Insurance Commission (NAICOM).

[823] Section 4(4) (a) & Section 4 (5) Guidelines for Takaful Operators 2013.
[824] Frenz, T. & Soualhi, Y., *op cit*, p. 257.
[825] *Ibid.*

Investment challenges under conventional insurance are quite limited in comparison to those faced by *Takaful* operators because of the *Shari'ah*-compliance requirement. For example:

(1) The limited availability of Islamic investment options in general and in long term and high quality instruments in particular leads to potentially lower investment returns, restricts product innovation and increases the concentration and liquidity risks.[826]

(2) It might further raise the capital requirements for *Takaful* operators subject to risk-based capital requirements and make asset-liability management more challenging vis-à-vis conventional insurance.[827]

(3) Restrictions on the asset allocation of the *Takaful* fund assets might be difficult to follow for a *Takaful* operator due to the limited availability of proper Islamic investments.[828]

(4) Suitable Islamic investments might be issued in a different currency (e.g. USD), exposing the operator to a potentially significant currency exchange risk.[829]

Due to the special expertise and additional resources and systems required, *Takaful* operators often outsource this function to professional fund management companies. Conventional insurance investment practice has no such worries.

Also on the issue of staffing, there is a serious shortage of both *Shari'ah* advisors well versed in *Takaful* and managers, actuaries, underwriters, accountants, sales agents and investment experts familiar with the *Shari'ah* principles. The staff and agents of *Takaful* operators most likely have conventional insurance backgrounds and require further training to fully absorb the *Takaful* idea and specifics. The expertise of experts in

[826] Frenz, T. & Soualhi, Y. *op cit*, p. 258.
[827] *Ibid.* See also Ma'asum, B.M., (2001), *Principles and Practices of Takaful and Insurance Compared,* Malaysia: International Islamic University of Malaysia (IIUM)
[828] *Ibid.*
[829] *Ibid.*

conventional banking, insurance and finance is still very much critical to the development of *Takaful*. The two distinct insurance systems do have a common ground and complement each other.

The Guidelines for *Takaful* in Nigeria still require the *Takaful* operator to ensure that assets and liabilities allocated to the funds match and must set out objectives and long term strategies for each class of funds. He is also required to consider risk profile of the fund in line with the characteristics of *Takaful* liabilities.[830] The operator must ensure that various funds are segregated and ring-fenced to protect the interest of the participants.[831]

Still on investments, the areas of investment in the two types of insurance are similar with differences in components of the investment and the nature of the returns.[832] In conventional insurance interest is a key component of admissible assets under Section 24 (13) of the Insurance Act. It provides;

> …..''Admissible assets'' means assets designated as admissible assets consisting of the following –
>
> a) cash and bank balances;
>
> b) quoted investment at market value;
>
> c) unquoted stock at cost;
>
> d) land and buildings;
>
> e) furniture and fittings;

[830] Section 4 (4) (b) & (c) *Takaful* Guidelines 2013.
[831] Adamu, A.I., *op cit*, p. 120.
[832] For economic development, investments are necessary. Investments are made out of savings. A *Takaful* operating company is a major instrument for the mobilization of savings of people, particularly from the middle and lower income groups. These savings are channelled into investments for economic growth. The Insurance Act, 2003, has strict provisions to ensure that insurance funds are invested in safe avenues like government bonds, companies with good records of performance etc. Even at that, *Takaful* operators have several avenues of non-interest yielding portfolios to invest its huge funds, accumulated through the payments of small amounts of premium of individuals. These funds are invested in ways that contribute substantially to the economic development of the countries in which they do business. See Yusuf, T.O., *op cit*, p. 227.

f) office equipment;

g) motor vehicles;

h) prepared expenses made to member of staff;

i) amount due from retrocession;

j) staff loans and advances; and

k) claims receivable''[833]

However, under a *Takaful* undertaking, interest is the vitiating factor of the transaction. This position is, however, subject to the purification provision stipulated in the *Takaful* Guidelines.[834]

Another area of contention is with regards to whether the provisions of Section 25 of the Insurance Act will apply to *Takaful* insurance besides its specific provision under the *Takaful* Guidelines. If the provisions of the Act apply besides regulation of *Takaful* investment in the Guidelines, the *Takaful* operator must also meet the requirements of Section 25 of the Act. The Act provides as follows:-

'' (1) An insurer shall at all times in respect of the insurance transacted by it in Nigeria, invest and hold invested in Nigeria assets equivalent to not less than the amount of policy-holders' funds in such insurance business as shown in the balance sheet and the revenue accounts of the insurer.

(2) Subject to the provisions of this section, the policy-holders' funds shall not be invested in property and securities except –

(a) shares of limited liability companies;

[833] Section 24 (13) Insurance Act 2003
[834] See Section 4.4(b) & (c) of *Takaful* Operational Guidelines, 2003.

(b) shares in other securities of a co-operative society registered under a law relating to co-operative societies;

(c) loans to building societies approved by the Commission;

(d) loans on real property, machinery and plant in Nigeria;

(e) loans on life policies within their surrender values;

(f) cash deposits in or bills of exchange accepted by licensed banks; and

(g) such investments as may be prescribed by the Commission.

(3) No insurer shall –

(a) in respect of its general insurance business, invest more than twenty-five per cent of its assets as defined in subsection (1) of this section in real property; or

(b) in contract of its life insurance business, invest more than thirty-five per cent of its assets as defined in subsection (1) of this section in real property.

(4) An insurer which contravenes the provisions of this section commits an offence and is liable on conviction to a fine of N50,000.00 which is about RM 1000.

(5) In this section, references to real property include references to an estate in land, a lease or a right of occupancy under the Land Use Act.''[835]

It is humbly submitted that the provisions of this section of the Act will be difficult to be applied to instances of *Takaful* operations because of the usury or interest factor.

[835] Section 25 Insurance Act 2003. The provisions in this section are confusing and appear to conflict with the provision of investments under *Takaful*. The Guidelines have not fully insulated *Takaful* from the effects of this section. Even if they appear to have done so by the generalizing statement that everything about *Takaful* has to be in full compliance of *Shariah*, it needs to be made clear and certain that Section 25 of Insurance Act, 2003 has no bearing at all on the provisions of the *Takaful* Operational Guidelines, 2013. Laws must be made expressly clear and certain if they are to provide enabling environment for their application. Ambiguity breeds mistrust and confidence. The supremacy of the Insurance Act, 2003 contained in Section 100 is a worrisome provision that NAICOM failed to take into cognisance when drafting the Guidelines. It is such regulatory uncertainties that this study aims to highlight with a view to effecting corrections under a substantive *Takaful* Act in Nigeria.

This area is yet to be tested either in a court of competent jurisdiction or in a review parley of the National Assembly. What remains imperative is that the *Shari'ah*-compliant nature of *Takaful* is something that cannot be compromised or condoned in the course of its application. It is either there is full compliance or the contract is rendered void *ab initio.*

4.2.6 Re*Takaful*/Reinsurance

Re*Takaful*,[836] which is ''*Takaful* for *Takaful* operators'' is strictly based on *Shari'ah* principles. Re*Takaful* is a transaction whereby one company (the re*Takaful* operator) agrees to indemnify another *Takaful* company (the ceding company or cedant) against all or part of the loss that the latter sustains under *Takaful* contracts that it has issued. For this service, the ceding company pays the re*Takaful* operator a contribution.[837]

Re*Takaful* allows operators to share risks that they cannot, or do not wish, to absorb themselves. The main purpose of re*Takaful* is similar to that of reinsurance – to spread risk and add capacity so that larger or more risks can be written. By spreading risk within the *Takaful* industry, re*Takaful* enables the *Takaful* industry to function more efficiently.[838]

This sounds very much like reinsurance, but the fundamental difference is that re*Takaful* is about sharing the risk, i.e. risk is not transferred to the re*Takaful* operator. The re*Takaful* operator becomes a risk manager instead of a risk taker. This is a mirror of the relationship between a *Takaful* operator as agent and the *Takaful* participants as owners of the *Takaful* fund. The risk remains with the participants and by extension to re*Takaful* it implies that the risk remains with the ceding *Takaful* operator. This is the

[836] Re*Takaful* is a global scourge affecting the trending *Takaful* industry. *Takaful* industry is just beginning to take root and the issue of Re*Takaful* has not made it easy because of inexperience. Conventional insurance companies have no such problems because they have been in the business for quite long and the issue of *Riba* firmly stands in their favour in aid of their industry. The situation is so bad for *Takaful* industries that many *Takaful* Operators resort to the services of conventional reinsurance companies to reinsure in spite of the *Shariah* prohibition elements. The case in Nigeria is even made worse because the *Takaful* Operating companies are just coming on stream and the issue of re*Takaful* is not even being contemplated.
[837] Frenz, T. & Soualhi, Y., *op cit*, p. 258.
[838] *Ibid.*

theoretical view, though in practice the requirement of *Qard Hasan* puts the re*Takaful* equally at risk.[839]

4.2.7 Risk and Claims Management

Literally, risk is the possibility of adverse results stemming from any occurrence. An insurance risk means uncertainty about a financial loss. It is also an unforeseeable psychological uncertainty of the mind. A risk must meet the following conditions, if it is to be covered by an insurance policy:

(i) It must be something that can be defined even though it is unexpected.

(ii) The purpose of having an insurance cover against a risk must be for the purpose of a material protection against loss, but not purely for a material gain or chance.

(iii) No risk on an unlawful subject matter should be covered by a policy.

(iv) The risk should not be deliberately invented.

(v) The occurrence of a risk must not be certainly known prior to the time it happens[840].

There are different categories of risk which have been discussed in details earlier on in this study. These include subjective risk which brings financial loss to the risk owner and it is judged by personal and emotional assessments in a certain situation.[841]

There is also objective risk which is a risk that is measured by the number of losses or transactions that happen within a certain time frame for a particular item. It can be counted and records are usually properly documented for accounting purposes.

[839] Frenz, T. & Soualhi, Y., *op cit.*
[840] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 13.
[841] *Ibid.*

Assessing objective risks in a business may help the management to control their production line and value their operation risk.[842]

There is pure and defined risk where one can expect two possible outcomes, which is loss or no loss. No beneficial outcome may result from the event of a pure risk. The event mentioned is beyond the risk owner or risk taker's control and therefore one cannot consciously choose for the event not to happen. The risk should be an event that can be defined and described in common language. Not all financial losses due to a pure risk are covered by insurance. A detailed definition of risk must be clearly defined to the insured.[843]

A risk is categorized as speculative if there is a possible outcome of benefit, apart from any loss if the event of risk occurs. A risk taker usually makes a decision to accept speculative risk with his conscious mind, that he will gain a benefit or lose his investment in the action preceding the event. This action is similar to gambling and therefore not permitted in Islam. Almost every investment is involved in speculative risk. However, the degree of speculation varies between the types of investment. For example, investment in bonds has a lower speculation risk due to lower default risk and government bonds have the least risk compared to investment in a firm's shares.[844]

Other categories of risk include risk that is deliberately invented, risk of a certain event happening, risk on unlawful subject matter, risk on un-owned subject matter and risk on unknown subject matter.

From *Takaful* perspective, risk is seen as a possibility that something unpleasant or undesirable might happen. The possible or nearest Islamic equivalent concept to risk is *Gharar*. Literally, in Islamic context, risk is defined as an event that contains a number

[842] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 13.
[843] *Ibid.*
[844] *Ibid.*

of negative elements, e.g. deceit/fraud (*Khid'ah*), uncertainty, danger/risk, and peril/hazard (*Khatar*) that might lead to destruction and loss. From the Islamic legal terminology, risk is defined as something that is folded in its nature and concealed in its consequence. Thus, risk, is viewed as both uncertainty and hazard.[845]

Generally, *Gharar* is the negative element in a commercial transaction. All jurists agree on the need to avoid *Gharar* in commercial transactions essentially because of its prohibition in Islamic law.[846]

In insurance, the idea of risk is two-fold. The first has to do with uncertainty about the future outcome of an event. Risk is related to an unfavourable outcome or unfortunate event, whereas, chance, is something which relates to a favourable outcome.[847] The second feature of risk is the entire insurable interest and subject matter of the contract. The concept of risk, in Islam, is wrongly perceived from the point of view of fate or predestination (*Qadr*). However, Muslims are required to be proactive in order to be able to change their condition. Allaah SWT stated in the Noble Qur'an that:-

> ''Verily never will Allaah change the condition of a people until they change it themselves.''[848]

The essence of insurance in both conventional way and *Takaful* is to minimize or hedge risk. Therefore, the perception of risk management from the point of view of the two systems of insurance is the same. A prudent insurer or *Takaful* operator would ensure

[845] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 13.
[846] However, some learned authors like Siddiqi maintain that the uncertainty involved in the contract tends to disappear when large numbers are involved. See Sadiq, C.M., (2001), *Islamic Insurance (Takaful); Concept and Practice*, Encyclopaedia of Islamic Banking and Insurance, London, Institute of Islamic Banking and Insurance. Ma'asum, also pointed out that the possibility of *Gharar* being involved in the subject matter of the contract is only through the 'happening of the risk' and this uncertainty will forever be known only by Allaah. The uncertainty comes in the form of pure risk which is implicated with the fear of risk, for example, the death of the policyholder or the incident insured is not vague and is identified before the commencement of the policy. See Ma'asum, B.M., (2001), *Principles and Practices of Takaful and Insurance Compared*, Malaysia: International Islamic University of Malaysia (IIUM). Rosly, has however, questioned the address of *Gharar* pinpointed by the *Fatwa* from the perspective of risks which are dealt with by a commercial insurance contract. He suspected that that the issue of *Gharar* contended by the *Fatwa* is misplaced in certain parts that is in the uncertainty of the events, for example the occurring of death or injury. These uncertainties are pure risks that are transferred to the insurer companies by the insured through the payments of premiums and are beyond human control. See Rosly, S.A., (1997), Economic Principles in Islam, International Islamic University, *Journal of Economics and Management.*
[847] Zulkifli, A., et al, (2012), Basic *Takaful* Practices Publication of IBFIM & Malaysian *Takaful* Association, p. 19.
[848] Noble Qur'an Chapter 13 verse 11.

that when risks are identified and assessed, he deploys all the techniques and measures to manage the risks. This risk management is from the perspective of the insurer and operator and will be in the form of risk avoidance, risk reduction, risk retention, risk transfer or risk sharing.[849]

As with conventional insurance, the concept of risk categorization[850] also applies to the *Takaful* operator. However, risks that can be covered by *Takaful* are subjective risk, objective risk and pure risk. All these three types of risks do not contain elements of *Gharar* as per speculative risk. Some speculative risks such as hedging in a future contract are covered by conventional insurance.[851]

Even though conventional insurance and *Takaful* are among the tools used in risk mitigation, there is a slight difference in terms of managing risk. In an insurance contract, risk is being transferred from the insured as the actual risk owner to the insurance company, by paying a certain price (premium). The premium paid by the policyholder is in exchange with the benefits of the contract. The insurer has an obligation to provide the sum insured as per agreement to pay the insured for the financial loss claim, if the event covered by the policy occurs.[852]

However, *Takaful* does not apply the same concept because Islamic law requires the contract of exchange to be free from *Gharar* (risk protection is not of equal value to the premium charged). To make it legal, a *Takaful* contract must be based on a *Tabarru'* (donation) contract. The *Takaful* contract should be valid (*Shari'ah* compliant).[853]

In a *Takaful* contract, the defined risk is being shared among the participants in the same group. Each of them contributes a portion of money called *Tabarru'* and each participant will relinquish the claims on this amount of contribution if none of the

[849] Adamu, A.I., *op cit*, p. 122.
[850] Classifying risks as 'Legal Risk', 'Reputational Risk', 'Regulatory Risk', 'Operational Risk' etc.
[851] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 18.
[852] *Ibid.*
[853] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 19.

covered risks occurred. This act is in line with the principle of *Takaful* whereby there is need for the participants to mutually assist each other in the event of a loss.[854]

Some common misconceptions of risk management in *Takaful* by the public include;

(a) Risk protection is against *Tawakkul,*[855] i.e. total dependence upon Allaah SWT;

(b) All risk protection are equivalent with conventional insurance, and therefore, it is prohibited, (*Haram*);

(c) All insurance is a form of gambling or wagering, which is forbidden in Islam;

(d) All insurers are maximizing profit which takes benefits away from policyholders;

(e) All *Takaful* operators' nature of business is the same as conventional insurance companies.

Shari'ah compliance is a fundamental attribute of *Takaful*. The *Takaful* operator must always comply with this requirement.[856] This is a huge risk which the *Takaful* operator is exposed to because he cannot afford to slip. Any veering off in the operations and transactions from this strict adherence renders the contract null and void. Were this to occur, the operator may face the risk of non-recognition of income and reputational risk which could lead to regulatory sanctions in the form of contract cancellation and donation of the income to charity.[857]

On claim management,[858] Section 70 of the Insurance Act provides for timing of settlement of claim by conventional insurance. The section demands for settlement of

[854] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 19..
[855] Sole reliance on the Decree of Allaah SWT.
[856] Authors and scholars are unanimous in pointing out the fact that *Shari'ah* compliance is everything about Islamic finance which includes *Takaful.* Any attempt in circumventing this fact not only renders the transaction null and void but is a major sin which could take a Muslim out of the fold of Islam.
[857] Adamu, A.I., *op cit*, p. 122.
[858] The issue of claims management is so vital to the revival of the stagnant insurance industry in Nigeria. One of the major complaints about conventional insurance practice is that insurance companies are always eager to collect premiums from clients but reluctant to settle claims even when it has been certified that the claim is genuine. The low claims ratio of 24% in the country shows that the industry offers very little value to insurance clients. According to NAICOM Insurance Statistics Report, 2015, the average claims ratio (gross claims over gross premium income) for all companies including reinsurance stood at 24.2%. This is dismal, according to a Lagos based legal practitioner, Mahmoud Magaji who is a Senior Advocate of Nigeria (SAN) in an interview with

claim where the discharge voucher is executed, not later than ninety (90) days of doing so. Where the claim is repudiated, the insurer must communicate to the insured within those days. The Act states;

> ''(1) Subject to Section 69 of this Act, in every case where a claim is made in writing by the insured or any other party entitled thereto under insurance policy, the insurer shall –
>
> (a) Where he accepts liability, settle the claim not later than 90 days after the issuance of the discharge voucher;
>
> (b) Where any claim remains unpaid as provided in subsection (a) above, the insured may request the Commission to effect the payment from the statutory deposit of the insurer and the Commission shall have power to effect such payment; or
>
> (c) Where he does not accept liability, deliver a statement in writing stating the reason for disclaiming such liability to the person making the claim or his authorized representative not later than 90 days from the date on which the person delivered his claim to the insurer.
>
> (2) Any insurer who contravenes this section commits an offence and on conviction is liable to a fine of N500, 000.00 equivalent of RM 10,000.00.''[859]

Underwriting and claims management are the two most important aspects of *Takaful* operations. Out of any *Takaful* contract, participants usually have the following expectations:

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the researcher. He further stated that this is a pitfall the nascent *Takaful* industry in Nigeria must seek to avoid by all means because non-settlement of claims totally erodes the confidence and trust of the insuring populace. There are too many obstructions lined up on the road towards claims settlement, including fraud like fake insurance and fake insurance agents. Any form of insurance is all about claims settlement. The client's expectation that claims is a certain and easy process must be satisfied. See Appendix 1.2 of the thesis.

[859] Section 70 Insurance Act 2003.

(1) Adequate *Takaful* coverage;

(2) Timely delivery of defect-free certificates with relevant endorsement, conditions and warranties; and

(3) Prompt payment and settlement of claim to his or her satisfaction, should a claim arise.[860]

However, the settlement of a claim must always be in line with the terms and conditions of the contract as stipulated in the *Takaful* certificate. Once the claim has been notified and all parties have carried out their respective duties, all that remains is for the claim to be settled.

If it is proven that the claim application is valid, settlement will be made immediately. The actual settlement, or amount payable, depends upon a number of factors including the nature of the cover, the adequacy of the cover and the application of any conditions which limit the amount payable.[861]

On every claim from the general *Takaful* fund, there are aspects of recovery either from the defaulted party or re*Takaful* to minimize the loss of the fund as much as possible. Whilst recoveries from a defaulted party usually take a longer legal process, recovery from re*Takaful*/reinsurance may exist in two forms:

(a) From excess of loss, where the operator's net loss exceeds the limit of the company;

(b) From surplus re*Takaful*/reinsurance on their share of the loss.[862]

[860] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 57. The reputation of conventional insurance industry has suffered immensely due to lack of prompt claims settlement and the industry in Nigeria is now paying the price because insurance is looked upon with such contempt and derision. This has made the industry to stagnate without any meaningful growth despite the huge potential. Incidentally, the loss of the conventional insurance industry is the gain of *Takaful* because there is so much buzz in the air now with the introduction of *Takaful* which is dubbed insurance with human face. Muslims and non-Muslims are buying into it.
[861] *Ibid.*
[862] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 57.

Settlement of claims under *Takaful* is usually less strenuous. In the Nigerian context, the Guidelines require the *Takaful* operator to process and settle the claim within a reasonable time frame where there is no adverse issue with the claim.[863]

The Guidelines further provide for payment of claims from the correct *Takaful* fund and in line with the *Takaful*-Insurance contract terms and conditions.[864] This is similar to what obtains in conventional insurance under segregation of accounts and funds in respect of Life and General business insurance as provided in Section 19 (1) of the Insurance Act.[865] It states, thus;

> '' (1) Where an insurer carries on the two classes of insurance business, all receipts of each of those classes of insurance business shall be entered in a separate and distinct account and shall be carried to and from a separate insurance fund with the appropriate name so that in case of life insurance there shall be –
>
> (a) the individual life insurance business fund;
>
> (b) the group life insurance business and pension fund; and
>
> (c) health insurance business.
>
> (2) Each insurance fund shall represent the liabilities in respect of all contracts of insurance of that particular class and shall consist –
>
> (a) in the case of life insurance business, the life business funds shall be a sum not less than the mathematical reserve; and
>
> (b) in the case of general insurance business of the provisions for unexpired risk and provisions for outstanding claims, including in the case of the latter,

[863] Section 5 (7) Operational *Takaful* Guidelines 2013.
[864] Section 5 (8) *Ibid*..
[865] Insurance Act, 2003, LFN.

provisions estimated to provide for the expenses of adjustment or settlement of such claims.

(3) The insurance fund of each particular class shall –

(a) be absolutely the security of the policy holders of that class as though it belonged to an insurer carrying on other business than insurance business of that class;

(b) not be liable for any contract of the insurer for which it would not have been liable had the business of the insurer been only that of particular insurance class; and

(c) not be applied, directly or indirectly, for any purposes other than those of the class of business to which the fund is applicable.''[866]

4.2.8 Actuarial and Ratings[867]

The word rating has two different connotations in the corporate finance world. The first context is the credit rating of a financial institution which is used by conventional insurance companies to demonstrate financial strength, transparency and viability and sometimes for management purposes. However, the word rating is construed in insurance transactions as the determinant factor in pricing risks.[868] The focal point is about standard pricing of the insurance product that is offered to the market.

Section 51 of the Insurance Act[869] bars insurance operators from making general increase in the minimum rates of premiums charged in respect of class of insurance

[866] Section 19 (1) (a),(b), (c), (2), (a), (b) and (3), (a),(b), (c) Insurance Act 2003.
[867] This is one of the critical areas that Islamic finance industry is facing in its bid to thrive and remain relevant on the global economic stage. Although Islamic regulatory bodies have established standards, different interpretations of religious texts and weak implementation means they lack harmonization. Such challenges being faced may not only be impeding the development of the industry but could also encourage complex practices and products that carry heightened risks.
[868] Adamu, A.I., *op cit*, p. 123.
[869] Insurance Act 2003, Laws of the Federation of Nigeria.

made compulsory by law. Instances of this class of business are third party indemnities under Motor Insurance and Employers' Liabilities. The section provides:-

'' (1) No insurer shall either by itself or as a member of an association of insurers make a general increase in the premium rates of premiums charged or to be charged with respect to any class of insurance business made compulsory by law except with a prior approval of the Commission.

(2) An insurer who makes a general increase otherwise than in compliance with subsection (1) of this section commits an offence and is liable on conviction to a fine of ten times the amount of premium charged and received by the insurer or N100, 000.00 whichever is greater.

(3) An insurer who increases rates of premium charged or to be charged with respect to any class of insurance business made compulsory by law otherwise than in compliance with subsection (1) of this section commits an offence and is liable on conviction to either of the additional penalties –

(a) suspension of its operations in respect of new insurance business for a period of not less than six months or more than three years; or

(b) cancellation of its certificate of registration, and in addition to either of the foregoing, the insurer shall refund the excess payment to every person making such excess payment or to other person entitled thereto.

(4) The penalties referred to in subsection (3) of this section shall be imposed by the Commission and an insurer who feels aggrieved may appeal to the Minister of Finance in accordance with the provisions of section 7 of this Act.

(5) The provisions of this section shall not apply to non-tariff insurance business where premiums are charged according to the risk covered by the insurance policy.[870]

The issue of rating in *Takaful* is based on the participant's contribution ability. However, the Guidelines for the registration of *Takaful* operators demands that the applicant for registration as *Takaful* operator to submit its risk management and rating procedures.[871] Although it is not clear whether the risk rating under tariff policies would apply to *Takaful* operators underwriting third party insurance, the fact remains that some of the provisions of the Insurance Act will apply in *Takaful* underwriting as it is in conventional insurance.[872]

On the issue of actuaries, an actuary deals with the business of insurance and is responsible for many areas under the broad category of insurance. The actuary is an individual who will analyse important data such as mortality, sickness, injury and disability rates and use that information to aid those involved with insurance. An actuary is responsible for collecting the data to forecast future risks and see how these predictions will affect various aspects of insurance.[873]

Actuaries use skills in mathematics, economics, computer science, finance probability and statistics, and business, to help businesses assess the risk of certain events occurring and to formulate policies that minimize the cost of that risk. For this reason, actuaries are essential to the insurance and reinsurance industry as staff or consultants to other businesses, including sponsors of pension plans.[874]

[870] Section 51 (1), (2), (3), (a) (b), (4) and (5) Insurance Act 2003.
[871] Appendix 6, Registration Requirement for *Takaful* Operators in Nigeria, Part 2 b, v.
[872] This is a grey area that needs harmonization because the provision is unclear as to whether the Insurance Act 2003 will apply to *Takaful* on the issue of ratings. This is just one of numerous examples of regulatory discrepancies that are replete in the Insurance Act 2003 and *Takaful* Guidelines 2013 which will not augur well for the smooth application of *Takaful* if it remains unresolved. A new comprehensive Takaful legislation will put to rest all these conflicting issues.
[873] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 76.
[874] *Ibid.*

They also address financial questions, including those involving the level of pension contributions required to produce a certain retirement income and the way in which a company should invest resources to maximize its return on investments in light of potential risk. Using their broad knowledge, actuaries help to design and price insurance policies, pension plans, and other financial strategies in a manner which will help ensure that the plans are maintained on a sound financial basis.[875]

The *Takaful* product/scheme constructed by actuaries must meet the actual needs of the customer/participant and should be marketable. The more attractive the products are, the more people in the same group of risk will join the scheme. More participants with various degrees of risk exposure may reduce risk and add cash value in the participants' special account. Various risk degrees of the participants may eliminate anti-selection or adverse selection.[876]

In Nigeria, Section 29 of the Insurance Act requires an insurer transacting life insurance business to cause for investigation into its activities every three years by an actuary. This investigation relates to valuation of the company's assets and liabilities as determined by how the liabilities are represented. In the same manner, the requirement of the section will seem to apply to *Takaful* Family operator in a similar way to a Life insurer under conventional insurance.[877] The section provides:-

> ''(1) An insurer transacting life insurance business shall in respect of its life insurance business once in every period of three years, cause an investigation to be made into its financial position by an actuary appointed or secured by the insurer.
>
> (2) An investigation under subsection (1) of this section shall include –

[875] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 76.
[876] *Ibid*, p. 78.
[877] *Ibid*.

(a) a valuation of the assets and liabilities of the insurer; and

(b) a determination of any excess over those liabilities of the assets representing the funds maintained by the insurer.

(3) For the purposes of an investigation under this section, the value of any asset and the amount of liability shall be determined in accordance with applicable valuation regulations.''[878]

4.3 SUPERVISORY ISSUES IN CONVENTIONAL INSURANCE AND *TAKAFUL*[879]

The application and integration of *Takaful* contracts into the supervisory framework of conventional insurance in Nigeria is full of challenges. In order for the *Takaful* contract to be valid and enforceable under the law, the operator is expected to comply with the strict requirements of *Shari'ah* principles, other relevant provisions of the law and at the same time adhere to the principles and regulations guiding conventional insurance. The underlying effect of complying with a plethora of legal frameworks presents possibilities of disputes arising out of conflict of laws. Conventional insurance and *Takaful* have so many distinct features that conflict with each other in terms of essence and implementation.

Furthermore, the challenges are compounded by the dearth of expertise in *Shari'ah* skills among the regulators. Again, the principles of *Shari'ah* are largely un-codified and in Arabic which is not an easy language to deal with. This makes the role of Islamic scholars indispensable. This study looks at the challenges posed by the distinctions in

[878] Section 29 (1), (2)(a)(b) and (3) Insurance Act 2003.

[879] The development of financial markets and the insurance sector in particular depends to a great extent on the existence of an enabling policy, regulatory and supervisory environment. Policies are important as they define the priorities, the roles and responsibilities of significant stakeholders, and influence where the bulk of financial, political and human resources, from both private and public actors, are invested. Regulation above all sets the rules for entry, operation and market conduct. Supervision ensures compliance with the rules and penalizes violations, being therefore an important factor to increase public confidence. See Dias, D. et al, (2013), *Towards Inclusive Insurance in Nigeria: An Analysis of the Market and Regulations,* Access to Insurance Initiative, Eschborn, p. 50.

conventional insurance and *Takaful* within the context of their governance structures, financial and prudential constituents in order to make a case for the harmonization of these supervisory and regulatory discrepancies.

4.3.1 Governance

The International Association of Insurance Supervisors (IAIS) sets out an over reaching framework for supervision which articulates the relationship between the different elements of supervision. It provides:-

> ''The framework for insurance supervision consists of three groups of issues: financial issues, governance issues and market conduct issues. It also encapsulates three levels or aspects in relation to these issues, reflecting three different responsibilities; preconditions for effective insurance supervision, regulatory requirements, and supervisory action.''[880]

The precondition for the effective insurance supervision covers such issues as institutional and legal framework for the insurance, efficient market and the existence of a supervisory authority with operational independence, adequate powers and resources.[881] These preconditions presuppose the existence of three fundamental factors:-

(a) The financial strength of the insurer;

[880] A New Framework for Insurance Supervision: Towards a Common Structure for the Assessment of Insurer Solvency (the Framework) International Association of Insurance Supervisors, October 2005.
In Malaysia, the Islamic Financial Services Act (IFSA) 2013 outlines thorough statutory duties for the Board of Directors, *Shari'ah* Committee and the management of *Takaful* operators to ensure that the *Takaful* industry achieves *Shari'ah* compliant status in totality. Accordingly, IFSA 2013 provides a new horizon on the *Shari'ah* governance for Islamic Financial Institutions (IFIs). This is true in the sense that the IFAS 2013 upholds the *Shari'ah* Governance Framework ('SGF') for IFIs issued by Bank Negara Malaysia ('BNM') in 2011. The SGF is considered as the most important guideline issued by BNM on *Shariah* governance for IFIs. The SGF and other guidelines issued by BNM are given a statutory force by virtue of Section 29 of the IFSA, 2013.
As provided under Section 29(2) of the IFSA 2013, SGF now becomes a standard that shall be complied with by all IFIs. The ultimate objective of the SGF is to ensure all operations and business activities of IFIs are in accordance with the *Shari'ah*. The SGF puts a significant emphasis for the IFIs to establish *Shari'ah* compliance functions consisting of *Shari'ah* review, *Shari'ah* audit, *Shari'ah* risk management and *Shari'ah* research functions as important components of sound and robust *Shari'ah* governance in IFIs. It is worth noting that failure of the IFIs to comply with the requirements of the SGF will expose the IFIs and its officers to severe statutory punishments as provided under IFSA 2013. This shows the gravity of the SGF in relation to the IFSA 2013. See generally Abd Hamid M.H. & Hassan, R., *op cit.* p. lxviii.
[881] Adamu, A.I., *op cit*, p. 126.

(b) The governance structure of the insurer;

(c) How an insurer conducts his business and presents himself in the market.

The *Shari'ah* foundation for *Takaful* is based on the divine revelation as well as the practice of the Prophet pbuh and his companions. *Shari'ah* has set out the rules and regulations as guidance to ensure all Islamic transactions are practiced according to the teachings of Islam. As such, *Takaful* services are obliged to follow the said Islamic teaching. Nonetheless, *Takaful* institutions are also governed by the laws of the countries where they operate. It is vital for Islamic financial institutions to develop financial services and instruments that are not only *Shari'ah*-compliant, but also viable and enforceable based on the governing laws of the country.[882] In Malaysia, for example, cases involving Islamic financial institutions fall under the civil and not *Shari'ah* court jurisdiction. Thus legislations relating to these institutions' operations and Islamic law generally are to be applied and implemented within existing common courts and all other existing laws. This includes not only substantive but procedural laws, court systems and procedures. Because the existing regime of secular legislation is not designed to implement and facilitate the application of Islamic law, some obstacles and challenges to the Islamic financial industry have resulted.[883]

Specifically, in the case of *Takaful*, the governance issues relate to embracing the rights and obligations of the various parties and structures that balance and safeguard the contending interests. The governance structure of *Takaful* in Nigeria under the Guidelines is similar to that of a conventional insurer under the Insurance Act. This presupposes that the operator must be a limited liability company and must meet the minimum capital and registration requirements. The point of departure in this regard is that the operation of *Takaful* can be undertaken as a subsidiary of another insurer which

[882] Hassan, R., *op cit*, p. 73.
[883] *Ibid.*

is called 'window operation'. In this regard, the National Insurance Commission has issued licenses to some insurance companies who already operate the business of *Takaful* along with their substantive business as conventional insurers.[884]

Another fundamental area of difference in the operational structures of the two systems of insurance is the requirement of the *Takaful* operator to have in place an Advisory Council of Experts (ACE).[885] It provides;-

> ''The *Takaful* insurance operator before starting *Takaful* insurance operations shall have in place an Advisory Council of Experts (ACE) to ensure the operations are in line with best practice. Any alternative approach to the establishment of ACE must be preapproved by the Commission as per 3.11.''[886]

The Council will consist of at least one member who is professionally qualified and knowledgeable in insurance and two other members who shall be scholars qualified and experienced in *Shari'ah* and specialized in *Fiqh al Mu'amalat* (Islamic commercial jurisprudence). The Council members are expected to execute codes of conduct and to conduct themselves in a professional and ethical manner. They must also be just, honest and impartial and must avoid any circumstance that will impair their independence. The members shall not have beneficial interest in the *Takaful* operator.[887]

Under conventional insurance, Board membership is the equivalent of ACE. However, the strict requirements laid down for ACE membership are not as stringent as in conventional insurance, although certain levels of education and experience are mandatory.

Section 12 of the Insurance Act provides for grounds of disqualifying appointment as Director or Chief Executive of an insurance company. The section specifically

[884] Adamu, A.I., *op cit*, p. 126.
[885] Section 3(6) Operational Guidelines for *Takaful* Operators 2013.
[886] *Ibid.*
[887] Adamu, A.I., *op cit*, p. 127.

mentioned several acts of misconduct which include: disqualification from professional calling, conviction for dishonesty and fraud.[888]

The distinction that becomes evident from the point of view of governance issues embodied in the two systems of insurance is the challenge of capacity on the part of the Regulator to enforce the demand of high ethical standard which *Takaful* operation insists upon.

It is pertinent to note that regulators in traditionally conventional insurance markets are adopting a ''level playing field'' approach by incorporating *Takaful*-specific guidelines/sections within existing regulatory framework. *Takaful* regulation in many markets mirrors conventional insurance guidelines, without considering to a full extent the specifics of *Takaful* business. These are pertinent issues that need to be addressed quickly if harmonization is to be achieved.

4.3.2 Financial Considerations

The assets profile of a *Takaful* operator is different from that of its counterpart under conventional insurance. Therefore, the capital regime needs to take that into consideration. Operators are faced with a potentially more volatile and less diversified portfolio in view of the small market place, though this could easily be managed through an appropriate re*Takaful* arrangement.[889]

[888] Section 12(1) Insurance Act 2003, provides;-
No insurer shall appoint or have in its employment a director, chief executive, manager or secretary if he –
(a) is or becomes of unsound mind, or as result of ill health, is incapable of carrying out his duties;
(b) is convicted of any offence involving dishonesty or fraud;
(c) is not fit and proper person for the position;
(d) is guilty of serious misconduct in relation to his duties;
(e) in the case of a person with professional qualification, has been disqualified or suspended from practising his profession in Nigeria by the order of any competent authority made in respect of him personally;
(f) is a person who has been a director of or has been directly concerned with the management of an insurance or financial institution whose license to operate is cancelled or whose business has been wound-up on grounds specified in Sections 408(d) and 409 of the Companies and Allied Matters Act, 1990;
(g) is a person whose appointment with an insurance or a financial institution has been terminated or who has been dismissed for reasons of fraud or dishonesty; or
(h) has been convicted by a court or tribunal of an offence in the nature of criminal misappropriation of funds or breach of trust or cheating.

[889] Frenz, T. & Soualhi, Y., *op cit*, p. 217.

The financial issues with *Takaful* operators are virtually the same with those of conventional insurers. Some of the financial challenges that will be encountered in regulating *Takaful* in Nigeria are the adequacy of capital to meet the ethical standards of *Shari'ah*. This implies that the Regulator must be resourceful and innovative in ensuring that the *Takaful* undertaking is adequately resourced to support the early growth and development period of the business.[890]

Another area of financial concern in regulating *Takaful* is the prudential supervision concerning asset risk bearing in mind the relatively limited choice of investment and assets available to the operator.[891] The need for the regulator to safeguard the interest of the policy holders compounds the challenges on the regulator to be more vigilant in the assessment of risk run by the *Takaful* operators.[892]

4.3.3 Market Conduct Issues

The market conduct refers to the way an insurer deals with its policy holders or prospective policy holders. It also covers its dealings with other market players and its disposition towards market manipulation. Market conduct or prudential issues relate to attention given by the regulator on protection of policy holders.[893] The tools typically

[890] Adamu, A.I., *op cit*, p. 128. An Assistant Director in NAICOM who pleaded anonymity during an interview with the researcher stated that one huge criticism of NAICOM which is the insurance regulator in Nigeria is that it has left the issue of development of insurance to insurers while it concentrates mainly on supervision. NAICOM currently takes a compliance approach to supervision, with significant resources spent on verifying annual regulatory filings and on assessing fines for non-compliance with legislation. The framework for transparency and consumer protection in the insurance industry is not strong enough to offer protection to policyholders. This has contributed in no small measure towards the continued stagnation of the industry. *Takaful* that has just come on stream is bound to face similar challenges from the apathy of the regulatory institution. It is up to the practice to pick up the gauntlet and put their destiny in their hands. See Appendix 1.1 of thesis.

[891] Section 24(13) of Insurance Act, 2003 is instructive here. Conventional insurance investment portfolio has no problem here because the issue of interest is not a prohibitive factor. They can invest in any undertaking such as brewery, piggery, casinos, winery, lottery etc. whereas with *Takaful*, the investment options are limited because the *Shari'ah* compliance requirement of the ethics-based industry. This makes it more difficult and more challenging for *Takaful* operators to match the investment prowess of conventional insurers. But *Takaful* operators must seek solace in the fact that there is so much *Barakah* (blessing) in their enterprise which serves to please Allaah and solve the problems of their fellow human beings.

[892] Adamu, A.I., *op cit*, p. 128.

[893] Currently, NAICOM sets only a few market conduct and consumer protection rules which need to be improved. One of the main aspects that need urgent improvement is setting minimum standards for claims management in a way that policyholders can easily claim and receive benefits. Standards should also be set for complaints handling by insurance companies, including their capacity to manage and report complaints data through information systems.

employed by regulators in dealing with prudential discipline are regulation of contract terms and ratings as well as disclosure requirements.[894]

The primary focus of regulation in *Takaful* in this regard is compliance issues not only relating to the vitiating elements of the contract (*Riba, Gharar, Maysir* etc), but also other areas of contravention with conventional insurance regulations. The regulators will therefore need to have sufficient knowledge of *Takaful* to understand the products they are regulating and those significant differences between *Takaful* products and conventional ones. The emergence of *Takaful* market will significantly impact on the supervision of conventional insurance as well. The most obvious situation would be in the entry and expansion of *Takaful* players which will expose conventional insurers to greater competition and financial pressure thereby leading to possible market abuse.[895]

4.3.4 Supervisory Priorities

The overall priorities of a supervisor will be determined by its proffered assessment of the risk assumed by the supervised entities. In this context, the objectives will vary from the level of the risk appetite of the particular entity. Therefore, supervisory priorities will be driven substantially by the knowledge of peculiarities of the entity and circumstances surrounding its operations.[896]

The differences between *Takaful* and conventional insurance will always dominate supervisory attention and, this being the case, the regulator is bound to grapple with assessing emerging risks and determine the regulatory tools to use in mitigating them.[897]

[894] Adamu, A.I., *op cit.*
[895] Although consumer protection is a very relevant issue in insurance, the Consumer Protection Council Act and the Council itself does not seem to cover financial services, being focused on safety and health issues of consumer goods in other industries. See http://www.cpc.gov.ng.
[896] Adamu, A.I., *op cit*. See also Dias, D. et al, *op cit.*
[897] *Ibid.*

4.4 Conclusion

Insurance, whether conventional or Islamic, seeks to mitigate loss. In spite of similarities in the objectives of the two systems of insurance, the differences between them in relation to their historical origins, essence, ethical contents and approach to the issue of insurable risk are fundamentally distinct. It must always be borne in mind that Islamic insurance is very much conventional insurance when the *Shari'ah* vitiating elements are removed. The survival and growth of *Takaful* owes so much to the expertise and structure of conventional insurance.

The differences between the two forms of insurance serve to complement rather than divide each other in the global quest for financial inclusion. In this context, the effectiveness and competence of the Supervisor becomes critical in understanding the smallest of the differences with a view to deploying the relevant regulatory checks in governance, financial issues and market conduct of insurance operators.

In regulating *Takaful* companies, the regulators may, generally speaking, seek assistance from the administrative principles of conventional insurance companies. The regulators may use the conventional principles and actuarial rules for *Takaful* companies. This is an administrative procedure that would not be objected to by *Shari'ah*. The reason is that administrative procedures are actions that do not involve any contractual undertakings which may go against the principles of *Takaful* operation. *Shari'ah* allows benefitting from the good things of conventional insurance management and regulation methodology on the basis of the principle of valid public interest (*Maslahah Mu'tabarah*) or principle of *Siyasah al-Shari'ah*, which are

employed to allow rules and regulations that would have no explicit rules from the Qur'an and *Sunnah* provided their use will not violate basic principles of Islamic law.[898]

It is submitted that the insurance regulator also needs to deepen its understanding of the principles of *Takaful* from the primary source and how to apply those principles within the context of *Shari'ah* supervision.

The fact that *Takaful* is not identical with conventional insurance will invariably lead to some changes in regulatory approach. The accommodation should be healthy as this will serve to bolster financial inclusion. It will therefore become imperative for the National Insurance Commission (NAICOM) to adopt risk-based approach to supervision and to put its lean resources to maximum use.

The application and integration of *Takaful* into the legal framework of the Nigerian insurance industry which is tailored in a conventional insurance pattern will demand from the National Insurance Commission a higher level of capacity building and outsourcing of skills to meet regulatory demands. In view of this, it is safe for this study to add that there is nothing mystical in the unity of opposition if the much desired financial inclusion is realized at the end of the day.

[898] Arbouna, M.B., (2008) Regulation of *Takaful* Business: A *Shari'ah* Overview of Contractual Aspects of *Takaful* Models, In Essential Readings in Islamic Finance, *op cit*, p. 242.

CHAPTER 5: GENERAL AND REGULATORY CHALLENGES IN THE APPLICATION OF *TAKAFUL* WITHIN CONVENTIONAL INSURANCE

5.1 INTRODUCTION

Nigeria has taken a positive step towards the application of Islamic insurance (*Takaful*) with the introduction of Guidelines for the operation of *Takaful* in March, 2013 by the insurance regulator, National Insurance Commission of Nigeria[899] (NAICOM). The primary aim of the introduction of *Takaful* is to boost insurance penetration thereby sizing up to the universal objective of financial inclusion. This will ultimately help facilitate the establishment and delivery of suitable and affordable financial services for the underserved and disadvantaged segments of the Nigerian population regardless of religious conviction. Addressing the constraints for building inclusive financial sector is, therefore, paramount in helping to improve the lives of the people through the creation of sustainable financial services in the society. Therefore, considering the sizeable number of the financially excluded segment of the Nigerian population today, which constitutes more than seventy per cent, it is important to indicate that non-interest finance can be a very important tool for the promotion of financial inclusion in the country. The *Takaful* platform is about the protection of lives and properties based on

[899] Section 101 of the Insurance Act 2003 empowers the National Insurance Commission (NAICOM) to issue Guidelines on *Takaful*. The Section provides that ''The Commission may make rules and regulations generally for the purposes of giving effect to this Act''.
Furthermore, Section 86 of the Act provides that ''subject to the provisions of this Act, the National Insurance Commission (in this Act referred to as ''the Commission'') shall be responsible for administration and enforcement of this Act and is hereby authorized to carry out the provisions of this Act''.
Section 7(a) of NAICOM Act, 1997, states that the Commission shall ''establish standards for the conduct of insurance business in Nigeria''.
The objectives of the Guidelines on *Takaful* are:
a) providing minimum standards for the operation of *Takaful* insurance in Nigeria;
b) ensuring consumer protection in relation to *Takaful* insurance products;
c) setting up general requirements for *Takaful* insurance;
d) establishing duties and responsibilities of *Takaful* insurance operators and other insurance institutions in the market; and
e) setting conditions for the entry and exit of operators from *Takaful* insurance business.
The Guidelines (Registration Requirements for *Takaful* Operators, 2013, National Insurance Commission) prescribed general requirements for carrying out *Takaful* insurance in Nigeria, which include:
a) Entry Requirements:- a limited liability company or a subsidiary of the insurance company; minimum paid up share capital prescribed by the Commission;
b) Class of Business:- two broad classes of Family Solidarity and General *Takaful*;
c) Qualification Requirements:- the aims and operations of *Takaful* will not involve anything not approved by *Shariah*; establishment of *Shari'ah* Advisory Committee to advise the operator.
d) Grounds for Cancellation of Operators' Authorization: pursuing aims or carrying out operation which is not approved by *Shariah*; failure to carry on business after twelve months of registration.

the risk sharing in line with the principles and practice of Islam as against risk transfer in conventional insurance.[900]

Conventional insurance practice in Nigeria has been largely controversial. The industry has faced great challenges in its attempt to rev-up the critical insurance sector and make it bullish. It has been accused of serving only the elite and those formally employed. It contributes a paltry 0.72% to the country's GDP. Again, conventional insurance is largely focused on non-life insurance products for corporate businesses, particularly the oil and gas industry, and has been relatively slow to innovate and meet the challenges of expanding the market to cover insurance products that are of interest to the low-income segment of the Nigerian population.[901]

Before the advent of the *Takaful* Guidelines, there has been some form of low level *Takaful* insurance practice in Nigeria. The African Alliance Insurance Company Limited, being the oldest and strongest life insurance and pension office, blazed the trail in introducing Islamic insurance (*Takaful*) into the market in 2003.[902] Since then other two conventional insurance companies have joined the fray. These are Niger Insurance Plc and Cornerstone Insurance Plc. As a composite insurance company, Niger Insurance Plc transacts all classes of insurance business and offers a wide range of innovative products and customer-oriented services to its growing clientele.[903] In addition, they support their products with one of the most efficient and constantly improving claims settlement procedures in the insurance market.

[900] Fola Daniel, former Commissioner NAICOM said '' *Takaful* is not a product, it is a concept. It is not about religion really. It is about a way of sharing risks and not transferring risks. *Takaful* is a kind of community risk sharing, it is fantastic, people will take it. It does not matter whether they are Christians or Muslims''.
He stated further that ''…rather than allowing people to see Islamic insurance as being designed only for the Muslim population, Christians and any other person would patronize *Takaful* insurance products by the time they understand what *Takaful* is all about and that it has a prospect of returning part of their premium at the end of the year, many people will buy into it, it is not about religion, it is about a way of sharing risks''.

[901] See generally, Dias, D., et al, (2013), *Towards Inclusive Insurance in Nigeria: An Analysis of the Market and Regulations,* Eschborn.

[902] Yusuf, T.O., (2012), Prospects of *Takaful*'s (Islamic insurance) Contributions to the Nigerian Economy, *Journal of Finance and Investment Analysis,* Vol. 1, No. 3, p.217-230, ISSN: 2241-0988.

[903] Yusuf, T.O., *op cit.*

However, as laudable as the objectives of *Takaful* are, what remains critical to the realization of these financial inclusion objectives is overcoming the plethora of challenges that confront this trending form of insurance often referred to as ''insurance with a human face''. There are general, specific and regulatory challenges that abound which, if not handled properly and in time, will surely act to the detriment of the teeming populace who have waited patiently and for so long for this financial inclusion opportunity.

The Nigerian Vision 2020 Project[904] describes the insurance sector as an ocean of 'grossly untapped opportunities'. The insurance sector's contribution to Nigerian GDP stands at a paltry 0. 72% which is quite insignificant when compared to that of South Africa which in way back 2011 accounted for 16% of that country's GDP.[905] As mentioned earlier in the second chapter of this study, there are only about 800,000 Nigerians with any form of policy cover out of a population of over 150 million. This is dismal. This puts it at less than 1% of the adult population that has insurance policy which is far lower than in many developing countries such as Philippines where insurance covers about 7% of the population.[906]

Part of the problems identified by the NAICOM diagnostic study[907] on insurance, which is in tandem with the objectives of this study, was that the current regulatory framework of insurance in Nigeria is not adequate for the development of micro insurance and *Takaful* to full potential. The study found that the current rules include high entry requirement and operating minimum standard and excessive regulatory reporting which were not developed to meet the peculiarities of *Takaful* operations.

[904] A comprehensive and ambitious developmental project geared towards the rapid socio-economic and infrastructural advancement of Nigeria, launched by the late Head of State, General Sani Abacha in 1998.
[905] Sigma World Insurance Report 2011, Swiss Re.
[906] NAICOM/Access to Insurance Initiative Report, *Towards Inclusive Insurance in Nigeria*, Eschborn 2013, p. 27.
[907] *Ibid.*

This study posits that considering the challenges and opportunities posed by regulation of the insurance industry and the specific business needs of *Takaful* operations in Nigeria, there will be need for a more enabling regulatory framework in addition to a more strict minimum consumer protection and market conduct standards that are effectively enforced. This will no doubt serve to protect the *Takaful* operators while at the same time protecting policyholders.

As mentioned earlier in the previous chapters, there are numerous conflicts in the regulatory provisions of insurance in Nigeria thereby militating against the growth of the industry. These conventional regulations are bound to clash with the provisions of the Guidelines on *Takaful* operations. Such conflicts will surely be tested in the courts of law in the years to come because *Takaful* is quite different from conventional insurance. However, as long as there are no activist-minded judges who will tackle these conflicting issues headlong, the best option is for an amendment of existing legislation to harmonize the conflicting laws or to enact an entirely new legislation specifically for *Takaful.*

This chapter discusses the issue of challenges to *Takaful* practices in Nigeria from the general and specific regulatory perspectives. Since *Takaful* is a global concept, challenges to its application in other jurisdictions are referred to while at the same time linking the challenges to local situation.

It is a curious thing to note that the Nigerian Insurance Act makes no express mention of *Takaful* insurance in its provisions.[908] This absence of mention in insurance

[908] Section 1 Insurance Act 2003, Laws of the Federation of Nigeria (LFN). It provides thus:
'' This Act applies to all insurance businesses and insurers, other than insurance business carried on or by insurers of the following description –
(a) a friendly society that is an association of persons established with no share for the purposes of aiding its members or their dependants where such association does not employ any person whose main occupation-
(i) is the canvassing of other persons to become members of the association;
(ii) is the collecting of contributions or subscriptions towards the funds of the association from its members; or
(b) a company or any other body (whether corporate or unincorporated) or person whose business is established outside Nigeria, engaged solely in reinsurance transactions with an insurer authorized or pursuant to the provisions of this Act to carry on any class of insurance business, but not otherwise however''.

legislation[909] is a fundamental lacuna. *Takaful* is alluded to only by inference. For a concept that has gained so much recognition and momentum, it is an affront to be taken with so much levity.[910] The implication of this oversight portends grave consequences in the course of applying *Takaful* in Nigeria over time. The thrust of this study highlights this anomaly with a view to making recommendation for statutory and regulatory harmonization and possible legislative safeguard because *Takaful* is so important that it needs to be engrained in the statutes.

5.2 GENERAL CHALLENGES

5.2.1 General Awareness

One of the major obstacles identified in the universal fight against the prevalence of financial exclusion is the lack of financial literacy among the populace. In Nigeria, for example, the percentage of those who can read and write is so embarrassingly low not to talk of those who are financially literate. There is financial illiteracy even among the educated percentage. The observed gap in financial literacy is especially wide among women and of course the less educated segment of the society. Therefore, it is evident that people often lack the ability to save and manage their little earnings for effective personal financial decisions.[911] For instance, lack of financial education leads many people to erroneously understand insurance as something that can only be done where there is disposable income. This idea forms the basic understanding on risk and the need for mitigating it among many people.[912] Perhaps, in order to improve on the issue of

[909] Yusuf, T. O. & Babalola, A.R., (2015), *Takaful* in Nigeria: Penetration, Challenges and Way Forward

[910] To compound the problem of non-legislative express mention of Islamic insurance or *Takaful*, there is no plausible excuse that can convince a discerning mind on this monumental legal gaff since Decree No. 40 0f 1988 had recognized Islamic insurance in its provisions. Moreover, some companies like African Alliance Company and Cornerstone Insurance Co. have been operating *Takaful* windows in Nigeria before the advent of the 2003 Insurance Act so where did the companies derive the authority to offer *Takaful* services?

[911] Kollere, A.U., (2014) *op cit*, p. 1.

[912] See Kollere, A.U., (2014) *op cit*, p. 1.Generally, there is low awareness and trust in insurance. Many Nigerians are wary of the concept because of distrust in how businesses traditionally operate in Nigeria. Some Nigerians have knowledge mainly with respect to health and motor insurance. Motor insurance is compulsory so the level of knowledge about it is higher. However, most people only have third party liability insurance. Among these, some Nigerians believe insurance is good, yet do not engage in it as they consider it too expensive. Among some Nigerians who are aware of insurance, many of them do not seem to believe that products are good or necessary which once again indicates the lack of understanding and the lack of value the current products offer. See Dias, D., et al, (2013), *Towards Inclusive Insurance in Nigeria: An Analysis of the Market and Regulations,* Eschborn.

financial literacy, the Organization for Economic Co-operation and Development (OECD) initiated a project in 2003 to develop common financial literacy principles that will serve the needs for global financial education.[913] Many other countries have also identified their various financial education needs and have developed strategies towards closing these gaps. The key important areas that require proficiency in personal finance include savings, investment, tax, insurance and retirement among others.[914]

One of the biggest challenges facing the introduction of *Takaful* Guidelines in Nigeria is that of creating awareness. The issue of awareness is so fundamental that it could singlehandedly destroy all the good work done to bring about *Takaful* insurance in the country. There must be high level customer awareness for *Takaful* and its products if it is to thrive. Many Muslims still live under the misconception that *Takaful* is contrary to the principles of Islam, particularly with regards to ''life protection.'' People have to be made aware that *Takaful* provides an acceptable religiously validated solution[915] to the issue of insurance. In view of Nigerians' conventional insurance industry distrust, building the appropriate culture of honesty and sincerity would assist in creating positive customer awareness about *Takaful* products in Nigeria.

Other misconceptions about *Takaful* include:

(1) Risk protection is against *Tawakkal*, i.e., total dependence upon Allaah SWT.;

(2) All risk protection are equivalent with insurance, and therefore, it is prohibited (Haram);

(3) All insurance is a form of gambling or wagering, which is forbidden in Islam;

(4) All insurers are maximizing profit which takes benefits away from policyholders;

[913] Kollere, A.U., op cit, p. 1.
[914] *Ibid.*
[915] Ismail, E., (2011), *Basic Takaful Broking Handbook: Course Manual for Basic Certification Course in Takaful Broking (BCCTB)*, IBFIM, Kuala Lumpur, p. 126.

(5) All *Takaful* operators' nature of businesses is the same as conventional insurance companies.[916]

Still on the misconceptions, it has been stated that *Takaful* contains elements of *Riba*, *Gharar* and *Maysir* where it is associated with risks and uncertainties in a contractual agreement. In *Takaful*, the customer is paying a certain amount of money (premium) for the protection of life, whereas in real life, there is the uncertainty of life and death.[917]

However, it is posited that this perception is wrong since the subject matter of *Takaful* is dealing with life or property (on which the risk is presumed to occur in future), and not the exact time of death of a certain individual or the exact time of the damage done to the property. It is also wrong to claim that there exists an element of *Maysir* in which the aim is for a chance to gain material wealth while beating the other gamblers at the same time.[918]

Opponents argue that *Maysir* exists in the case of life insurance, when the sum paid out by the insurer in the event the insured dies during the earlier period of the contract, exceeds what the insured has paid in premiums. Another argument against *Takaful* is that policy money is paid together with bonuses and dividends. In the case of non-life insurance, the insured will recover more than what he has paid out as premiums in the event he suffers great loss over the insured property.[919]

This is untrue because the payment for the policyholder (in the case of early death or early termination) is from the social contribution provided by other policyholders based on the concept of *Tabarru'*. The *Takaful* concept deals with pure risk and not the speculative one. Thus, *Maysir* cannot be associated with *Takaful* since the element of

[916] Ahmad, R. & Auzzir, Z.A., (2009), *Takaful, The 21st Century Insurance Innovation*, McGraw-Hill Malaysia Sdn Bhd, p. 18.
[917] Hassan, R., (2011), *Islamic Banking and Takaful*, Pearson Custom Publishing, Malaysia Sdn Bhd, p. 187.
[918] *Ibid*, p. 187.
[919] *Ibid.*

risk that exists in *Maysir* is not a pure risk but instead creates new unnecessary speculative risks.[920]

Again, it has been stated that *Takaful* is contrary to the principles of *Mirath* (succession) and *Wasiyyah* (will). This is because in life insurance, or *Takaful*, the nominee is the absolute beneficiary from the policy after the death of the insured. This will deprive the rights of the legal heirs based on the principles of inheritance (*Mirath*) and will (*Wasiyyah*). This contention is contradictory. This is because the nomination of the nominee in the policy as an absolute beneficiary is not a right conferred by insurance law. Instead, it is a right conferred by the contract with the insurer and can therefore be easily removed or modified without affecting the validity of the contract of the life insurance itself. A nominee named in the insurance policy is no more than a trustee who is under an obligation to receive the benefits from the policy on behalf of the heirs of the insured (deceased) and distribute the benefits.[921]

Another misconception is that *Takaful* is contrary to the principle of *Tawakkal*. The opponents' argument is based on the fact that the insured puts a trust in the insurer to protect him against unexpected loss instead of putting the trust in Allaah.[922] This can be rebutted by understanding the real concept of *Tawakkal*, whereby one does his best to protect the risk and hope afterwards for the best by putting trust in God and His blessings. As *Takaful* is protection against the occurrence of loss, initiative or effort to the best of the insured's ability to overcome future unexpected difficulties is highly encouraged. This may be referred to a *Hadith* of the Prophet pbuh:

> ''One day, the Prophet pbuh saw a Bedouin leaving his camel untended and asked the Bedouin, why don't you tie down your camel? The Bedouin answered

[920] Hassan, R., *op cit*, p. 187.
[921] *Amtul Habib v. Musarrat Parveen* (1974) PLD 185 (SC)
[922] Some religious people may approach risk in varying degrees stating that ''God will take care of things''. In such cases, insurance (including *Takaful*) has no appeal and would not work without awareness and sensitization efforts. Nothing will improve awareness and subsequent demand for insurance more than improved market practices where claims procedures are significantly enhanced.

that ''I put my trust in Allaah''. The Prophet pbuh said, tie your camel first then put your trust in Allaah.''[923]

In a nutshell, the general misconception about insurance or *Takaful* to insure one's life against death or insuring one's wealth and property is unfounded. The argument put forward by opponents is based on the fact that no one can insure life except God. They further argue that insuring or protecting wealth is only allowed in three situations; fear for unjust enrichment, fear of losing property and fear of property being destroyed. In *Takaful*, the protection is given in all situations provided that the risk is an identified risk.[924]

It needs to be reiterated that non-Muslims need to be made aware of why *Takaful* is ethical. This is very important to ensure the public, as a whole, has the right perception towards *Takaful* industry. Without such knowledge, it is very difficult to penetrate into the market not only among the Muslims, but also towards non-Muslims. Hence, effective steps need to be taken to educate the public to understand what *Takaful* is all about. More public talks, seminars, forum, discussions, articles published in the media,[925] rallies in market places which is quite effective in Nigeria, engaging religious and traditional leaders to talk to their followers and subjects, jingles on radio and television, drama presentations etc are necessary to achieve this very noble purpose.

The Nigerian *Takaful* industry must be very careful not to toe the line of conventional insurance practice which has been nothing but dismal over the years. In spite of its sophistication, this system of insurance has not lived up to its billing in the purpose the insurance industry was set out to achieve. Contrary to expectations, the conventional

[923] There are also numerous Hadiths on the concept of *Tawakkal* whereby in one instance, the Prophet pbuh commanded his companions to migrate to Madinah by batches instead of moving in one large group. Also there was an instance where he put on his armour instead of wearing light clothing during the war. The Prophet pbuh knows and trusts Allaah best but he took precautionary measures.
[924] Hassan, R., *op cit*, p. 189.
[925] Ismail, E. (2011), *Basic Takaful Broking Handbook: Course Manual for Basic Certification Course in Takaful Broking (BCCTB)*, IBFIM Kuala Lumpur, p. 127.

insurance industry in Nigeria has only succeeded in creating an endemic gap which is becoming too difficult to fill because of low level patronage. It is disheartening to note that the insurance industry which ought to be a growth sector is struggling and stagnant despite the vast potential existing in the country. Several factors have been identified as reasons for the unimpressive performance. These include the twin problems of lack of public awareness for insurance and the absence of public confidence in the system.[926] These are pitfalls *Takaful* must seek to avoid. The conventional insurance sector has continued to face crisis of confidence, as the insuring public continues to hold insurance with contempt. Today, the average insurer in Nigeria is perceived by the insuring public as eager to collect premium only to repudiate claims at the slightest opportunity[927].

General awareness in Nigeria about actuaries and other professionals is a major militating factor against the growth of insurance. The crucial block in building a robust insurance market is the availability of a reliable cadre of insurance professionals in the field of actuaries, accountants, underwriters, agents and loss adjusters. One of the challenges in the way of seamless integration of *Takaful* into the wider insurance industry is the lack of awareness even among the various stakeholders in the insurance industry. *Takaful* providers must have in-depth skills in the technical, operational, legal and *Shari'ah* compliant requirements for *Takaful* operations.[928] The lessons of recent global financial crises bring about the compelling need for *Takaful* operators to have in place robust risk management and corporate governance structure. In line with this concern, the National Insurance Commission of Nigeria must ensure that the applicant of a *Takaful* license must have appropriate risk management and corporate governance

[926] Dateline Insurance Magazine, (2013), vol. 3 no. 3, July/August, p. 5.
[927] *Ibid.* Several insurance companies attribute mistrust to too many co-insurance arrangements (these are agreements by several companies to share a large account), poor record of paying claims or too many obstructions in the claims procedures e.g. frauds in the form of fake insurance agents and fake insurance.
[928] Adamu, A.I., *op cit*, p. 136.

policies to serve their customers' needs as well as adequate assurances to dispel misconceptions about insurance to foster the acceptance of *Takaful.*[929]

The insurance industry in Nigeria is faced with the problem of skills in the field of certified actuaries. This has resulted in dearth of technical skills towards the evaluation of risk thereby weakening the supervisor's ability to monitor reserves, pricing adequacy and solvency of the regulated companies. The cost effective solution identified by this study for building actuarial capacity in the insurance industry is the need for massive and continued education of university undergraduates and graduates with the collaboration of local and foreign partners. It is also paramount to integrate all requisite fields of competence within the training curriculum of CIIN to encourage professional certification for the development of the insurance industry in Nigeria.[930]

In this regard, other key stakeholders in the operations of the insurance industry such as rating agencies and standard setting bodies should be carried along in the drive toward towards the integration of *Takaful* into mainstream insurance practice in Nigeria. All these stakeholders need to be sensitized to ensure that standards set are to meet customers' demands in a most cost-effective manner.

5.2.2 Meeting Public Expectations

The next challenge for *Takaful* as a new player in the insurance industry is meeting expectations. Drawing from the Malaysian experience, Malaysia like Nigeria, is practicing dual banking and insurance system i.e. conventional as well as Islamic banking/*Takaful* which run parallel to each other. The financial strength, stability and standards of conventional insurers are well established and already well known. These conventional insurers have been in the industry for many years and their service levels

[929] Adamu, A.I., *op cit*, p. 136.
[930] *Ibid.* Shortage of expertise in the *Takaful* sector has led some *Takaful* operators to hire from conventional insurance staff pool. The shortage of expertise in the *Takaful* sector, lack of actuaries with *Takaful* knowledge, and a mindset stuck in the broker-agent model that caters to corporate accounts impede *Takaful* to develop and reach scale and sustainability.

are perceived as better than those of *Takaful* operators. Thus there is need to overcome negative perceptions of *Takaful* and prove to the market that its operators are capable of providing competitive services that are on par with other or better than conventional insurance companies.[931]

In terms of product availability, the *Takaful* operator must be able to identify and select the most saleable product for them to promote more aggressively. For example, products that would help to improve savings among the masses, such as family *Takaful* plans which are essential components for ensuring economic growth should be actively promoted.[932]

5.2.3 Dearth of Expertise/Human Resources[933]

The potential for *Takaful* worldwide and in Nigeria in particular is enormous; however, several hurdles must be overcome for the market to actualize this potential. Dearth of expertise and inadequate human resources pose major obstacles to *Takaful* growth, as the market faces severe shortage of qualified staff that have adequate knowledge and experience about *Takaful*, as well as understanding of *Shari'ah* finance in Nigeria. It is envisaged that the large unemployed and willing populace are ready to learn about Islamic finance.[934] This constitutes ready manpower for Nigeria's *Takaful* market. This implies that *Takaful* operators need to allocate funds specifically for human resources development.[935]

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[931] Ismail, E., *op cit*, p. 127.
[932] *Ibid.* For this reason, existing as well as the new potential operators must intelligently position themselves in terms of service and product design that can satisfy the needs of the market. They must be willing to invest in the IT system to ensure that their services are fully automated with minimal human intervention to maintain a high level of information integrity.
[933] Human resources is the set of individuals who make up the workforce of an organization, business sector, or economy. ''Human capital'' is sometimes used synonymously with human resources, although human capital typically refers to a more narrow view (i.e., the knowledge the individuals embody and economic growth). Likewise other terms sometimes used include ''manpower'', ''talent'', ''labour'', or simply people. See https://en.m.wikepedia.org/wiki/Human_resources.
[934] Fadun, O.S., (2014), *Takaful* (Islamic Insurance) Practices: Challenges and Prospects in Nigeria, *Journal of Insurance Law & Practice*, Vol. 4 No. 2, p. 21.
[935] *Ibid.*

It is submitted that the dearth of human resources is a critical challenge that will be inimical to the survival or rapid growth of the *Takaful* industry if not properly addressed because the industry needs persons that are well versed in order to facilitate its expansion in a more cohesive manner. This very important industry is facing a severe shortage of qualified staff who understand both the technical insurance principles coupled with adequate awareness of *Shariah*. The case of Nigeria is even worse due to the low level

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Being part of the service industry, the pace of progression for *Takaful* would to a great extent depend upon its manpower and competency of its human resources. Lacking of trained and experienced manpower would hinder the development of *Takaful*. At present, the developing countries in general, of which, most of the Islamic countries fall within the category, are facing scarcity of qualified and trained professionals in the field of insurance. For this reason, *Takaful* is also affected in view of the fact that experienced conventional insurance personnel at present form the core staff for most *Takaful* operators.[936]

The constant need to identify qualified *Takaful* talents has forced operators to recruit personnel from conventional insurers, and retrain them to take up the *Takaful* challenge. But this will involve spending considerable amount of money and time to retrain them on the differences between both concepts.[937]

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[936] Ismail E., *op cit*, p. 128.

[937] *Ibid.* For *Takaful* to succeed in Nigeria and the world in general, special programmes should be initiated to train the manpower not only on the technical aspects of insurance but also in areas covering finance and investment as well as the appreciation of

As daunting as these challenges are, solutions have been proposed which seem to be working out effectively. On this note, it is wise to borrow a leaf from the experiences of the number one *Takaful* nation in the world in dealing with those challenges mentioned earlier.

Malaysia has begun to play its leading role by organising and conducting special educational programmes for *Takaful* personnel through the formation of Bank Islam Research and Training Institute (BIRT) which is now known as Islamic Banking and Finance Institute Malaysia (IBFIM) to train more professionals in the *Takaful* discipline. Besides, the International Centre for Education in Islamic Finance (INCEIF) has been set up to develop more professionals and specialists in Islamic finance including *Takaful*. Apart from that local universities are now offering courses in Islamic finance at all levels including PhDs.[938] Bahrain is also another country that Nigeria and the rest of the world can take a cue from in surmounting challenges facing *Takaful* industry. Bahrain's Islamic Finance and Banking Training also offers courses targeted at financial industry experts that cover applications of key Islamic banking and financial instruments.

5.2.4 Uniform *Shari'ah* Interpretations and Guidelines

The non-existence of uniform terminologies and the degree of unresolved *Fiqh* issues is more serious in the *Takaful* segment than in any other segment of the Islamic finance industry. This is a universal problem that affects the whole Muslim *Ummah* (community) and is not limited to new entrants into the *Takaful* industry like Nigeria.

Shari'ah. On a personal experience, even trained legal practitioners sometimes find it difficult to grapple with the intricacies of insurance. Many lawyers shy away from insurance because of this. It is bound to be difficult also for non-Muslim personnel to fully understand and appreciate *Shari'ah* law. To most, *Shari'ah* appears incongruent and inflexible. However, it needs to be stated that there are some who have exhibited remarkable understanding and appreciation of *Shari'ah* principles and have gone ahead to show some Muslims the way on complex *Takaful* issues.

[938] *Ibid.* In Nigeria, the Chartered Insurance Institute of Nigeria (CIIN) has taken giant strides towards the training of insurance personnel. There is also the West African Insurance Institute of which Nigeria actively contributes towards the training of the much needed insurance manpower. However, what remains critical is the training of personnel that are specific to *Takaful* insurance matters as the two insurance systems are fundamentally different.

Islamic jurisprudence or *Fiqh* in Arabic is divided into two parts: the study of the sources and methodology (*Usul-al-Fiqh*) or roots of the law and the practical roots (*Furu'-al-Fiqh*) or branches of the law. It was only during the second Islamic century that important developments took place in the field of *Usul-al-Fiqh*. During the Prophet's pbuh lifetime, the guidelines and solutions to problems were obtained either through divine guidance or through his direct rulings. Following his death, his companions remained in close contact with the Prophet's pbuh teachings and their decisions were inspired by precedents. Their proximity and intimate knowledge of most events and sayings of the Prophet pbuh provided them with the authority to rule on practical issues without being in need for a methodology.[939]

However, with the regional expansion of Islam a change was needed to avoid and counter misunderstandings and misinterpretations.

When confronted with a legal issue the first reference for any Islamic scholar is the Qur'an. If no concrete answer on a particular legal issue can be found, the *Sunnah* is considered next. If no ruling is found in the divine sources, the *Ijma* or consensus of the Imam *Mujtahids* (those who do *Ijtihad* i.e. independent judgement) is referred to. If there is none, then one does *Ijtihad* to come up with a ruling based on *Qiyas*, i.e. individual reasoning based on analogy. The outcome is a religious ruling or *Fatwa* (Decree) which becomes part of the *Shari'ah*. The *Shari'ah* can thus be considered as a kind of case law.[940]

A pluralism of cases or *Fatwas*, sometimes even contradicting each other, is an integral component of Islamic law. It should be noted that such interpretations can vary widely

[939] Frenz, T. & Soualhi, Y., (2010), *Takaful & ReTakaful: Advanced Principles and Practices*, IBFIM/Munich Re, Malaysia, p. 25. The IMF said Islamic finance has the potential to contribute to the global economy, promising to foster greater financial inclusion, especially of large underserved Muslim population. It further reiterated the fact that although Islamic regulatory bodies have established standards, different interpretations of religious texts and weak implementation mean they lack harmonization. Such differences must be resolved or reduced to the barest tolerable minimum. Copyright AFP (Agency France Press), 2015, accessed on Tuesday, 7th April, 2015.

[940] Frenz, T. & Soualhi, Y., *op cit*, p.25.

amongst scholars or schools of thought and a *Fatwa* does not automatically become applicable to all Muslims in the world[941]. *Fatwas* can be derived from the primary sources, i.e. Qur'an and the *Sunnah* or from the secondary sources such as *Qiyas* (analogy), *Masalih al-Mursalah* (public interest) and *'Urf* (custom).[942]

An important issue in *Usul-al-Fiqh* is how to interpret the primary sources of Islam, the Qur'an and the *Sunnah*. This requires a deep understanding of both the Qur'an and the *Sunnah*. Naturally, a scholar who wants to interpret the primary sources at any level (in depth or otherwise) would also require a deep understanding of Arabic. As explained earlier, interpretation is not normally attempted if the Qur'anic text itself is self-evident. However, the greater part of *Fiqh* is derived through interpretation, as most of the legal texts are not self-evident. It is important to note that in the process of deducing legal rulings or decreeing *Fatwas*, both the letter and the spirit of the revealed texts must be adduced and relied upon. Relying on the letter of the text only would result in rigid rules being promulgated, and the reliance on the mere spirit of the text would result in the rationalization of the entire teachings of *Shari'ah* including the definitive principles of *Shari'ah* that are meant to remain unchanged.[943]

Previously, there were no specific *Shari'ah* guidelines on even very basic issues. The *Fiqhi* views differ widely, often challenging even the basic concept of *Takaful* because they cannot find its express basis in the Qur'an or *Sunnah*. However, the first international conference on Islamic economics held in Makkah in 1976 and the *Fiqh*

[941] However, it must be noted that it was the *Fatwa* of the Islamic *Fiqh* Academy in 1406 after *Hijra* which corresponds to 1985 that gave global impetus to *Takaful* as it stands today. The *Fatwa* stated that ''commercial insurance contract, which earns fixed premium as practiced by commercial insurance companies, involves significant *Gharar* that makes the contract null and void. This form of transaction is prohibited''. The same resolution of the Academy allows cooperative insurance that is based on the principle of donation and cooperation. The resolution stated that ''the alternative contract that observes principles of Islamic transactions is the cooperative insurance which operates on the basis of donation and cooperation. The same rule applies to the reinsurance protection that is based on cooperative insurance''. It is this type of cooperative unity in the acceptance of the *Fiqh* Academy resolution on *Takaful* that is needed at all times to sustain the practice of *Takaful* globally.

[942] Frenz, T. & Soualhi, Y., *op cit.*

[943] *Ibid.* See also the statement of Dato' Abdul Hamid Bin Haji Mohamad, former Chief Justice, Federal Court of Malaysia in Foreword message in Essential Readings in Islamic Finance, Bakar, M.D. & Ali E.R.A.E. (eds), *op cit*, where he said ''the other point I observe is that the creation of an Islamic product and the determination of the *Shari'ah*-compliance of a product is much more difficult exercise than determining the legal status under Islamic law as in other matters. It is not just a matter of knowing the relevant verses of the Al-Qur'an or Hadiths or the ability to read the *Fiqh* books in Arabic. What is more difficult is to understand the intricacies of the product before the relevant law (*Shari'ah*) can be applied. Applying the right law to the wrongly perceived facts will lead to a wrong ruling. Knowledge of the mechanism of the product is of utmost importance''.

Academy of the Organization of Islamic Conference (OIC) meeting in 1985 resolved that conventional insurance was not *Shari'ah* compliant[944] and that *Takaful* was the alternative. Muslim jurists have acknowledged that the benefits of insurance outweigh its defects, therefore clearly exceeding its disadvantages and unfairness. An insurance system that addresses the problems of *Gharar, Maysir* and *Riba*, therefore, is much desired by the Muslim communities.[945]

It should be noted that any social devices to help individuals in financial hardship is not contradictory to Islamic tenets. *Shari'ah* is concerned with human welfare, justice and equity. *Maslaha* or public interest has always been the utmost priority of Islam. An arrangement similar to insurance should be encouraged in the society because it promotes co-operation, shared responsibility, mutual protection and solidarity[946]. The views of those questioning the validity of *Takaful* due to lack of express texts in the Qur'an should be discountenanced.

Malaysia will always remain an important player in spearheading *Fiqhi* expositions in Islamic finance. The regulator, Bank Negara Malaysia (BNM), has made a lot of initiatives to ensure *Takaful* business can expand by providing such rules and regulations.[947] Nigeria must do well to draw from these Malaysian initiatives and in doing so become the hub of *Takaful* industry in Africa. In Malaysia, currently, there is an association of *Takaful* operators known as Malaysian *Takaful* Association (MTA), for the players to come together to discuss and resolve whatever issues that may arise. MTA always provides a common platform for the *Takaful* operators to address the

[944] Yusof, M.F., *op cit* . Also Rashid, S.K., *op cit.*
[945] Rahman, Z.A. & Redzuan, H., *op cit*, p. 21.
[946] *Ibid.*
[947] After almost three decades of the Malaysian *Takaful* Act, 1984, regulating *Takaful* operations in Malaysia, the Government of Malaysia introduced a new legislation to rectify the weaknesses and cover the loopholes of the TA 1984. With emphasis on *Shariah* compliance, the Islamic Financial Services Act (IFSA), 2013, it is hoped will provide sufficient regulatory requirements on *Shariah* aspects and thus public confidence in Islamic finance industry in Malaysia will be improved together with the increase in Islamic awareness amongst the public. The impact of IFSA, 2013 is wide-ranging. The IFSA 2013 not only affects the Board of Directors, *Shariah* Committee and management officers of the operators as a whole, but also modifies the operational aspects of *Takaful* operation, including the corporate structure, product management, underwriting, sales, marketing and claims. See Abd Hamid, M.H. & Hassan, R., (2014), Islamic Financial Services Act 2013: A Preliminary Note on its Impact to *Takaful* Industry, 2 *Malaysian Law Journal*, p. lxv.

issues and interests of the *Takaful* industry.[948] This is remarkable. For the Nigerian *Takaful* industry to thrive, it is suggested that more active participation is required from the industry players to ensure that their voices are heard. This will pave the way for the desired success and progress.

Secondary sources are equally important in *Shari'ah* interpretations. Secondary sources are those derived from the divine sources. To allow secondary sources as a method for deriving new rulings is often traced back to a well-known Hadith on a discussion between the Prophet pbuh and Mu'adh Ibn Jabal, who was appointed the judge in Yemen:

> Prophet pbuh: ''According to what will you judge?''
>
> Mu'adh: According to the Book of Allaah''
>
> Prophet pbuh: ''And if you find nothing therein?''
>
> Mu'adh: ''According to the *Sunnah* of the Prophet pbuh''
>
> Prophet pbuh: ''And if you find nothing therein?''
>
> Mu'adh: ''Then I will exert myself to form my own judgement.''[949]

Sometimes also those derived via *Ijma'* and *Qiyas* are considered primary. Qur'an, *Sunnah, Ijma'* and *Qiyas* are also called the agreeable sources of *Shari'ah* because all schools of Islamic jurisprudence have agreed on their authority.[950]

Other sources such as *Istihsan, Maslahah* and *'Urf* are normally called the disputable sources of *Shari'ah* because not all schools of Islamic jurisprudence would adopt them

[948] Ismail, E., *op cit*, p. 129.
[949] Sahih Bukhari.
[950] Frenz, T. & Soualhi, Y., *op cit*, p. 26. These agreeable sources of the *Shari'ah* are unanimous in upholding that there are five hundred verses in the Noble Qur'an which deal with legal sanctions. There are indeed a number of Divine injunctions in the Noble Qur'an which justify the validity of an insurance contract. The contract of insurance contains the elements of mutual co-operation as provided for by the Qur'an in the following verse ''help one another in furthering virtue and God Consciousness (*Taqwa*), and do not help one another in furthering evil and enmity (5:2). It is such unity in acceptance of fundamental rulings that the *Takaful* industry yearns for to scale sustainability

as valid sources of *Shari'ah*. The various schools of Muslim jurisprudence differ on the number of methods to be used or emphasised, although all of them include the Qur'an, the *Sunnah, Ijma'* and *Qiyas*, except the *Zahiri* school of jurisprudence. The latter is referred to as literalists as they only accept the literal meaning of the divine sources (Qur'an and *Sunnah*) and disregard secondary sources.[951]

Different schools of juristic interpretation or (*Madhab-al-Fiqh*) of the Qur'an and *Sunnah* developed over time. Four mainstream schools were finally formed in Sunni Islam, each offering a rationalized version of the sources and differing only in emphasis and details. The four schools are Hanafi, Shafi'i, Maliki and Hanbali. The majority of Sunni Muslims believe that all four schools give ''correct guidance'', and the differences between them lie not in the fundamentals of faith, but in finer judgements and jurisprudence, which are a result of the independent reasoning of the imams and the scholars who followed them. As their individual methodologies of interpretation and extraction from the primary sources have been different, they have come to different judgements on particular matters.[952]

Global standardization on certain economic matters is proving to be challenging due to the different interpretations. For example, there is dispute concerning the distribution of underwriting surplus of an Islamic insurance company. There is disagreement between scholars as to whether *Takaful* operators can share in the underwriting surplus or not. Many scholars in the Gulf region object whilst others, e.g. in parts of Southeast Asia, approve this practice.[953]

[951] Frenz, T. & Soualhi, Y., *op cit*, p. 26.
[952] *Ibid.*
[953] *Ibid.* Global standardization on certain economic matters is proving to be challenging due to the different interpretations. For example, there is dispute concerning the distribution of underwriting surplus of an Islamic insurance company. There is disagreement between scholars as to whether *Takaful* operators can share in the underwriting surplus or not. Many scholars in the Gulf region object whilst others, e.g. in parts of Southeast Asia, approve this practice.

Differences in interpretation have been an obstacle to the progress of Islamic finance, in particular to cross-border transactions. *Takaful* is not immune to these challenges. These gaps need to be filled or narrowed in other to overcome the challenges.

5.2.5 Product Innovation and Services

The Nigerian *Takaful* market is a very young market. There is so much buzz in the country concerning the introduction of Islamic finance and *Takaful* insurance in particular. This goodwill being experienced needs to be sustained if the much talked about insurance penetration is to be realized. There is no better way to this than for the *Takaful* operators to always be a step ahead in terms of innovation of new products and service delivery. This is what endears a customer to be addicted.

It is obvious that the interaction of demand and supply will determine the consumption of *Takaful* in Nigeria and the world over. The shift in demand for *Takaful* will occur as it is an innovative product and suits the socio-economic and religious teachings of Islam. However, the major increase in the consumption of *Takaful* will result from the increase in the supply of *Takaful*. The demand already exists. The extent to which it is tapped would depend on the extent to which the supply curve moves to the right. In short, the *Takaful* industry must design new and innovative products that meet client and market expectations, failing which its growth will be stifled. This must be done at a faster rate.[954]

Takaful companies that grow rapidly (as has been seen in Malaysia) face the challenge of ensuring that the systems they have in place can cope with such rapid growth. Along with these challenges, *Takaful* providers must enhance their product innovation and

[954] Ismail, E., *op cit*, p. 130. Some writers opine that better business practices are likely to be more powerful than starting with education and information efforts in a bid to boost insurance awareness and participation. Some Nigerians stated that if claims were paid and premiums were affordable, those who understand the potential benefits would buy insurance. Increasing insurance knowledge would surely help the public's understanding, however, the insurance industry, making claims processes easier and designing products that meet the needs of the people would go a longer way in changing the perception of the industry and openness to insurance. Among those who are aware of insurance, a great number do not seem to believe that products are good or even necessary which once again indicates the lack of understanding and the lack of value many products offer. See generally, Dias, D., *op cit*, p. 47.

continue to offer a high level of customer service. They must be able to understand evolving customer and market-specific needs and be willing to renew or re-engineer product design and consumer benefit packages, as well as expand customer reach across various distribution channels.[955]

The basis of every business plan is an assessment of the market potential. The potential in Nigeria seems enormous considering the sheer size of the Muslim population, which is mostly un(der)insured, and it's favourable demographic profile with rather a young population. The dramatic growth of Islamic insurance in the world has increased awareness and demand. However, projections should be treated with caution as the application of *Takaful* in Nigeria is still at its infancy stage and there is little credible data available. It is fair to say that many *Takaful* projections have been too simplistic and too optimistic, and have ignored the effort required to actually tap the Muslim market.[956] This is what Nigerian *Takaful* industry must guard against.

Takaful operators are often in direct competition with conventional insurers as *Shariah* compliance might not be the sole reason for customers buying protection. Consumers expect *Takaful* operators to be on a par with conventional insurers in respect of product range, service level, financial security and value for money. However, *Takaful* is a relatively young and small market and achieving critical mass within a reasonably short period of time is difficult, but crucial for a better spread of risks and economies of scale. This is why Nigerian *Takaful* operators must also actively target non-Muslims going by the success rate in Malaysia.[957]

[955] Dias, D., *op cit*, p. 47. This is necessary as conventional insurers have been in business for years and their products and experiences are more obvious than those of *Takaful* operators. To overcome these challenges, wider range of *Takaful* products should be offered as an alternative to those offered by conventional insurers. Consequently, needs of lower income groups should be adequately addressed, as they constitute the greater majority of *Takaful* prospects.

[956] Frenz, T. & Soualhi, Y., *op cit*, p. 242.
The industry is largely nascent, lacking economies of scale and operating in an environment where legal and tax rules, financial infrastructure and access to financial safety nets and central bank liquidity are either absent or do not take its special characteristics into account, according to the IMF.

[957] *Ibid.*

With new *Takaful* operators comes increasing competition and this results in pressure on rates and terms, with the risk of under-pricing in order to win market share.[958]

The acceptance of Islamic savings, education, marriage and retirement plan is gradually growing among the affluent customer base in many jurisdictions. Thus, investment in customer education and training of financial planners and investment advisors is needed. A successful distribution model needs to develop a thorough understanding of customer needs, deliver on its promise, offer product and process innovation, eliminate flaws in product terms and enhance customer service delivery. The model should give priority to the understanding of the individual customer needs and concerns by conducting customer focus groups and surveys with its banks who are their distribution partners. Efficient product design, open investment architecture, customer convenience and transparency are some of the salient points which are reviewed carefully.[959]

Marketing of *Takaful* products is a huge challenge, particularly as *Takaful* seeks to expand its customer base. What was introduced as alternative for Muslims to perform *Takaful* insurance transactions, has now become the ''*Takaful* office next door''. Yet, one of the most common questions posed by non-Muslims to *Takaful* operators is ''is this only for Muslims?'' It is also not surprising to find that Muslims' uptake of *Takaful* products is quite low in many Muslim dominant countries, due to lack of awareness and product knowledge. These demonstrate the magnitude of the challenge for *Takaful* operators to attract and retain customers.[960]

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[958] Frenz, T. & Soualhi, Y., *op cit*, p. 242.
The IMF has warned that the challenges facing Islamic finance which includes *Takaful* insurance may not only be impeding its development, but could also encourage complex practices and products that carry heightened risks. Also affecting the industry are slow innovation of products and a scarcity of *Shari'ah* scholars with financial expertise. Copyright AFP (Agency France- Press) 2015, accessed on 7th April, 2015.

[959] Ismail, E., *op cit*, p. 130.

[960] Syed, A.M.S., (2008), *Islamic Banking: Trend, Development and Challenges, In Essential Readings in Islamic Finance*, Bakar, M.D. & Ali, E.R.E., (eds), *op cit*, p. 102.
''……rather than allowing people to see Islamic insurance as being designed only for the Muslim population, Christians and any other person would patronize *Takaful* insurance products by the time they understand what *Takaful* is all about and that it has a prospect of returning part of their premium at the end of the year, many people will buy into it. It is not about religion, it is about a way of sharing risks - per Fola Daniel, former Commissioner National Insurance Commission of Nigeria when launching *Takaful* Operation Guidelines in Abuja, Nigeria, March, 2013.

At the heart of the marketing efforts lie two basic objectives. The first is to demystify the operations of Islamic finance and clear the many misconceptions and common perceptions about Islam and Islamic finance. Secondly, the marketing effort must be focused to promote the value proposition of *Takaful.*[961]

Without educating the consumers of what *Takaful* is and how it really works, the consumers will keep shying away from *Takaful* insurance, thus resulting in a huge gap in the potential target market for *Takaful.*[962]

5.2.6 Information Technology[963]

This study submits that this is one area where the challenges of *Takaful* practice will be critically felt in Nigeria because of infrastructural underdevelopment. Power supply is largely epileptic and information technology is just slowly making its way into the Nigerian environment. There is a prevalence of poor communication network in most African countries and Nigeria's case is worse off. Years of neglect brought about by corruption have served to compound the woes of socio-economic underdevelopment.

It is common knowledge that we are now living in a world that has been totally transformed by immense technological advancement and change. This century has largely been significant in the history of humanity as a result of the technological revolution. Essentially, the age of this transformation revolves around the advancements made in telecommunication and information technology. These consist of the invention of hardware, software and media for collection, storage, processing, transmission,

[961] Syed, A.M.S., *op cit.*

[962] Fola Daniel, *op cit.* Some writers opine that better business practices are likely to be more powerful than starting with education and information efforts in a bid to boost insurance awareness and participation. Some Nigerians stated that if claims were paid and premiums were affordable, those who understand the potential benefits would buy insurance. Increasing insurance knowledge would surely help the public's understanding, however, the insurance industry, making claims processes easier and designing products that meet the needs of the people would go a longer way in changing the perception of the industry and openness to insurance. Among those who are aware of insurance, a great number do not seem to believe that products are good or even necessary which once again indicates the lack of understanding and the lack of value many products offer. See generally, Dias, D., *op cit,* p. 47.

[963] Information technology is the application of computers to store, retrieve, transmit and manipulate data, often in the context of a business or other enterprise. It is considered a subset of information and communications technology (ICT). The term is commonly used as a synonym for computers and computer works but it also encompasses other information distribution technologies such as television and telephones. See https://en.m.wikipedia.org/wiki/information_technology.

retrieval and presentation of information. They also include communication and computing equipment and programmes which include satellites, transmission lines, computers, modems, routers, the internet, intranet, email, wireless networks, cell phones and other operating systems and applications.

Wikipedia, the free online Encyclopaedia defines information technology as

> ''set of tools, processes, and methodologies (such as coding/programming, data communications, data conversion, storage and retrieval, systems analysis and design, systems control) and associated equipment employed to collect, process, and present information.''[964]

Indeed, information technology is:

> ''an umbrella term that includes all technologies for the manipulation and communication of information.''[965]

It is an undeniable and unalterable fact that information technology now affects every facet of human endeavour. In many ways, information communications technology has revolutionized the world and defined how we work, how we live, how we think and has launched the world on information superhighway.[966]

Technology has driven conventional insurance to the level of success it is enjoying today and there is no reason why same drive cannot be applied to *Takaful*. The phenomenal growth of the internet has transformed society tremendously and this has changed the way people communicate, exchange information, sell products etc. *Takaful* is no exception to this rule.[967]

[964] Wikipedia Online Free Encyclopaedia, http://en.wikipedia.org/wiki/information_technology
[965] Owoeye, J.E., (2011), Information Communications Technology (ICT): Used as a Predictor of Lawyers Productivity, Retrieved from: connection.ebscohost.com/c/articles/663325214/information….
[966] *Ibid.*
[967] Rahman, Z.A. & Redzuan, H., *op cit*, p. 84.

For a *Takaful* operator to succeed, it is essential that the segment provides services that are clear and transparent. Long term contracts in life *Takaful* need to deal with transactions over the life time of a contract, which can be as long as 40 or 50 years. Such facilities can only be assured where the level of technology implemented by the operator can provide the participant with assurances that his or her long term interest is protected. The speed of technological development in the *Takaful* segment must be matched by such developments in the general market place. As such, a good and efficient information system is required should the company wish to be at par with the rest of the players currently in the industry.[968]

In addition to technology risk, another type of risk is the IT operational risk, which is associated with the use of software and telecommunication systems that are not specifically tailored to the needs of *Takaful*. Terminologies, accounting treatment and profit computation and distribution methods are all serious issues which left unchecked could lead to disastrous implications and impact on the reputation and image, not to mention incurring legal risks for the *Takaful* operators.[969]

Nigeria has no choice but to vastly improve its information technology profile if it wants to get the best out *Takaful* insurance that has just taken-off. In a country with abundant oil wealth, it is such an embarrassment to see High Court judges taking procedural notes in shorthand and filing of cases are done manually. Recording systems in the courts are just being introduced in a few states.

[968] Ismail, E., *op cit*, p. 131.
[969] Syed, A.M.S., *op cit*, p. 104.

5.2.7 Re*Takaful*[970]

The challenge posed by re*Takaful* is a worldwide problem. The main problem generally, is the lack of re*Takaful* companies that are capitalized to the levels required by insurers and more particularly the lack of 'A' rated re*Takaful* companies. This has resulted in *Takaful* companies having to reinsure on a conventional basis, contrary to the preferred option of seeking cover on Islamic principles. The *Shariah* scholars have allowed dispensation to *Takaful* companies to reinsure on conventional basis so long as there is no re*Takaful* alternative available.[971]

However, the matter is not as simple as it appears because there are a lot of complex issues involved in the matter of re*Takaful* that have developed over the years which seem to negate the practice of *Takaful* operators taking up re*Takaful* with reinsurance companies.[972]

Re*Takaful*, which is ''*Takaful* for *Takaful* operators, is strictly based on *Shari'ah* principles. Re*Takaful* is a transaction whereby one company (the re*Takaful* operator) agrees to indemnify another *Takaful* company (the ceding company or cedant) against all or part of the loss that the latter sustains under *Takaful* contracts that it has issued. For this service, the ceding company pays the re*Takaful* operator a contribution.[973]

Re*Takaful* allows operators to share risks that they cannot, or do not wish, to absorb themselves. The main purpose of re*Takaful* is similar to that of reinsurance – to spread

[970] This is the same thing as conventional reinsurance once the *Shari'ah* prohibitive features are removed. However, there are many other fundamental differences occurring between the two practices as discussed further. See chapter four of the thesis. Conventional reinsurance companies enjoy unfettered monopoly here due to their vast experience and pristine presence in the industry. Many *Takaful* operators have no option but to patronize them for protection. This is a chain that has to be severed because of its dire consequences.

[971] Yassin, N. & Ramly, L., *op cit*, p.256.

[972] See Fadun, O.S., *op cit*, p. 23. The issue of re*Takaful* in the Nigerian insurance industry is bound to cause a lot of concern because the *Takaful* practice has just taken off. There must be a prevalence of many quality *Takaful* companies before re*Takaful* can be successfully undertaken. This is clearly lacking. However, since the market is still young and vibrant, it is submitted that adequate safeguards be put in place for re*Takaful* in anticipation of the rapid boom expected of the industry. It is recommended that *Takaful* operators should collaborate to establish a re*Takaful* facility or pool in Nigeria. This is beneficial, as it would enhance mutual cooperation among operators and minimize capital outflow from Nigeria. However, it is noted that it would be difficult for such re*Takaful* pool to survive in terms of business support without sufficient number of *Takaful* operators. Initially, the re*Takaful* can take-off by depending solely on cessions from i operators. The pool can be expanded subsequently, and possibly be registered as an independent re*Takaful* company in Nigeria in the nearest future.

[973] Frenz, T & Soualhi, Y., *op cit*, p. 263.

risk and add capacity so that larger or more risks can be written. By spreading risks within the *Takaful* industry, re*Takaful* enables the *Takaful* industry to function more efficiently.[974]

The global re*Takaful* market was very quiet until 2005 with only a few small active players, which were mostly taking a follower share in re*Takaful* arrangements, with the lead given to conventional reinsurers. However, the re*Takaful* market has gained momentum since then, in particular following the entry of multinational re*Takaful* operations like Munich Re's re*Takaful* unit with a financially very strong capital base and a wide network of offices.[975]

Prior to 2005, most *Takaful* operators primarily ceded to conventional reinsurers, and this was considered acceptable as long as there was no appropriate *Shari'ah* compliant alternative. This exemption was based on the *Darurah*[976] principle in *Shari'ah* that basically says that necessity allows what is prohibited.[977]

It is submitted that since the Nigerian *Takaful* industry is just coming to grips with the practice of Islamic insurance, the issue of re*Takaful* could be solved by adopting the *Darurah* principle for a limited period of time in order for *Takaful* operators have access to conventional reinsurance for the purpose of sharing risk. Once risks are spread and capacity added it follows that larger and more risks can be written. By spreading these risks within the Nigerian *Takaful* industry, this reinsurance will enable the young *Takaful* industry to function more efficiently.

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[974] See Frenz, T & Soualhi, Y., *op cit,* p. 263.This sounds very much like reinsurance, but the fundamental difference is that re*Takaful* is about sharing the risk, i.e. the risk is not transferred to the re*Takaful* operator. The re*Takaful* operator becomes a risk manager instead of a risk taker. This is a mirror of the relationship between a *Takaful* operator as agent and the *Takaful* participants as owners of the *Takaful* fund. The risk remains with the participants and by extension to re*Takaful* it implies that the risk remains with the ceding *Takaful* operator

[975] *Ibid.*

[976] *Darurah* – The rule ''necessities justify that which may be unlawful'' is an important principle that provides Muslims with guideline to bypass the impasse in practicing upon the principles of the *Shari'ah.* The rule continues to subsist as long as that impasse remains in place. However, it is mostly of a temporary nature.

[977] Frenz, T. & Soualhi, Y. *op cit,* p. 265. *Darurah* is only granted temporarily, as every effort must be taken to overcome the dilemma as soon as possible. It is for instance stated in the Pakistani *Takaful* Rules under paragraph 28.3 that ''in the event that the capacity provided by a *Shari'ah* compliant re*Takaful* operator is not sufficient to support the business strategy of the *Takaful* operator, the *Takaful* operator, under advice of its *Shari'ah* Board, may be allowed to enter into re*Takaful* and reinsurance contracts with conventional reinsurance companies till such time that proper re*Takaful* arrangements are available''

The same applies to retro*Takaful* where re*Takaful* operators cede part of their business to another reinsurer or re*Takaful* operator. The Labuan regulator states in paragraph 20 (iv):

> ''Retrocession: Retention strategy should also include placement of business under re*Takaful* arrangements. It is necessary to first offer the retrocession, where practicable, to re*Takaful* operators.''[978]

In practice though, most re*Takaful* operators will cede to conventional reinsurers.

The significant increase in first grade re*Takaful* capacity since 2007 has made the *Darurah* exemption obsolete and there is mounting pressure on operators from both regulators and *Shari'ah* Boards to utilize re*Takaful* facility first. For instance, the IFSB Guiding Principles on Governance for Islamic Insurance (*Takaful*) Operations state that:

> ''As far as possible, TOs should strive to use re*Takaful* operators, rather than conventional reinsurers, in support of a fully *Shari'ah* compliant financial system for the *Takaful* undertakings.''[979]

Some of the bigger re*Takaful* companies can now provide underwriting support to the *Takaful* players to write, for example, complex classes of commercial lines business.

Quantitatively, there seems to be enough re*Takaful* capacity available in the re*Takaful* market. Regarding quality, there is also an increasing number of secure, first-rate re*Takaful* operators, which is of utmost importance for the global *Takaful* industry as it guarantees continuing growth and competitiveness vis-à-vis conventional insurance.[980]

[978] Frenz, T. & Soualhi, Y. *op cit*, p. 265. See also Yassin, N. & Ramly, J., *op cit*, p. 255.
[979] *Ibid.*
[980] *Ibid*, p. 266. Almost all *Takaful* operators have a re*Takaful* programme arrangement. The ultimate goal of that programme is to reduce their exposure to loss by sharing the exposure to loss to a re*Takaful* or group of insurers. With re*Takaful*, the *Takaful* operator can issue certificate cover with higher limits than it would otherwise be allowed, therefore, being permitted to take on more risk because some of that risk is now shared with re*Takaful* company.

However, concentrating only on capacity would put the industry in direct and fierce competition with the conventional players, as is currently the case. On the other hand, there might be the danger of giving priority to what might be perceived as a 'more' *Shari'ah* compliant re*Takaful* operator which, however, lacks technical expertise and financial security. The operators then compete with the conventional players at a structural disadvantage.[981]

It is therefore essential at this early stage of the re*Takaful* industry to look at both qualities – a strong financial rating, superior technical expertise, a solid understanding of and strict adherence to the *Shari'ah* and willingness to develop innovative re*Takaful* concepts.[982]

5.2.8 Fund Management and Investments[983]

Fund management and investments are twin critical challenges that can make or mar the operations of *Takaful*. The Nigerian *Takaful* operators must adhere strictly to the issue of fund management and investments if the fragile industry is to take root. As custodians of public funds, *Takaful* operators must ensure that the *Takaful* funds are not only soundly but more importantly safely managed. The conventional insurance industry in Nigeria suffered serious setbacks due to mismanagement of insurance funds, non-settlement of due claims and outright fraud. The resultant effect of this was the birth of apathy to anything about insurance in the country. The fact that the *Takaful* operation is essentially based on profit sharing, prudent investment of the funds becomes fundamentally important as underwriting. However, in the case of *Takaful*,

[981] Yassin, N. & Ramly, J., *op cit.*
[982] *Ibid.* p. 266.
[983] In finance, an investment is a monetary asset purchased with the idea that the asset will provide income in the future or appreciate and be sold at a higher price. To invest is to allocate money (or sometimes another resource, such as time) in the expectation of some benefit in the future. In finance, the expected future benefit from investment is a return. The return may consist of capital gain and/or investment income, including dividends, interest, rental income etc. Investors generally expect higher returns from riskier investments. Financial assets range from low-risk, low-return investments, such as high-grade government bonds, to those with higher risk and higher expected commensurate reward, such as emerging markets stock investments. Investors, particularly novices, are often advised to adopt an investment strategy and diversify their portfolio. Diversification has the statistical effect of reducing overall risk. See https://en.m.wikipedia.org/wiki/investment$/issues. Any investment in Islamic finance must be done according to the tenets of *Shari'ah* otherwise it is null and void.

there is another essential dimension to be considered, in that avenues of investment must be in accordance with *Shari'ah* principles.[984]

The basic requirement of investment in *Takaful* is its compliance with *Shar'iah* principles. This presupposes that the investment must be free from any form of *Riba* (interest), *Maysir* (gambling) and *Gharar* (uncertainty). In line with this requirement, the Guidelines[985] require the *Takaful* operator to establish investment policies for the Participants' Risk Fund (PRF) and Participants' Investment Fund (PIF). The requisite policies shall include:

> '' (a) The *Takaful* operator must seek to manage funds aligned with *Shari'ah* compliant methodology as practiced internationally and approved by its Advisory Committee of Experts (ACE)
>
> (b) Where income is generated from non-compliant or partial investments, a process of purification of the income must take place by giving the percentage of the income generated to charitable purpose. This approach must be ratified by the operator's ACE and approved by the Commission;
>
> (c) The investment policies must be approved by the ACE and the Commission and the operator shall ensure utmost diligence when selecting where the funds are to be invested, in order to maintain strict compliance with the *Shari'ah* standard.''[986]

In spite of the issues of compliance with *Shari'ah* principles, the Guidelines require the *Takaful* operator to ensure that assets and liabilities allocated to the funds match and

[984] Section 25 of the Insurance Act 2003 remains largely controversial once it pertains to the issue of investment under Islamic finance. This is largely so because of ambiguity in the provisions of the Insurance Act 2003 and the *Takaful* Operational Guidelines 2013 that seem to conflict. It is not clear if *Takaful* operators will still have to comply with the provisions of Section 25 of the Insurance Act on investments as well as the requirements of *Shari'ah* which are fundamental. The confusion arises because Nigeria follows a dual system of application of laws and conflicts of laws are bound to arise in such situations that are not normally contemplated by the law makers.
[985] *Takaful* Guidelines for Operators in Nigeria 2013.
[986] *Ibid*, Section 4.4 (a) & 4.5

must set out objectives and long term strategies for each fund. The operator is also required to consider risk profile of the fund in line with the characteristics of *Takaful* liabilities.[987]

The strict requirements stated above are in line with the objectives of Islamic economics which is to create an exploitation-free society, promotion of welfare of the people and safeguarding their lives and property. However, as laudable as the objectives are, the requirements are a tall order because of the relative limitations of investment avenues unlike what obtains under conventional insurance where the insurer can invest in virtually anything as long as it is legal under the law. It is, therefore, highly timely for all relevant parties such as government authorities in Nigeria and in Islamic countries, financiers, bankers including central bankers, *Takaful* operators, economists and *Shari'ah* scholars to study, develop and promote the diversity of investment instruments and products acceptable to *Shari'ah.*[988]

It is pertinent to understand that *Takaful* operations are subject to fluctuations of contributions, claims and investment performance. Excess accumulation of participants' contributions and investment profits may sustain the *Takaful* fund over claims paid and its provision over time. This is called surplus assets. However, if the *Takaful* expenses are high, claims are heavy and investments are at loss, the surplus may be depleted. If a *Takaful* fund is weakened and unable to meet future benefits to participants, the *Takaful* fund is deemed to be declared insolvent. The inability of the fund to pay claims will be in contrast with the purpose of joining the *Takaful* scheme. Therefore, it is a primary objective of *Takaful* operators and regulators to ensure that fund solvency is maintained at all times.[989] Solvency makes the results of insurance transaction certain and

[987] Section 4.4 (b) & (c) of *Takaful* Operational Guidelines 2013.
[988] Ismail, E. *op cit*, p. 132.
[989] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 91.

predictable.[990] This is the function of insurance whether conventional or Islamic; to reduce financial risk and uncertainty faced by individuals in the event of a loss occurring.

5.2.9 Infrastructural Challenges

Inadequate infrastructure is a major concern for the newly introduced *Takaful* insurance system. *Takaful* has an explicit ethical structure that can be marketed to both Muslims and non-Muslims. This is because it is based on fairness, transparency, simplicity and sharing the participants' burdens.[991] The development of *Takaful* depends largely on healthy growth of Islamic banking system. This has found acceptance in Nigeria in spite of the furore that greeted its introduction by non-Muslims. The Islamic banking system itself is still at its infancy stage and is undergoing transformation. Most conventional banks operate Islamic banking as a window and the first wholly Islamic bank has just been granted license to operate in Nigeria.[992] Immature Islamic banking system and poor communications infrastructure constitute major hitches confronting *Takaful* practices in Nigeria. Most of the impediments confronting *Takaful* practices in Nigeria are strategic as the market is still in its formative stage. To considerably manage these teething problems, appropriate skills and resources can be borrowed from conventional insurance markets.[993]

5.2.10 The Challenge of Multi-Dimensional Diversities

Nigeria is a diverse multi-ethnic, multi-lingual and multi-religious country. There are well over 250 ethnic groups and languages living uneasily with each other as suspicion and mistrust are rife among the citizens. The worst of the multi-faceted problems facing

[990] Dorfman, M., (2001), *Introduction to Risk Management and Insurance*, 7th Edition, Prentice Hall, USA.
[991] Ferguson, T., (2008), *''Takaful 2.0'' Using the Power of the Web to Realise the Global Holy Qur'an: Text, Translation and Commentary* By Abdullah Yusuf Ali, Sartaj Company, Durban, South Africa Surah ii 262, 267, 270, 274, 277. Potential of *Takaful*, No. 15.
[992] JAIZ bank was granted license to operate a full-fledged Islamic bank in Nigeria on the 20th of September, 2015.
[993] Stagg-Macey, C., (2007), *An Overview of Islamic Insurance*, No. 8. sabbir@icmif.org.

the country is religious intolerance. Violence and killings are bound to erupt within a short time span on mere suspicion of religious degradation. This has brought so much to bear on governance that everything has to be treated with so much caution for fear of being labelled bias. The introduction of Islamic banking brought so much bitterness and rancour to the polity as the government was roundly accused of attempting to Islamize Nigeria.[994] The same problem is being experienced with the introduction of *Takaful* in spite of the so many assurances by government and Christian leaders that the *Takaful* insurance system is about doing business which is open to everybody. Mr Fola Daniel, a Christian had this to say about *Takaful*:

> ''……rather than allowing people to see Islamic insurance as being designed only for the Muslim population, Christians and any other person would patronize *Takaful* insurance products by the time they understand what *Takaful* is all about and that it has a prospect of returning part of their premium at the end of the year, many people will buy into it. It is not about religion, it is about a way of sharing risks.''[995]

As *Takaful* originates from an Islamic concept, one of the greatest challenges it is facing now is the misconception that it is exclusively for Muslims. This is unfortunate because multi-racial countries like Malaysia have succeeded in creating innovative *Takaful* products that have attracted even non-Muslims, despite the obvious cultural and religious differences.[996] Nonetheless, the interest shown by non-Muslims and the support shown by Muslims is not enough to create awareness about *Takaful* in Nigeria.

[994] See http://www.igbofocus.com/islamic_banking_in_nigeria/islamic_banking_in_nigeria.html {accessed December 16, 2015}. Opponents of Islamic finance in Nigeria based their arguments for the opposing the system on what they called ''major contravention of the Nigerian Constitution, illegal redefinition of non-interest banking, introduction of religion into banking and unconstitutional exclusion of non-Muslims from non-interest banking''.

[995] Alabadan, S., *op cit.*

[996] Ahmad, S.Y., (2009), *Takaful: Potential Demand and Growth*, Malaysia, Faculty of Business Management, University of Malaya. See also Divanna, J. & Shreih, A., (2009), *A New Financial Dawn: The Rise of Islamic Finance*, United Kingdom, Leonardo and Francis Press Ltd.

Low level awareness about *Takaful* is a major impediment militating against *Takaful* practices in Nigeria.[997]

Development and marketing of suitable *Takaful* products should be a major priority of the Nigerian *Takaful* operators. The operators need to invest in research and development (R & D) of *Takaful* products based on needs of *Takaful* prospects. This is necessary as conventional insurers have been in business for years and their products and experiences are more obvious than those of *Takaful* operators. To overcome these challenges, wider range of *Takaful* products should be offered as an alternative to those offered by conventional insurers. Consequently, needs of lower income groups should be adequately addressed, as they constitute the greater majority of *Takaful* prospects.[998]

Closely tied to the issue of religious intolerance is the menace of Islamic fundamentalism. Nigeria today is facing a huge security challenge in the form of Boko Haram. This is a violent, brutal and misguided sect that wants to establish an Islamic caliphate in Nigeria. They have killed and maimed thousands of innocent citizens since July 2009 to date in order to overthrow the Nigerian government and achieve their aim. This violence has invariably rubbed-off on the credibility and confidence in Islamic finance and *Takaful* stemming from a set of factual issues combined together with a slew of misrepresented beliefs about Islam. Perceptions of Islamic finance being a conduit of terrorist funding and home of anti-money laundering, is far from the truth as it is a serious an issue to address. It is paramount that these false ideas about Islam and its financial industry are corrected.

[997] Fadun, O.S., *op cit*, p. 24.
[998] Ahmad, S.Y., *op cit*. See also Usman, A.Y., (2012), *Prospecting for sustainable micro-Takaful Business in Nigeria.* Available at http;//dx.doi.org/10.2139/ssrn.199744 [Accessed 17 December 2014].

5.3 REGULATORY CHALLENGES[999]

Takaful insurance is relatively new in Nigeria, hence the need for adequate implementation of *Takaful* Operational Guidelines, 2013. It is paramount that the operational requirements should be adequately enforced by the National Insurance Commission (NAICOM) which is the chief regulating body and other relevant agencies. It is important to set out clear principles on how to manage *Takaful* funds, and how *Takaful* business should be taxed. Likewise, it is essential to create a regulatory regime that does not treat *Takaful* less favourably than conventional insurance in Nigeria. This is necessary to promote virile *Takaful* practices that are consistent with *Shariah* principles and NAICOM regulations in Nigeria.[1000]

The most critical regulatory challenge currently facing the nascent *Takaful* industry in Nigeria today has to do with the provisions of the Insurance Act, 2003. The Act, which is the primary legislation regulating insurance business in Nigeria, makes no mention of Islamic insurance or *Takaful* at all. Section 1 of the Act[1001] delineates its area of regulation by limiting its operations to all insurance business and insurers other than the insurance business carried on or by insurers of the following description:-

a) A friendly society; and

[999] While achieving conducive market dynamics is a priority, Nigeria will also need to improve the policy, regulatory and supervisory framework for *Takaful* to develop good market conduct principles. The fragmentation of insurance policy-making, regulation and supervision between different authorities leaves gaps for insurance market development and creates an uneven playing field across different insurance practices and products. The harmonization of these regulatory and supervisory discrepancies in the enabling insurance instruments especially between the Insurance Act, 2003 and the *Takaful* Operational Guidelines 2013 has been the main thrust of this study. The study further submits that the mandatory insurance policy may give comfort for the insurance companies to stick to current business practices, and hence is somehow conflicting with market development goals and an environment that fosters innovation and competition.

[1000] Fadun, O.S., *op cit*, p. 22.

[1001] '' This Act applies to all insurance businesses and insurers, other than insurance business carried on or by insurers of the following description –
(a) a friendly society that is an association of persons established with no share for the purposes of aiding its members or their dependants where such association does not employ any person whose main occupation –
(i) is the canvassing of other persons to become members of the association;
(ii) is the collection of contributions or subscriptions towards the funds of the association from its members; or
(b) a company or any other body (whether corporate or incorporated) or person whose business is established outside Nigeria, engaged solely in reinsurance transactions with an insurer authorized or pursuant to the provisions of this Act to carry on any class of insurance business, but not otherwise however''.

b) A company or person established outside Nigeria to engage solely in reinsurance business.

The section defines 'a friendly society' as an association of persons established with no share for the purpose of aiding its members or their dependants where such association does not employ any person whose main occupation is: (i) canvassing others to become their members and (ii) collecting contributions from members for the association's funds.

A careful perusal of the provision shows an express omission of the term *Takaful* or Islamic insurance. This absence in insurance legislation is a grave error which is bound to produce ambiguities in the complex application of *Takaful* within conventional insurance. *Takaful* is quite different from conventional insurance and as such should have been specifically and specially provided for in the Insurance Act. The resultant ambiguity is bound to make potential investors consider the situation as too risky to invest their hard earned capital into high level of uncertainties. Furthermore, *Takaful* operators might be reluctant to invest more on marketing and product development since there are no express legal guarantees due to conflict of laws.

Even the regulatory authority is not raising enough of awareness on the release of the Operational Guidelines to warrant being taken serious by willing investors.[1002] Regulatory and supervisory guidelines have the propensity to clear several foggy areas for all stakeholders. This study has not been able to identify any efforts made by the regulatory authorities towards addressing this serious issue. The effectiveness and efficiency of the Operational Guidelines which are already in conflict with the basic provisions of the Insurance Act are being questioned two years after their introduction and have contributed to the slow start of full-fledged *Takaful* operations in Nigeria. This

[1002] Yusuf, T.O. & Babalola, A.R., *op cit*, p. 114.

view corroborates that of Saad, Gambo and Kassim who posit that potential investors will question the murky nature of the Nigerian insurance legislation[1003] towards the application of *Takaful.*

A cursory look into the definition of a friendly society by this section will tempt a conclusion that *Takaful* insurance falls into the variant of the businesses excluded from the regulation of the Act. However, the commercial nature of modern *Takaful* operation demands that the operator should maintain a minimum paid up share capital and canvass for business to remain afloat in the competitive insurance market.[1004]

The opening provision[1005] of the Act also presupposes that:-

(a) The Act recognises the existence of some form of insurance business or insurers other than all those it regulates;

(b) That all insurance business not specifically mentioned in subsections (a) and (b) should be under regulatory remit of the Act.

This means *Takaful* is only alluded to by inference. This omission is bound to create confusion where complex issues affecting *Takaful* regulation in the Guidelines surface. The courts are yet to test this ambiguity, at any level, in the course of their proceedings. It is one of the thrusts of this thesis that the issue of express mention of *Takaful* in the Insurance Act be effected immediately by amending the section to address the anomaly.

Generally, the Act sets standards for registration, regulation, administration and control of the insurance business as well as establishes financial and prudential requirements for insurance institutions in Nigeria. Section 86 of the Act vests in the National Insurance Commission the responsibility for administration and enforcement of the provisions of

[1003] Gambo, G., Saad, N., & Kassim, S., (2014), ‘’Assessing the Impact of Islamic Micro-Finance on Poverty Alleviation in Northern Nigeria. *Journal of Islamic Economics, Banking and Finance,* Vol. 10, No. 4, October-December, 2014. Available at http://ibtra.com/journal_current_issue.php.
[1004] Adamu, A.I., *op cit*, p. 77.
[1005] Section 1 of the Insurance Act 2003.

the Act and authorizes it to carry out the requirements of the Act. This, in effect, places responsibility for the regulation and enforcement of *Takaful* in the Commission. The section provides:-

> '' Subject to the provisions of this Act, the National Insurance Commission (in this Act referred to as ''the Commission'') shall be responsible for administration and enforcement of this Act and is hereby authorized to carry out the provisions of this Act.''[1006]

Consequently, in an effort to integrate *Takaful* into the existing conventional insurance legal framework, the need arose to come up with Operational Guidelines for *Takaful* to make some of the provisions of the Insurance Act accommodating to *Takaful*. In this regard, Section 9[1007] which provides for minimum paid up capital was relaxed in the Guidelines to bring down the minimum paid up capital for *Takaful* insurers to N100 million[1008] about RM2 million. This accommodation of *Takaful* is however, subject to controversy as the Commission's power under the Act relates only to upward review of the minimum paid-up share capital and not its downward review.[1009] It remains arguable whether the power to increase paid-up share capital vested in the Commission would accommodate the discretion to decrease in the prescribed minimum paid-up capital. These are some of the challenges that this study is highlighting with a view to coming up with an appropriate legislation to safeguard the application of *Takaful* in Nigeria.

[1006] Section 86 Insurance Act 2003.

[1007] ''(1) No insurer shall carry on insurance business in Nigeria unless the insurer has and maintained, while carrying on that business, a paid-up share capital of the following amounts as the case may require, in the case of –
(a) Life insurance business, not less than N150,000,000:00;
(b) General insurance, not less than N200,000,000:00;
(c) Composite insurance business, not less than N350,000,000:00;or
(d) Reinsurance business, not less than N350,000,000:00
(2) The paid-up share capital stipulated in subsection (1) of this section in the case of existing insurer –
(a) Shall come into force on the expiration of a period of nine months from the date of commencement of this Act; and
(b) May be subscribed to by the capitalization of undistributed profits as approved by the Commission.
(3) The Commission shall –
(a) cancel the registration of any insurer or reinsurer that fails to satisfy the provisions of subsection (1) of this section as it relates to the category of operation of such insurer or reinsurer; and
(b) Not later than thirty days after expiry of the period specified in subsection (2) of this section publish a list of all insurers and reinsurers that have complied with the provisions of this section.
(4) The Commission may increase from to time the amount of minimum paid-up share capital stated in subsection (1).

[1008] Paid up capital requirement contained in the registration requirement for *Takaful* operation.

[1009] Section 9(4) Insurance Act 2003.

Another potential area of conflict which poses a huge challenge to the application of *Takaful* in Nigeria is found in Section 10 of the Insurance Act.[1010] The Section requires an insurer/*Takaful* operator intending to commence business, to deposit the equivalent of fifty per cent of the paid-up share capital with the Central Bank of Nigeria (CBN) as its statutory deposit. However, after registration, eighty per cent of the statutory deposit would be released to the insurer/*Takaful* operator with interest not later than sixty days after registration. The Section further states that in the case of an existing company, ten per cent of the paid-up share capital shall be deposited with the CBN attracting interest at CBN rate on the 1st of January each year.

The issue of interest (*Riba*) is what is unacceptable to the *Takaful* operator because it clearly violates *Shari'ah* principles. *Riba* is often translated as 'usury' or 'interest' for which no counter value is given. It is often regarded as any unjust or excessive gain or unjustified increase in capital for the earning of which no appropriate effort was made[1011]. In all his transactions, a Muslim is forbidden to enrich himself unjustifiably:

> '' O ye who believe! Do not appropriate unlawfully one another's property except it be a trade by mutual consent.''[1012]

There a number of passages in the Qur'an whereby unjustified enrichment is prohibited. This prohibition extends to *Takaful* practice because the absence of *Riba* in *Takaful* is a cardinal requirement for its enforceability. One thing that makes Islamic financial system different from its conventional counterpart is the fact that it prohibits the giving

[1010] '' (1) An insurer intending to commence insurance business in Nigeria after the commencement of this Act shall deposit the equivalent of fifty per cent of the paid-up share capital referred to in Section 9 of this Act (in this Act referred to as the ''Statutory Deposit'') with the Central Bank.
(2) Upon registration as an insurer, eighty per cent of the statutory deposit shall be returned with interest not later than sixty days after registration.
(3) In the case of existing companies, an equivalent of ten per cent of the minimum paid-up share capital stipulated in Section 9 shall be deposited with the Central Bank.
(4) Any statutory deposit made under subsection (1) of this section shall attract interest at the minimum lending rate by the Central Bank on every 1 January of each year.
(5) Any withdrawal from the statutory deposit shall be made good within thirty days, failure of which shall constitute a ground for suspension from business and such suspension shall be published in the newspapers.
(6) Failure to deposit the statutory deposit shall constitute a ground for cancellation of the certificate of registration''.
[1011] Mannan, M.A., (1980), *Islamic Economic Theory and Practice*, Delhi, p. 161.
[1012] Noble Qur'an Chapter 4 verse 29.

and taking of *Riba* in all types of transactions. *Takaful* offers and provides services to its customers free from interest or *Riba.* There is a consensus of opinion among Islamic scholars that the term *Riba* extends to all forms of interest.[1013]

In 1992, the Pakistani *Shari'ah* Court ruled that:

> ''It makes no difference whether the loan is for consumption purpose or for commercial purposes. It does not matter if the rate of interest is low or high, simple or compound for short or long times, between two the Muslims or between a citizen and a state or between two states. Any excess which is predetermined over the principal sum in a loan transaction will constitute *Riba* in all circumstances.''[1014]

Islam only allows *Qard Hasan* (benevolent loan) whereby the lender does not charge any interest or additional amount for the money lent. The prohibition also applies to any disadvantages or benefits that the lender might secure from the borrower out of the *Qard* (loan) such as using the borrower's car, his computer etc. As such any direct or indirect benefits which could potentially accrue to the lender from lending money are strictly prohibited. Therefore, with the rejection of interest, in order for Islamic financial system to operate, profit and loss sharing replaced the interest rate mechanism, where profit and loss sharing acts as the method of resource allocation and financial intermediation. An Islamic bank of *Takaful* outfit does not charge interest but rather participates in the yield resulting from the use of funds.[1015]

It remains a curious issue as to how this challenge will be resolved. It will be difficult for the principle of *Darurah* (necessity) to be applied here because it is no longer feasible. In the alternative, whatever interest that might have accrued to the *Takaful*

[1013] Kettle, B., (2008), *Introduction to Islamic Banking and Finance*, London: Brian Kettle Islamic Banking Training, p. 39.
[1014] Mohammed, T.U., (2003), *The Text Of The Historic Judgement On Riba By Supreme Court Pakistan*, Islamic Book Trust: Karachi, p. 83.
[1015] Hassan, R., *op cit*, p. 9.

operator by virtue of the provisions of Section 10 of the Act, will have to undergo fund purification and donation made to charity. The best way out of this quagmire is for an enactment by the legislature to harmonize all the conflicting regulatory provisions existing in the Insurance Act and the newly introduced *Takaful* Guidelines in order for *Takaful* operate smoothly.

The investment portfolio provision contained in Section 25 of the Insurance Act[1016] is a potential source of conflict with the *Takaful* Operational Guidelines, 2013. The basic requirements of investment in *Takaful* are its compliance with *Shari'ah* principles. This presupposes that the investment must be devoid of the *Shari'ah* prohibitive elements namely, interest, uncertainty and gambling. The *Takaful* Operational Guidelines impress on the operator to establish investment policies for the Participants' Risk Fund (PRF) and Participants' Investment Fund (PIF).[1017] However, Section 25 of the Insurance Act, which is the main regulatory law provides for investment by an insurer in a totally different way from the provisions of the *Takaful* Guidelines. There is no express exemption of *Takaful* from the requirements of Section 25 of the Insurance Act. Furthermore, interest is a key component of admissible assets under Section 24(13) of The Insurance Act, while under *Takaful* interest is the averting factor of the transaction.

[1016] Section 25 Insurance Act 2003 provides:
''(1) An insurer shall at all times in respect of the insurance transacted by it in Nigeria, invest and hold invested in Nigeria assets equivalent to not less than the amount of policyholder's fund in such insurance business as shown in the balance sheet and the revenue accounts of the insurer.
(2) Subject to the other provisions of this section, the policyholders' funds shall not be invested in property and securities except –
(a) shares of limited liability companies;
(b) shares in other securities of a co-operative society registered under a law relating to co-operative societies;
(c) loans to building societies approved by the Commission;
(d) loans on real property, machinery and plant in Nigeria;
(e) loans on life policies within their surrender values;
(f) cash deposits in or bills of exchange accepted by licensed banks; and
(g) such investments as may be prescribed by the Commission.
(3) No insurer which shall –
(a) in respect of its general insurance business, invest more than twenty-five per cent of its assets as defined in subsection (1) of this section in real property; or
(b) in contract of its life insurance business, invest more than thirty-five per cent of its assets as defined in subsection (1) of this section in real property.
(4) An insurer which contravenes the provisions of this section commits an offence and is liable on conviction to a fine of N50, 000.00 about RM 1,000.
(5) In this section, references to real property include references to an estate in land, a lease or a right of occupancy under the Land Use Act''.

[1017] The requisite policies shall include: The *Takaful* operator must seek to manage funds aligned with *Shariah* compliant methodology as practiced internationally and approved by its Advisory Committee of Experts (ACE).

This view, however, depends on the purification concept stipulated in Section 4.4(a) of the *Takaful* Operational Guidelines.

What remains unclear is whether Section 25 of the Insurance Act will apply to *Takaful* insurance. If the provisions of the Act apply besides the regulations of *Takaful* investment in the Guidelines, the *Takaful* operator must also meet the requirements of Section 25 of the Law. The supremacy of the Insurance Act in regulating insurance business in Nigeria has been clearly stated in Section 100 of the Act.[1018] The murky nature of this plethora of general and regulatory challenges facing *Takaful* insurance will not bode well for its smooth application in Nigeria. A harmonization of these statutory and regulatory provisions in the frameworks cannot be overemphasized.

5.3.1 Conflict of Laws

As Nigeria is still governed by civil law, there are times conflict of laws arises with regard to their interpretations. *Takaful* contracts are expected to comply with *Shari'ah* rules and principles, as well as with the laws of the civil jurisdiction in which contracts are to be enforced. This is a potential area of friction because of the fundamental differences in Islamic and conventional laws. Insurance is a contract and is governed by the received English common law of contract as well as the Insurance Act and other statutory enactments, whereas *Takaful* is primarily governed by *Shari'ah* law and the recently released *Takaful* Guidelines. The issue of jurisdiction is critical here as the released Guidelines have been silent on the exclusivity of *Shari'ah* law application on *Takaful* contrary to what obtains in other *Takaful* operating countries.[1019] How this

[1018] Section 100 of the Insurance Act 2003, provides:
''The provisions of this Act are without prejudice to the application of the Companies and Allied Matters Act, 1990 and any other enactment applicable to insurance under this Act which are companies registered under that Act, so however that where any of the provisions of the Companies and Allied Matters Act, 1990 and other enactment is inconsistent with any provision of this Act, the provision of this Act shall prevail to the extent of that inconsistency''.

[1019] In Malaysia for example, in the event where there is a dispute before the court or arbitrator which involves the *Takaful* business in relation to any *Shari'ah* matters, the court or arbitrator is required to make reference to the *Shari'ah* Advisory Council (SAC) of the Central Bank of Malaysia by virtue of Part VII of the Central Bank of Malaysia Act, 2009. Once the reference is made to SAC, their decision is binding on the courts and arbitrator.
See also Section 56 of the Central Bank of Malaysia Act 2009.

conflict pans out will be made clearer in the course of time as the *Takaful* industry is just beginning to take roots in Nigeria.

5.3.2 Breaches by a *Takaful* Agent

A *Takaful* agent, as an intermediary, is a legal agent of a *Takaful* operator (as the principal). Agents are authorized to act as the marketing channel of *Takaful* products on behalf of a *Takaful* operator. However, agents and principals are also bound by common law rules governing agency relationships. It is trite agency rule that a principal will not be liable for any dealings or transactions carried out by an agent beyond his or her authorized express power, implied power or common authority power.[1020]

Therefore, there is bound to be complication for the participants when they claim for their rights on any misconduct of the *Takaful* agents. If proven that the agents have acted beyond their powers, the *Takaful* operator, as principal, may deny liability. At the end of the day, the participants/public are the parties at loss.[1021] This is another potential area of friction that is bound to cause problems in the relationship between the *Takaful* operator and participants that hugely depends on trust and transparency.

5.3.3 Regulatory Policy Initiatives

The effective application of *Takaful* within Nigerian insurance industry requires supportive policy objectives and risk-based approach to supervision. Risk-based approach gives the regulator the room to tailor supervisory activities to reflect the demand of a regulated entity (risk sensitivity). This system enables the supervisory

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Section 63 of the Malaysian *Takaful* Act 1984 provides that any prosecution in respect of any offence under the Act is to be referred to the Magistrate Court. There are also other laws applicable to *Takaful* matters, in which Section 67 of the *Takaful* Act 1984 allows the application of the Companies Act, Contracts Act 1950 and Insurance Act, 1963, Road Traffic Ordinance 1958 and Co-operative Societies Act. In the event where there is a conflict or inconsistency between the *Takaful* Act and other Acts, the *Takaful* Act prevails. This should be compared with Section 100 of Insurance Act 2003 of Nigeria cited above which claims supremacy in any matter on insurance in Nigeria.

[1020] Ahmad R. & Auzzir, Z.A., *op cit*, p. 39.

[1021] *Ibid.*

approach to reflect the peculiarities of *Takaful* so as to enable it compete favourably with the conventional insurance model.[1022]

In spite of the presence of the enabling frameworks for the application of *Takaful* in Nigeria, sound regulatory and supervisory system is necessary for maintenance of efficient, safe and sustainable *Takaful* industry. Therefore, supervisory objectives must be clearly defined and religiously observed. The supervisor should be adequately equipped to conduct effective off-site monitoring and evaluation of new entrants to the market as well as assess the adequacy of technical requirements for applicants seeking *Takaful* license.[1023]

5.3.4 Supervisory Capacity

The competence of the supervisory staff is critical to all forms of supervision. It is therefore necessary for the National Insurance Commission of Nigeria to hire and maintain knowledgeable staff both on the workings of *Takaful* and at the same time having in-depth knowledge of *Shari'ah* jurisprudence (*Fiqh*) and supervision expertise.

In order to address the teething challenges of *Takaful* application, the role played by Islamic Financial Services Board (IFSB) and the International Association of Insurance Supervisors (IAIS) is instructive by issuing prudential and supervisory standards for *Takaful* operations.[1024] The standard sets regulatory benchmark to safeguard the interests of the *Takaful* policyholders, beneficiaries and ensures safety and stability of the financial sector as a whole.[1025]

It is in this regard that the need for the support of these international Islamic institutions becomes imperative in the course of the application and integration of *Takaful* in

[1022] Adamu, A.I., *op cit*. p. 134.
[1023] *Ibid.* Sound supervision ensures strict compliance with the rules and penalizes violations appropriately. This is an important factor that is bound to increase public confidence in the *Takaful* industry.
[1024] IFSB-IAIS (2006) Issues in Regulation and Supervision of *Takaful.*
[1025] *Ibid.*

Nigeria. The support of the agencies to overcome the challenges of manpower, developing Islamic capital market as well as *Shari'ah*-compliant investments is very much critical to the success of the nascent *Takaful* industry.

5.3.5 Appropriate Accounting Standards[1026]

Appropriate accounting standard is another challenge *Takaful* operators in Nigeria are bound to grapple with. The Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) has created a standard that is the default accounting standard for *Takaful* businesses in some Middle East countries. *Takaful* firms in other countries account for *Takaful* under International Financial Reporting Standards (IFRS). However, applying IFRS to *Takaful* is complex because the regulations often require that *Takaful* be treated as conventional insurance, which, however, does not fully reflect the risk-sharing nature of *Takaful* and the segregation between the shareholder' and *Takaful* funds. The *Takaful* participants are the owners of the *Takaful* fund and as such both the insurer and the insured. The *Takaful* operator on the other hand is nothing but a third party administrator, very much like an investment manager for the assets and administrative agent for the risk fund. This is at odds with the definitions under IFRS relating to insurance contracts, as IFRS assumes a transfer of risk as in conventional insurance, which *Takaful*, clearly is not.[1027]

Furthermore, the aggregate accounting under IFRS on a corporate level distorts the nature of segregated funds under *Takaful*, unless additional details (revenue account, income statement or columnar balance sheet) are shown separately. IFRS does not account for claims equalization reserves, which, however, are a crucial component of

[1026] ''Islamic accounting is generally defined as an alternative accounting system which aims to provide users with information enabling them to operate businesses and organizations according to *Shari'ah* or Islamic law''. Although Islamic regulatory bodies have established standards, different interpretations of religious texts and weak implementation mean they lack harmonization.
Islamic accounting in many ways is quite holistic. *Shari'ah* prohibits interest-based income or usury and also gambling, so part of what Islamic accounting does is to help ensure companies do not harm others while making money and achieve an equitable allocation and distribution of wealth, not just among shareholders of a specific corporation but also among society in general. See www.accountingweb.com/aa/auditing-challenges-and-terror.
[1027] Frenz, T. & Soualhi, Y., *op cit*, p. 192.

Takaful, especially for re*Takaful* operators. Under IFRS it would be booked under equity and thus subject to different tax treatment.[1028]

There are many other issues under IFRS, but for the time being companies will simply have to consider *Takaful* as insurance under IFRS, until new or additional standards are developed. It is, therefore, paramount to enhance skills on how *Takaful* operations can be accounted for in Nigeria.[1029] Moreover, recent studies on Islamic financial transactions accounting[1030] found that practitioners are highly concerned on various *Shari'ah* issues, including applicability of time value of money, the terminologies used in IFRS and IAS that reflect conventional concepts of banking and *Takaful*. Consequently, it is paramount that NAICOM, *Takaful* operators and other stakeholders should affirm the acceptable accounting standard in Nigeria in order to promote uniformity and consistent *Takaful* accounting system.[1031]

Limited short-term non-equity financial instruments in Nigeria pose additional challenge for *Takaful* companies. These include: *Sukuk* and *Shari'ah*-compliant money market instruments equivalent to treasury bills.[1032] This portends enormous challenge to *Takaful* operators in Nigeria because *Takaful* funds cannot be invested in conventional bonds and cash assets. This is indicative of complications for the *Takaful* operators regarding management of *Takaful* investment portfolio. The basic requirement for investment in *Takaful* is compliance with *Shari'ah* principles. This presupposes that the investment must be free from any form of *Riba* (interest), *Gharar* (uncertainty) and *Maysir* (gambling). This compliance is not possible with conventional insurance instruments.

[1028] Frenz, T. & Soualhi, Y., *op cit*, p. 193.
[1029] Fadun, O.S., *op cit*, p. 22.
[1030] Shafi'i, Z. & Zakaria, N., (2013) Adoption of International Financial Reporting Standards and International Accounting Standards in Islamic Financial Institutions From the Practitioner's Viewpoint. *Middle East Journal of Scientific Research*, 13, pp 42-49.
[1031] Fadun, O.S., *op cit*, p. 22.
[1032] Venardos, A.M., (2005), Islamic Banking and Finance: Its Development and Future, Singapore, World Scientific Publishing.

5.3.6 *Qard* (Loan) Facility to Meet Fund Deficit

In other jurisdictions where *Takaful* is operational, the regulator sets standard for the operators to set aside reserve fund for an interest free loan under the principle of *Qard* to the *Takaful* fund. The provision for *Qard* loan facility is to enable *Takaful* fund meet its obligation in case of deficit or illiquidity.[1033]

Although the requirement for an interest-free loan is in the enabling Nigerian *Takaful* Guidelines[1034] the issue of adequacy of the fund in the early years of *Takaful* operations, as well as inadequate regulatory mechanism to ring-fence and protect the reserve, is a huge challenge and a matter for concern. Therefore, certain safeguards against abuse of the fund through related party transaction and disclosure of the draw-downs, are some of the regulatory framework solutions that must be considered in the course of safeguarding the nascent *Takaful* operations.

However, there are some issues with *Qard Hasan* which need to be dealt with. *Qard Hasan* was originally meant to provide an interest-free loan for temporary and short term cash-flow deficits, but in practice, it has evolved to have a much wider scope, also covering long term deficits.

Secondly, in Family *Takaful* we also observe the problem in some jurisdictions like Malaysia, that reserving has to be done on a conservative/prudent valuation basis, which results in a strain on the surplus in early years. This is critical to the Nigerian *Takaful* practice because it is in its formative years. For operators with a smaller capital base (small CCR), this deficit has to be made up by a *Qard Hasan*. The problem here is that

[1033] Interestingly, a loan facility is also applicable in the context of *Sukuk* (Islamic bond) which is a component of Islamic finance and has been disregarded as Haram by the AAOOIFI. However, the loan in that context is an inherent feature to guarantee regular coupon payments on the *Sukuk* and thus circumvent *Shari'ah* objectives. This is not the same here as the *Qard Hasan* is aimed at facilitating the Takaful operation and the loan is meant to be fully repaid. However, in practice, the *Qard Hasan* has assumed a more prominent role than that for which it was probably developed.

[1034] Section 4.8 of the *Takaful* Guidelines 2013 provides:
''The *Takaful*-insurance operator is required to fund any deficit that has occurred in the Participants' Risk Fund using a loan from its shareholders funds. This can be through an interest free loan (*Qard Hasan*) that can be repaid to the *Takaful*-insurance operator in subsequent years when a surplus is generated in the Participants' Risk Fund or where applicable the Participants' Investment Fund''.

this *Qard* is not due to under-pricing or bad claims experience but simply regulatory reserving requirements. This would not be a problem if it could be priced in, but *Shari'ah* scholars have so far hesitated to allow explicit capital costs to be considered in the pricing. However, in practice actuaries usually include charges for risk-based capital in their profit-testing.[1035]

One aspect that has to be kept in mind is how to maintain fairness between generations of policy-holders, in particular future generations: participants who have recently joined a pool with an outstanding *Qard Hasan* will be disadvantaged as they might receive a smaller share of the surplus arising in the short-term due to the (partial) repayment of the *Qard.*[1036]

There is obviously a related risk that participants might decide to leave the pool once the fund is in deficit if they cannot expect to receive any surplus in the short or medium term. This poses a significant challenge for *Takaful* companies most especially in newly established ones like in Nigeria. Again, it might be difficult to persuade potential participants to join a pool that is in deficit.[1037]

Other learned authors[1038] have identified additional problems plaguing *Qard Hasan.* Arbouna posits that *Qard* arrangement has no incentive to encourage the operator or a third party to offer the loan facility. This is because the standard in financial world is that financial institutions do not offer benevolent loans. It would be very difficult for the *Takaful* operator to secure loan facility from a third party without an incentive. The same applies to the shareholders. The shareholders would need to see the benefit of providing loan to the fund without interest. Thus a form of incentive needs to be devised to encourage providing such loan facility either by the operator or a third party. This

[1035] Frenz, T. & Soualhi, Y., *op cit*, p. 188.
[1036] *Ibid.*
[1037] *Ibid.*
[1038] Arbouna, M, B., (2008) Regulation of *Takaful* Business; A Shariah Overview of Contractual Aspects of *Takaful* Models; *Essential Readings in Islamic Finance* (Bakar, M.D. & Ali, E.R.A.E. (eds)) CERT Publications Sdn Bhd, Kuala Lumpur, p. 238.

incentive lies in the concept of ''mutual exchange of loans'' or *Tabadul al-Qurud* which is approved by AAOIFI *Shari'ah* standards,[1039] a number of *Shari'ah* Boards of Islamic banks and insurance[1040] in order to avoid payment of interest and at the same time secure loan without interest.[1041]

The *Shari'ah* Board of the Jordan Islamic Insurance Company argued that, ''there is no objection for the operator and the participants to exchange loan when one of the parties is in need of loan without payment of interest.''[1042] However, the *Fatwa* of some *Shari'ah* Boards see no legal problem with conditional exchange of deposits or loans.[1043] Thus the concept of *Tabadul al-Qurud* is an innovative product that could be introduced into the realm of Islamic insurance industry to encourage securing loans in a very fast and effective manner The Nigerian *Takaful* industry will surely reap from this arrangement if put in place and implemented. However, there would be no any practical problem if the loan is from the *Takaful* operator to the *Takaful* fund. However, one nagging question still remains: who is the party who deserves to approve the loan if the loan is to be released to the *Takaful* operator by the participants? This is a potential area for detailed research in the future.

5.3.7 Effects of *Mirath* (Inheritance) and *Wasiyah* (Will) on *Takaful* Nomination Clause

Mirath is law of succession and inheritance for Muslims, while *Wasiyah* is a binding will allowed to be made by an individual to bequeath his wealth to relatives who are not his or her legal heirs. *Wasiyah* must not exceed one third of the individual's wealth.

[1039] AAOIFI *Shari'ah* Standard No. 1: Trading in Currencies Clause 2/4 (a).
[1040] See for example *Fatwa* numbers 697 and 698 of the *Shari'ah* Board of Kuwait Finance House in *al-Fatwa al-Shari'ah fi al-Masa'il al-Iqtisadiyyah*, vol. 4, p. 146.
[1041] Arbouna, M.B., *op cit*, p. 239.
[1042] See Unpublished *Fatwa* of *Shari'ah* Board of Jordan Islamic Insurance Company.
Furthermore, According to the resolution of Al-Barakah Forum on Islamic economics, ''it is permissible in order not to pay or receive interest for two banks to agree on exchanging deposits of the same currency or different currencies as loan when each party is in need. This permissibility is circumscribed with a condition that the obligation of one party to provide loan is not dependent on the obligation of the other''.
[1043] See *Fatwa Hai'ah al-Raqabah al-Shari'ah Bank Faisal al-Islami al-Sudani*, vol. 1. Pp. 52-53.

There are explicit Qur'anic injunctions[1044] requiring Muslims to comply. For *Takaful* to be free from *Gharar* on the outcome of the *Takaful* contract, a participant must be clearly informed that nominee in the *Takaful* certificate only acts as an administrator of the benefits after the demise of the participant. Death benefits are paid to the entitled claimant nominated in the certificate and the *Takaful* operator shall dismiss their liability on the same. The nomination clause is the same in conventional life insurance policy which enables a Muslim to bypass the Islamic rules of *Mirath* and *Wasiyah* because nomination is made by the participant during his or her lifetime. The nominee of a Muslim policy owner receives the money from an insurance policy benefit only as an executor.[1045]

To avoid issues of *Gharar* (uncertainty) for the payment of the death benefit, a *Hibah* (gift) *Aqad* attached to a *Takaful* certificate allows the benefit to be given to a nominee already indicated by the participant.[1046]

5.4 RISK MANAGEMENT CHALLENGES IN *TAKAFUL*

The issue of what constitutes risk in *Takaful* has been dealt with in chapter three of this study. Any contract of insurance, whether conventional or *Takaful*, is about risk protection and prevention. The *Takaful* operator approaches risk management in the achievement of fees and profit sharing. Each *Takaful* operator is unique in this regard.

[1044] Surah Al-Nisa, Noble Qur'an, Chapter 4 verses 11-12 provides:
''Allaah chargeth you concerning (the provision for) your children: to the male the equivalent of the portion of two females, and if there be women more than two, then theirs is two-thirds of the inheritance, and if there be (only) one then the half. And to his parents a sixth of the inheritance, if he has a son; and if he has no son and his parents are his heirs, then to his mother appertaineth the third; and if he has brethren, then to his mother appertaineth the sixth, after any legacy he may have bequeathed, or debt (hath been paid). Your parents or your children: Ye know not which of them is nearer unto you in usefulness. It is an injunction from Allaah. Lo! Allaah is the Knower, the Wise.
And unto you belongeth a half of that which your wives leave, if they have no child; but if they have a child then unto you the fourth of that which they leave, after any legacy they may have bequeathed, or debt (they may have contracted, hath been paid). And unto them belongeth the fourth of that which ye leave if ye have no child, but if ye have a child then the eight of that which ye leave, after any legacy ye may have bequeathed, or debt (ye may have contracted, hath been paid). And if a man or a woman has a distant heir (having left neither parent nor child), and he (or she) has a brother or a sister (only on the mother's side) then to each of them twain (the brother and the sister) the sixth, and if they be more than two, then they shall be sharers in the third, after any legacy that may have been bequeathed or debt (contracted) not injuring (the heirs by willing away more than a third of the heritage) hath been paid. A Commandment from Allaah. Allaah is the Knower, the Indulgent''.
[1045] Ahmad, R. & Auzzir, Z.A., *op cit*, p. 38. See also Malaysian Insurance Act 1996; Section 65, Malaysian *Takaful* Act 1984, now Islamic Financial Services Act, 2013.
[1046] *Ibid*. However, some scholars argue that the benefit could not be considered as part of the deceased's estate, because it does not form part of the deceased's assets during his lifetime. The death benefit has not formed yet before the policy maturity date or at time of death, whichever comes first.

Traditionally, the operations of a *Takaful* business are split into two distinct portions – investment activities and underwriting activities. The investment activities are usually on either a *Mudharabah* (partnership) or *Wakalah* (agency) basis. If a *Mudharabah* basis is used, the operator will share in the investment profit. Normally, this is realized investment profit, but there are operators who use total profit of the business. For such cases, this is a significant risk which must be managed. For all *Mudharabah* models, this sharing of investment profits means that the various investment risks the *Takaful* fund is involved in is also a risk of the *Takaful* operator.[1047]

Nigerian *Takaful* operators and participants must be wary of this arrangement if the integrity of the nascent industry is to be preserved. Some *Takaful* funds, especially those operated on a unit-linked basis, have their investment operations based on a *Wakalah* model. Here, the operator would receive a fee as a percentage of the fund value (net asset value or NAV) such as 1% of NAV per annum. The operator in such cases takes relatively less investment risk than for the *Mudharabah* model.[1048]

Underwriting activities of the *Takaful* operation are also performed on either a *Mudharabah* or *Wakalah* basis. Under a *Mudharabah* basis, the operator receives a percentage of underwriting surplus, with operating expenses of the operations taken from the operator's fund, often in advance of the receipt of any underwriting surplus. Thus, the expense risk is a major concern for operators using a *Mudharabah* model, and must reflect prominently in the risk management plan.[1049]

Currently, many operators use the *Wakalah* model for underwriting activities. Here, a fee is charged to cover expenses and all underwriting surplus belongs to the participants. This model has significantly less risks than the *Mudharabah* model due to

[1047] Note that some *Takaful* operators state the model to be *Wakalah* even though investment profit is proportionally shared. In such cases for the purposes of risk management, it is classified as *Mudharabah*
See also Ismail, E. *op cit*, p. 123.
[1048] Ismail, E., *op cit*, p. 123.
[1049] *Ibid.*

the potential matching of fees with expenses, though there could be timing differences depending on the operator's set-up and any regulatory limitations.[1050]

In addition to the above, risks for the operator are risks such as with the distribution channel and competition, which could reduce new business and thus lower the fees received. There are other risks such as with the IT system and other technical processes which can cause interruptions and business losses, as well as loss of confidence from the public.[1051]

Insurance in general is built on trust. Unlike a company that makes furniture which can point to the quality of the furniture made, potential insured must put their fate in the fact that the insurer will be around to pay claims when needed. Maintaining this trust is a major risk in insurance which must be properly managed. This is equally true in *Takaful*, but with the added requirement for the operations to be conducted in an Islamic manner.[1052] This is particular true of the Nigerian situation where the whole insurance industry is looked upon with so much derision and contempt due to the fact that insurance companies always try to avoid settling claims even where the claims have been genuinely presented. This has accounted for low-level insurance penetration and stunted growth of the industry.

As mentioned earlier, there are three major prohibited elements of Islamic law which have relevance to *Takaful*. These are *Riba* (interest), *Maysir* (gambling) and *Gharar* (uncertainty). All these need to be avoided.

[1050] Critics of the pure *Wakalah* model cite the lack of incentives for the operator to properly run the *Takaful* fund as he does not share in any surplus or profits. As income is a fee based on turnover (i.e. *Takaful* contributions), he might be tempted to write as much business as possible without proper underwriting or claims handling. This is a typical principal-agent problem.

Therefore, some operators apply a *Wakalah* model with incentive compensation (also sometimes referred to as a modified *Wakalah*) where the *Wakalah* fee comprises an upfront fee (e.g. 20%) as well as a proportional share in the underwriting surplus (e.g. 25%. A concern with this model is that it blurs the clear distinction between *Wakalah* and *Mudharabah*. It must be kept in mind that this model is disputed by Islamic scholars due to the sharing of underwriting surplus.

[1051] This has been discussed in greater detail in relation to the Nigerian context in this chapter under subheading **5.2.6.**

[1052] Ismail, E., *op cit*, p. 124.

Surplus in *Takaful* is determined as contributions less *Wakalah* fee (where applicable) less change in technical reserves (including any claims fluctuation reserves) less claims paid. The determination of technical reserves can be subjective and subject to a significant amount of *Gharar.*[1053]

Another risk or challenge with respect to *Shari'ah* or Islamic concerns is the risk that the *Shari'ah* Advisors of the *Takaful* operator have not been furnished with adequate information or have received biased information about the venture from the operator. With management facing pressure from other operators as well as from conventional insurers, there is a risk that some information will be lost in the process of seeking *Shari'ah* approval. Although small, it is a risk nonetheless. A correlated risk is the risk of incompatible or sharp practices occurring in the *Takaful* operations for which the *Shari'ah* Advisors are unaware of. This risk is reduced through the process of *Shari'ah* audits, but is not common at this time. A recent development is the appearance of external organisations offering to rate Islamic agencies as to the level of *Shari'ah* compliance.[1054]

Insurance fraud results in reputation and financial damage as well as social and economic loss to the industry. The Regulatory Commission therefore, has a major task of plugging possible areas of abuse and operators fraudulent practices in the operation of *Takaful*. This can be managed through promoting exchange of information between operators within the industry, as well as across other financial sectors' operators/regulators in respect of fraud and money laundering concerns.[1055]

[1053]Ismail, E., *op cit*, p. 125. ''In many parts of the world, under different *Takaful* jurisdictions, this fact is used to restrict the operator from receiving any share of underwriting surplus. Some operators take this to the extent of not distributing surplus to participants as well as, preferring to leave all surpluses in the *Takaful* fund. In the context of risk management, there is the risk that what is accepted practice by an operator today becomes disallowed in the future, either by the regulator, by an international body such as AAOIFI (Accounting and Auditing Board for Islamic Financial Institutions), or by the operators' own *Shariah* Council. This has the potential not only to cause difficulties with administration and other systems, but also has the potential to damage the reputation of the *Takaful* operator''.

[1054] *Ibid.*

[1055] Adamu, A.I., *op cit*, p. 138.

With respect to all these *Shari'ah* issues mentioned above, should it be discovered the *Takaful* operations were not truly *Shari'ah* compliant, the amount of damage that will be inflicted on the reputation of the *Takaful* industry will be catastrophic. These are almost identical with the credibility challenges which conventional insurance has been battling with.

Another challenge with respect to risk management which is peculiar to *Takaful* is in the approach to underwriting certain product types. Different risks can be focussed on by an insurer depending on its perceived area of expertise. For instance, an insurer with a perceived strength in managing death claims might have a focus on mortgage reducing term insurance. Similarly, an insurer related to a major banking group will most likely receive significant amount of premium from this plan, and thus, needs to strongly focus on death risks. Other insurers strength could be in investment management, and may thus focus on non-participating endowment plans (fixed guaranteed maturity amount where any excess returns go to the insurer). Yet other insurers may focus on such diverse risks such as medical plans, personal accident, or other areas where a perceived strength lies.[1056]

Takaful is sorely lacking in product breadth, depth and sophistication. Despite the rapid growth of Islamic finance and *Takaful* and the evolving nature of product development, there are still very few risk-hedging instruments and techniques in *Takaful* insurance. This emanates from the prohibition of *Riba* and *Gharar* which effectively subject the conventional tools such as options, futures and forwards inapplicable to Islamic finance.

[1056] Ismail, E., *op cit*, p. 126. ''This approach to product offerings works similarly for *Takaful*, but in *Takaful*, this can be taken a step further. Take the long term care insurance, for instance. The price of this type of plan is difficult to estimate and thus is considered quite risky due to the accumulation of premiums over a number of years and subsequent payment of significant benefits at the very end of a policyholder's life. The pricing is extremely difficult and sensitive to the level of investment assumed and the expected claims incidence is extremely difficult to predict''.

Developments are notably taking place, but nevertheless, the product structure is either too complex and complicated or simply debatable as to its *Shari'ah* compliance[1057].

5.5 POTENTIAL

The importance of the insurance-growth nexus is growing due to the increasing share of the insurance sector in the aggregate financial sector in almost every developing and developed country.[1058] Insurance companies, together with mutual and pension funds, are one of the biggest institutional investors into stock, bond and real estate markets and their possible impact on the economic development will rather grow than decline due to issues such as ageing societies, widening income disparity and globalisation. This trend is likely to be accelerated with the new foray of Islamic insurance (*Takaful*) into the economic space by essentially targeting a sizeable mass of low-income earners.[1059] The growing links between the insurance and other financial sectors also emphasises the possible role of insurance companies in economic growth. The economy would benefit from the attendant accumulation of huge micro-finance fund and expansion of the micro-finance infrastructure.[1060]

In Nigeria, Muslims constitute 70% of the population.[1061] This is expected to rise as Muslims are noted to be sceptical about the use of contraceptives to plan their families. Muslims are also noted to marry early and even more, permitted to marry up to four wives at a time. These and other demographic characteristics account for the growing population of the Muslims. Currently, Nigerian conventional underwriters and intermediaries would admit the difficulty in penetrating the northern-Muslim dominated market. Of all the 49 registered underwriters, only 3 have their headquarters located in Northern Nigeria; 62 of 510 registered brokers and none of the 37 registered loss

[1057] Syed, A.M.S., *op cit*, p. 105.
[1058] Haiss, P. & Sumegi, K., (1999), *The Relationship of Insurance and Economic Growth – A Theoretical and Empirical Analysis*, openaccess.htm.
[1059] Yusuf, T.O., *op cit*, p. 226.
[1060] Daniel, F., *op cit*, p. 3.
[1061] CIA FactBook (2015).

adjusters are located up North.[1062] These figures are instructive to illustrate the skewed distribution of insurance patronage among the geo-political zones of the country. The main reason for this could be traced to religious and cultural factors which forbid Muslims to patronize corporate entities which deal in uncertainty, gambling and interest – elements seriously forbidden in Islam.[1063] Arguably, northern Nigerian states have been adjudged to be more impoverished than their southern counterparts. This accounts for why a poverty-reducing mechanism such as *Takaful* would attract a wide clientele in the north than in the south; more so for the religious concern.[1064]

Investments are vital for economic development. Savings is a veritable source of investment funds and the large Muslim population is a veritable source for *Takaful* savings funds. A *Takaful* operating company is a major instrument for the mobilization of peoples' savings, particularly from the middle and lower income groups. These savings are channelled into diverse investments for economic growth. As discussed earlier in the chapter, the Insurance Act, 2003 has strict provisions in place to ensure that insurance funds are invested in safe portfolios like government bonds, companies with bullish records of profits and other safe business institutions. Even at that, *Takaful* operators have several avenues of non-interest yielding portfolios to invest its huge funds, accumulated through the payments of small amounts of premiums by individuals who bought the policies. These funds are invested in ways that contribute substantially to the economic development of the countries in which they do business.[1065]

Insurances are similar to banks and capital markets as they serve the needs of business units and private households in financial intermediation.[1066] The availability of Islamic insurance (*Takaful*) services is essential for the stability of the economy and can make the business participants accept aggravated risks. By accepting claims, *Takaful* also has

[1062] Nigeria Insurance Digest. See also Yusuf, T.O., *op cit*, p. 227.
[1063] Billah, M.M., *op cit.*
[1064] Yusuf, T.O., *op cit*, p. 227.
[1065] *Ibid.* p. 227.
[1066] Haiss, P. & Sumegi, K., *op cit.*

to pool contributions (premiums in conventional insurance) and form reserve funds. *Takaful* can, thus, make vital contributions to the growth of the economy by enhancing cash flow for the contributors and creating large amount of assets placed on the capital market.[1067]

The potential for *Takaful* in Nigeria is hinged in several factors, namely;

a) Large Muslim population estimated to be around 70% of the total population.

b) Established *Shari'ah* law and culture in the mostly Muslim populated areas

c) The Nigerian constitution recognizes *Shari'ah* law/legal system.

d) A large underserved insurance population;

e) A thriving insurance industry;

f) The booming oil industry and its downstream industries.

The fact that *Shari'ah* law is already being practised in Nigeria makes *Takaful* in Nigeria viable. Nigeria is a multi-religious country, with a constitution that, whilst reflecting the expectations of the different faiths, remains essentially secular.[1068] Additionally, twelve out of the nineteen northern states apply the Islamic criminal law, while four states in the south have adopted the Islamic personal law. This shows that the constitutionality of applying *Takaful* is not in dispute.

The potential of *Takaful* application in Nigeria is also evident from the challenges the conventional insurance market in Nigeria has faced over the years. First, there is low

[1067] Yusuf, T.O., *op cit*, p. 227. The Nigerian economy needs to be diversified because the overdependence on oil is proving to be a fatal error now that there is a global glut in the production of the commodity. The Nigerian economy has for so long neglected several vital sectors like agriculture and mining that used to run the country. Diversification will surely allow for more economic stability leading to an influx of foreign investments. This is where the introduction of *Takaful* has the potential of making a huge difference.

[1068] Sections 275, 276 and 277 of the Nigerian constitution provide for the application of *Shari'ah* in civil matters. This means capital punishment (*Hudud*) like the cutting off of the hand in established cases of theft or stoning of the convicted adulterer/adulteress are only applied in some states in the north. Even then the intensity of the application has fizzled out lending credence to criticism that the introduction was political in the first place.

penetration into the market with a dismal contribution of about 0.72% to the GDP. While serving the needs of the elite and employed, Nigerian insurance market seems to have neglected the lower income population of Nigeria. *Takaful* can capitalize on this huge gap.

The prospect of *Takaful* in job creation is also a huge credit. Job creation is another growth contribution to the Nigerian economy through the *Takaful* mechanism. More Muslim conventional insurance personnel might be attracted into switching their employment to the *Takaful* alternative which might trigger the establishment of Islamic financial institutions in the country. With the expected patronage of the Muslim masses, backed, of course, by effective and efficient marketing strategies, new jobs are inadvertently created for Nigerians which ultimately translates into economic growth and development.[1069]

Takaful as well serves as a guarantee to credit providers just as policyholders benefit from loss prevention services put in place by service providers and share in the surpluses recorded at the end of the accounting period. The system is also likely to reduce insurance cost and economic waste and help alleviate poverty and increase the level of corporate social responsibility of the insurance industry. The market regulator's job would also be simplified when *Takaful* grows, while legislations on *Takaful* and insurance, generally, would improve significantly.[1070]

5.6 CONCLUSION

This chapter, as the epicentre of the study, discussed the introduction of *Takaful* Operational Guidelines, 2013 by the National Insurance Commission of Nigeria (NAICOM) and the challenges it is facing in the application of *Takaful* under conventional insurance in Nigeria. General challenges as are applicable to global

[1069] Yusuf, T.O., *op cit*, p. 227.
[1070] Ahmed, O.E. in Daniel, F., *op cit*, p. 3.

Takaful practice preceded the discussion on regulatory obstacles that stand in the way of full-fledged *Takaful* take-off in Nigeria. It needs to be reiterated that Section 1 of the Insurance Act, 2003, is a notorious statutory challenge facing the application of Islamic insurance in Nigeria. The legislative absence of Islamic insurance in the Act is a grave oversight because of the implications that are bound to ensue. *Takaful* holds the aces to deepening insurance penetration in Nigeria and this omission makes it all the more curious that such an important concept could be treated with levity. The pervasive cynicism surrounding the application of conventional insurance fully paved the way for the emergence of *Takaful* as a viable alternative. However, regulatory entanglements are proving to be equally detrimental to its nascent application in the insurance industry. The legal effect of this legislative absence in the Insurance Act is resultant conflict of laws with the *Takaful* Guidelines. No serious investor would want to invest his hard-earned capital in an industry that does not have clear regulatory guarantees. In the event of conflict, the Guidelines contain no exclusive provision insulating *Takaful* from conventional insurance regulations that are inimical to its essence. Furthermore, the much taunted financial inclusion of the majority underserved Muslim population will hardly be realized if these statutory and regulatory disparities are not harmonized. The ordinary un-insured who for long harboured a disdain for insurance because of murky practices will not be easily convinced to submit to *Takaful* if the regulatory framework remains largely ambiguous.

The chapter again discussed at length the issues pertaining to risk-based management which are inimical to the smooth operations of *Takaful* in Nigeria. Comparisons were made with application of *Takaful* in different jurisdictions and lessons drawn. Detailed findings and recommendation are discussed in the final chapter of the study.

Suffice it to mention that, enforcement of market discipline on operators of *Takaful* business at this nascent stage would keep the National Insurance Commission alert to

risky or self-serving behaviours of *Takaful* operators because they are the key to its successful implementation. The issue of building trust is fundamental in this regard and must never be allowed to waiver. Trust or the lack of it has been the undoing of conventional insurance practice in Nigeria. A critical factor therefore is to set standard for healthy market conduct and practices in compliance with and in harmony with the conventional regulatory framework. This will ensure that *Takaful* transactions are structured according to the enabling legal and regulatory framework as well as fundamental requirements of *Shari'ah* law for it to thrive and develop safely. The need for regulatory clarity cannot be overemphasized.

CHAPTER 6: CONCLUSION, SUMMARY AND RECOMMENDATIONS

6.1 INTRODUCTION

The introduction of the Operational Guidelines for *Takaful* Operators in 2013 as an alternative to conventional insurance could not have come at a better time. However, this research has revealed that the statutory and regulatory discrepancies replete in the enabling insurance frameworks pose serious threats to the successful operations of *Takaful* in the quest to achieve the all-important financial inclusion and insurance penetration objectives. The effects of the fragmentation of insurance policy-making, regulation and supervision between different authorities will result in constraints for *Takaful* market development thereby creating an uneven playing field across insurance products and providers. Also the mandatory insurance policy that the insurance industry relies on so much, may give comfort to the insurance companies to stick to current business practices, and hence is somehow conflicting with market development goals in an environment that fosters innovation and competition. The challenges facing *Takaful* application in Nigeria will fetter its successful application and development if proactive measures are not taken to remedy the situation. The harmonization of the statutory and regulatory insurance instruments is a panacea, among others, that can usher in regulatory certainty and confidence thus engendering active participation of the populace and stakeholders alike. In addition, policy makers and private entrepreneurs must adopt pragmatic measures to surmount the hurdles facing *Takaful's* entry into the Nigerian economy. With vibrant statutory and regulatory instruments in place, once Muslims and non-Muslims alike come to understand the real benefits of *Takaful* and cooperative risk sharing, the evolution of the *Takaful* industry would accelerate the actualization of the underwriting projections discussed in this study.

The advent and spread of the modern system of insurance is significant in so many ways. This is an age of great human achievements. The bewildering development of modern science and technology has set in motion forces that have produced and are still producing, startling changes in our ways of thought and action, life and manners. The old order has given place to new and the agrarian society has been transformed into a modern industrial society. The process of industrialisation has been so rapid that it may aptly be described as a revolution.[1071]

It may seem paradoxical that while this revolution has brought material benefits it has increased the chances of loss of life and property. The transition from countryside and cottage to city and factory, the development in transportation including steamship, automobile and airplane, the increased use of machinery, all of these are followed by accidents, hazards and injuries. To mitigate the seriousness of their consequences and to cover the chances of loss, insurance is pressed into service to such an extent that this institution has become an essential basis of modern life and its influence can be traced in almost all spheres.[1072]

It should be noted that there is a great disparity between insurance in its earliest forms and insurance as it has developed in the course of time. In its inception, it is a mutual institution to meet the actual loss when it occurs just like it is found in *Takaful* but in its development it is a device to cover the chances of loss, i.e. risks which are abstract and indeterminate. With the passage of time and as the capitalist adventure gained ground, there evolved a contract of insurance, personal in character, whereby, instead of losses, risks or chances of loss are insured.[1073] This is the speculative aspect which *Shariah*

[1071] Muslehuddin, M., (2012), *Insurance and Islamic Law*, Adam Publishers and Distributors, New Delhi, p. ix.
[1072] *Ibid.*
[1073] Muslehuddin, M., *op cit.*

frowns at. Thus, the modern contract of insurance, stripped of the virtue of mutuality, stands, today, as an offshoot of capitalist enterprise.[1074]

Although insurance practice is comparatively new in Nigeria, it has been in existence for a very long time in Europe.[1075] However, rudimentary form of insurance has been in existence long before the advent of English Common law in Nigeria.[1076] The Nigerian Insurance Act[1077] recognises this form of insurance although it does not legislate on it.

Conventional insurance has been the dominant insurance practice in Nigeria. This is an institution which reduces risks by combining under one management a group of objects so situated that the aggregate accidental losses to which the group is subject becomes predictable within narrow limits. Insurance includes certain legal contracts under which the insurer for certain consideration promises to reimburse the insured or render services in the case of certain accidental losses suffered during the term of the agreement.[1078] Greene[1079] combines both legal and functional approach in summing up insurance. The legal, economic and social viewpoints of insurance reflect the functions, features and purposes.

As to the nature of conventional insurance in Nigeria, the Court of Appeal in *Irukwu v. T.M.I.B.*[1080] said,

[1074] Further, as a science, the modern contract of insurance is based upon the principles of probability and the law of large numbers whereby the risks are converted into a fixed cost. This is done by combining large numbers of risks and applying the principles of probability to the mass of data relating to them. Exact mathematical measurement being impossible, the risk is determined by the chance of loss as estimated from past experience. This yields no accurate results and ends in uncertainty of compensation (subject matter).

[1075] Irukwu, J.O., (1991) *Insurance Law and Practice in Nigeria*, Heinemann, Ibadan, p. 1.

[1076] Under rudimentary form of insurance, age grade and tribal associations practice some form of mutual assistance resembling a life insurance contract and *Takaful*. The members raise funds through levies and donations from which a substantial amount is presented to the next of kin of a deceased member on the occasion of the demise of such a member. Islamic insurance or *Takaful* shares these same attributes.
See also Achike, O., (1985), *Commercial Law in Nigeria*, University Press, p. 316.

[1077] Section 1 of Insurance Act 2003.

[1078] See Greene: *Risk and Insurance* (1977), 4th ed., Butterworth, London, p. 49.

[1079] *Ibid*.
See also Ivamy: *General Principles of Insurance Law*, (1984), 4th ed., Butterworth, London, p. 3. See also *Prudential Insurance Co. v. Inland Revenue Commissioners*, (1904) 2 K.B. 658. Channel, J., emphasized that an important necessity in a contract of insurance is that the event should be one which involves some amount of uncertainty. There must be uncertainty whether the event will ever happen or not or if the event is one which must happen at some time or another, there must be some uncertainty as to the time at which it will happen. Compare this position with that of *Takaful* which expressly prohibits uncertainty (*Gharar*)

[1080] (1997) 12 N.W.L.R. (pt. 531) 113.

> ''A contract of insurance should be one of utmost good faith (*Uberrimae Fidei*). The insurer and the insured must be ready, and willing to engage in such a transaction. The court cannot foist on a party by a coercive order to enter into a contractual transaction more especially that of insurance, which also follows the normal characteristics of ordinary contract.''[1081]

Furthermore, as far back as 1776, Lord Mansfield had stated that contracts of insurance are contracts of speculation.[1082] It is speculative in the sense that the insurer agrees to make financial benefit or other consideration for an uncertain specified event. The insurer is not sure when it will happen.[1083]

The development of insurance has grown ever since with the recent recapitalization which has made the Nigerian insurance industry begin a new phase of transformation.[1084]

Today, insurance business in Nigeria covers a wide field ranging from life, property, goods in transit, liabilities to marine, aviation and petroleum, with about 49 insurance and re-insurance companies operating in the market.[1085]

Conventional insurance in Nigeria is government entrenched as reflected in the various enabling laws of insurance practice discussed in the second chapter of this thesis. Government has even gone farther in making some aspects of insurance compulsory like the third party motor vehicle insurance contract. This system of insurance has succeeded in creating an endemic gap in the industry due to the exclusion of the

[1081] (1997) 12 N.W.L.R. (pt. 531) 113.
[1082] See *Carter v. Boehm*, (1776) 3 Burr p. 1905. Lord Mansfield elaborated further when he stated that ''the specific facts upon which the contingent chance is to be computed lie more too commonly in the knowledge of the accused only. The underwriter trusts to his representation and proceeds upon confidence that he does not keep back any circumstances in his knowledge to mislead the underwriter into a belief that the circumstances do not exist and to induce him to estimate the risk as if it did not exist''. See also page 1909.
[1083] Takaful, in contrast, specifically prohibits speculation.
[1084] Mr Remi Olowude, Executive Vice Chairman, Industrial and General Insurance (IGI) in an interview with *The Guardian*, Thursday December 13, 2007, p. 45.
[1085] The Nigerian Council of Registered Insurance Brokers (NCRIB) via its President, Chief Dede Ijere, while lauding the actions taken by the National Insurance Commission (NAICOM) on recapitalization process at the December edition of NCRIB members evening in Lagos. See also *The Guardian*, Thursday, December 13, 2012, p. 30.

generality of the populace who are Muslims and the pervading cynicism occasioned by fraudulent practices of the insurers. Most Nigerians do not partake in it except the compulsory third party motor vehicle insurance. Bridging this prevalent endemic insurance gap through a *Takaful* industry that is established on unambiguous regulatory foundation formed the core thrust of the thesis.

Insurance legislation in Nigeria is fairly recent compared with the commencement of insurance business. Before 1961, all companies were incorporated under the Companies Act 1922,[1086] a law passed to cope with the prospects of rapid economic development after the end of World War 1. The few existing insurance companies, like the Royal Exchange Assurance and others were incorporated like other companies under the 1922 Act.

With respect to motor vehicle insurance, the Motor Vehicle (Third Party Insurance) Act[1087] was passed into law in 1950 to operate the three well known policies of motor vehicle insurance.[1088] The Act provides a compulsory insurance for private vehicles[1089] with third party protection under the insurance cover in respect of an injury caused by the insured or his servants.[1090]

However, the first comprehensive legislation on insurance was the Marine Insurance Act, 1961.[1091] This was followed by the National Insurance Corporation Act, 1969 with the objectives of recognition of government intervention and participation in insurance and the establishment of an institution which will assert a measure of control on the out-flow of foreign exchange by way of re-insurance premiums.[1092] This was the beginning

[1086] Cap. 37, Laws of The Federation of Nigeria, 1958.
[1087] Cap 128, Laws of The Federation of Nigeria, 1958.
[1088] They are – The Act, The Third Party and Comprehensive Fire and Policies.
[1089] Section 3(1).
[1090] *Adeoye v. West African Insurance Ltd*. (1970) N.C.L.R. 409.
[1091] As codified in the Laws of The Federation of Nigeria 2004.
[1092] Speech by Mr. D. Gaston-Jones, first Managing Director of NICON, at the conference of Insurance Institute of Nigeria, 1972, p. 15.

of government entrenchment in insurance practice in Nigeria. Thus, the Act empowered the company to operate as an insurer, re-insurer, agents and brokers.

The Insurance Act, 1976 was also enacted in like manner to govern and regulate insurance contracts. The Act repealed the previous legislation of the Insurance Companies Act, 1961 and the Insurance (Miscellaneous Provisions) Act 1964. However, the National Insurance Corporation of Nigeria Act, 1969 is still operative. There is also the Insurance Decree (Act), 1997 which abolished the 1991 Act. It is noteworthy that all these laws bothering on insurance are now codified in the Laws of the Federation of Nigeria, 2004 for easy accessibility, including the 2003 Insurance Act.

It is pertinent to note that the totality of all these legislations got their sources and origin from the constitution of Nigeria which is the grundnorm.[1093]

The Insurance Act 2003 is the latest legislation on insurance matters in Nigeria today. A combined effect of the explanatory notes or a repeal of other legislations puts this Act as the sole law known as the Insurance Act 2003. Insurance is an item on the exclusive legislative list in the 1999 constitution of the Federal Republic of Nigeria. Therefore, it is only the federal legislative authority that can make laws on the subject.[1094] Thus, where there is any inconsistency with the provisions of the constitution, such inconsistency will render such legislation void.[1095]

This thesis investigated and discovered that the performance of conventional insurance practice in Nigeria has to a great extent been dismal. This institution of sophisticated insurance system has not lived up to its billing in the purpose the industry was set out to achieve. It is disheartening to note that the insurance industry which ought to be a growth sector has been struggling and stagnant despite its vast potential in the country.

[1093] See Section 1(3) of the 1999 constitution (as amended).
[1094] See second schedule (legislative powers) constitution of the Federal Republic of Nigeria, 1999.
[1095] Section 1(3) *supra.*

It is on record that out of a population of over 150 million Nigerians, only about 800,000 of the adult population have any form of insurance cover whatsoever.[1096] Several factors have been identified as reasons for the unimpressive performance. These include circumscription of the powers of the National Insurance Commission (NAICOM), inadequate capital, limited human and technical capacities, and low-level confidence by the populace.[1097] However, what have been identified as the most critical challenges are the twin problems of lack of public awareness or financial literacy[1098] for insurance and the absence of public confidence in the system. This thesis has researched and recommended solutions to these problems so that the insurance sector can play its catalytic role in the growth and transformation of the Nigerian economy.[1099]

The Nigerian insurance sector's capital requirements of N3 billion for General Business; N5 billion for Life Business and N25 billion for Re-insurance are arguably the highest in Africa and among the highest in the world and have the major advantage of eliminating fringe players from the market such that the remaining insurers have adequate financial capacity to settle genuine claims as well as participate in the ''big ticket'' risks.[1100] But this has done little to galvanize the industry in terms of patronage. The insurance sector has continued to face crisis of confidence,[1101] as the insuring public continues to hold insurance with contempt. The study discovered that today, the average insurer in Nigeria is perceived by the insuring public as eager to collect premium only to repudiate claims at the slightest opportunity.[1102]

[1096] Dateline Insurance Magazine, (2013), vol.3, No. 3., July/August, p. 5.
[1097] *Ibid.*
[1098] One of the major obstacles identified by this study in the universal fight against the prevalence of financial exclusion is the lack of financial literacy among the Nigerian populace. The observed gap in financial literacy is especially wide among women and of course the less educated segment of the society. Therefore, it is evident that people often lack the ability to save and manage their little earnings for effective personal financial decisions. For instance, lack of financial education leads many people to erroneously understand insurance as something that can only be done when there is disposable income. This idea forms the basic understanding on risk and the need for mitigating it among many Nigerians.
See also Kollere, A.U., (2014), *Takaful* Insurance: Towards Deepening Insurance Penetration, p. 1.
[1099] Dateline Insurance Magazine, *op cit.*
[1100] (2013), Dateline Insurance Magazine, *op cit.*
[1101] According to Yusuf, T.O., the Nigerian insurance industry is today ranked 65th globally in terms of size and 6th out of the 8 largest markets in Africa. The sector has contributed less than two per cent to the Gross Domestic Product (GDP) due to systemic failures of regulation and supervision.
[1102] Yusuf, T.O., *op cit.*

At the technical level, some constraints that have contributed to the pervasive problems of the Nigerian insurance industry include the circumscription of the regulator which has led to the fettering of its discretion because, presently, the desired autonomy for the insurance regulator is still far-fetched and less proactive.[1103] The issue of deepening insurance penetration must be addressed quickly if the insurance industry is to overcome its hydra-headed problems.

This thesis also discovered that by far, the most critical contributory factor to the lack of growth of the insurance industry in Nigeria could be viewed from the Islamic perspective. The concept and nature of conventional insurance practice which stands at variance with the principles of *Shari'ah*, has succeeded in no small measure in financially excluding about 70 per cent of the Nigerian population who are Muslims. The conventional insurance product as packaged today is un-Islamic in its entirety. The Nigerian Muslim population which is the greater majority is reluctant to participate in conventional insurance schemes because of the gambling (*Maysir*), interest (*Riba*) and speculation or uncertainty (*Gharar*) obstacles. Conventional insurance has in its very embodiment anti-*Shari'ah* features which are integral to the survival of its operations. Thus *Gharar* (uncertainty), *Riba* (interest) and *Maysir* (gambling) will always remain abhorrent to the average Muslim no matter how attractive the insurance product may be.

It needs to be state in unequivocal terms that it is the very nature and concept of conventional insurance itself that has been largely responsible for the emergence and rapid spread of *Takaful*[1104] as a viable insurance alternative on the global financial stage.

[1103] Dateline Insurance Magazine, *op cit*, p. 3.

[1104] Khurshid Ahmad in Muslehuddin, M., (2012), *Insurance and Islamic Law*, Adam Publishers and Distributors, New Delhi, p. ix., said ''The Muslim world is faced with a disturbing situation: some of the important legal and socio-economic institutions which have developed in the West during the last four hundred years and which have made strong inroads in the Muslim society are, in their present form and structure, in conflict with the values and principles enunciated by Islam. The course of history has forced these institutions and organisations over us and we are, wittingly or unwittingly, the victims of this situation. The Muslim scholars are becoming more and more conscious of this conflict and are applying themselves of the task of wriggling the Muslim society from it. To achieve the purpose, it is necessary that an objective study of the contemporary institutions and of the law of Islam should be made and then attempts should be made to develop alternate institutions which can fulfil our needs without violating the fundamental principles of Islam, Insurance is one such problem''.

Takaful is not a product but a concept. It is not about religion really. It is about a way of sharing risks and not transferring risks. *Takaful* is a kind of community sharing and it doesn't matter whether one is a Christian or Muslim.

Unlike conventional insurance, *Takaful* complies with *Shari'ah* principles of compensation and shared responsibilities in the community. It has been expanded to cover general risks, health and family (life) plans for Muslim communities. Muslim faithful believe that insurance should be based on principles of mutuality and cooperation and this means shared responsibility, joint indemnity, common interest and solidarity. In *Takaful*, the policyholders are joint investors with the insurer (*Takaful* operator), who acts as manager for the policyholders. The policyholders share in the investment pool's profits as well as its losses. A positive return on policies is not legally guaranteed, because in Islam, any fixed profit guarantee is equivalent to paying interest.[1105]

Tracing its history, Islamic insurance or *Takaful* in Arabic, means joint guarantee. In practice, however, it can be visualized as a pact among a group of members or participants who agree to jointly guarantee one another against loss or damage that may be inflicted on them. Each member of the group pools effort to support the aggrieved member. This is similar to some customs or traditions practiced in Arab societies during the *Jahiliyyah* (before the advent of Prophet Muhammad pbuh) period, where mutual help was extended within the society upon the death of its members.[1106] They contributed together in terms of energy to help settle the funeral affairs of the deceased

[1105] Daniel, F., (2012), Challenges, Prospects of *Takaful* Insurance, *ThisDay* Newspaper Article, http://www.thisdaylive.com/articleschallenges-prospects-of-takaful-insurance/118793/accessed on Thursday 06 August, 2015, Updated 11:24

[1106] Yusuf, T.O., (2012), Prospects of *Takaful*'s (Islamic insurance) Contributions to the Nigerian Economy, *Journal of Finance and Investment Analysis*, vol. 1, No. 3, 2012, 217-230, ISSN:2241-0988. P. 222.

member. Some were more sympathetic and went farther to offer material or financial assistance to the deceased family.[1107]

During the era of Prophet Muhammad pbuh, some of the practices of the *Jahiliyyah* were continued. This specifically involved the payment of compensation to the relatives of the deceased in one tribe when killed by a person from another tribe. The practice was thought to be able to reduce the tension between the tribes, as the Arabs during that era, were more prone towards revenge. This practice of paying compensation is called *Diyat* or blood money and must be paid by the killer's relatives (*Aqilah*) to the heirs of the deceased. This was later extended to include that if a member of a tribe killed someone from another tribe, all the members of that tribe must be held responsible to compensate the deceased's relatives under the doctrine of *Aqilah* enshrined under Article 3 of the Madinah constitution.[1108]

The preliminary performance of *Takaful* in Nigeria is in fits and starts. The African Alliance Insurance Company Limited, being the oldest and strongest specialist life assurance and pension office, blazed the trail in introducing Islamic finance (*Takaful*) into the market in 2003. Since then, other two conventional insurance companies have joined the fray. These are Niger Insurance Plc and Cornerstone Insurance Plc. As a composite insurance company, Niger Insurance Plc transacts all classes of insurance businesses and offers a wide range of insurance products and customer-oriented services to its growing clientele. In addition, they support their products with one of the most efficient and constantly improving claims settlement procedures in the insurance market. Cornerstone is an ethical, dynamic and innovative custom products supplier for the large Muslim population in Nigeria and decided to establish *Halal Takaful* Nigeria

[1107] Yusuf, T.O. *op cit.*.
[1108] Fisher, O. & Taylor, D.Y., (2000), Prospects for the Evolution of *Takaful* in the 21st Century, available at http://www.takaful.comsa/m4sub3.asp.openaccess.htm.

for that purpose.[1109] Of the three existing *Takaful* underwriting companies, only Cornerstone Plc offers a separate *Takaful* office. It is being run by one of its subsidiaries – *Halal Takaful* Nigeria. Here assets of *Takaful* are not merged with the conventional insurance funds.[1110]

As part of the National Insurance Commission's (NAICOM)[1111] on going pursuit to increase insurance penetration in Nigeria and increase the contribution of insurance to the National GDP, the need for *Takaful* was identified following detailed research.[1112] *Takaful* insurance is a form of insurance which incorporates elements of mutuality and ethical finance considerations and is open to all people regardless of faith and background. Furthermore, the Guidelines for *Takaful* insurance provide guidance on elements that are specific to the operations of a *Takaful* insurance Operator.[1113]

The core subject of this research is the challenges being encountered in the application of *Takaful* under conventional insurance practice in Nigeria. The thesis researched into the statutory and regulatory insurance frameworks contained in the Insurance Act, 2003 amongst others and the newly released *Takaful* Insurance Guidelines for *Takaful* Operators with a view to harmonizing the inherent regulatory discrepancies. Without a vibrant regulatory framework in position the application of *Takaful* is bound to be a doomed project. In spite of the unanimous acceptance of *Takaful* as a vehicle for deepening insurance penetration, financial inclusion and poverty reduction in Nigeria, the thesis discovered that these lofty ideals may not be achievable unless the challenges of conflicting regulations and weak enforcement mechanisms are tackled. That has been the aim of this research.

[1109] Yusuf, T.O., *op cit,* p. 226.
[1110] *Ibid.*
[1111] Section 1.1 of the *Takaful* Operational Guidelines for *Takaful* Operators, 2013. These Guidelines were issued pursuant to Section 7 of the NAICOM Act 1997.
[1112] Section 1.2 of *Takaful* Operational Guidelines for *Takaful* Operators, 2013. These Guidelines are issued to provide regulatory guidance for *Takaful* insurance in the industry with the desire of enhancing financial inclusion in Nigeria and to ensure *Takaful* insurance providers are not disadvantaged.
[1113] Section 1.3 of the *Takaful* Operational Guidelines for *Takaful* Operators. These Guidelines are to be read in conjunction with all other relevant legislations, guidelines and circulars as determined to be applicable to *Takaful* insurance Operators by the Commission. The Guidelines will represent the primary regulatory framework with regards to *Takaful* insurance.

The research has established that in spite of the resilience and appreciable performance of *Takaful* in similar multi-religious, multi-ethnic societies like Nigeria, the prospect of replicating such success in Nigeria is dependent on so many variables. Apart from overcoming the challenges of statutory and regulatory discrepancies, the prospect of integrating *Takaful* within the existing legal framework of insurance in Nigeria also depends on the dynamic application of the provisions of the various enabling legislations by the regulator. It is also significant for the regulatory framework to be applied dynamically to support outsourcing of relevant skills and to develop effective internal control structure within the regulated *Takaful* operators.

Once the insurance industry is able to put its acts together and close the endemic gap in insurance practice by putting in place a solid regulatory *Takaful* insurance framework, ''the future of Nigerian insurance industry is going to be eventful and vibrant as the industry deepens insurance penetration through micro insurance and *Takaful*. It is expected that the contribution of insurance to the GDP will increase tremendously when these opportunities are harnessed in the coming years.''[1114] The imperative for an enabling robust legal and regulatory framework (e.g.*Takaful* Act)[1115] that will have *Takaful* engrained and engender its application, integration and growth in the Nigerian insurance terrain is the premise on which this thesis is established. A good regulatory environment underscores the importance of having a well-functioning authority. This enhances trust and confidence in the industry.

6.2 SUMMARY OF FINDINGS

The modest contribution of this thesis towards unearthing and overcoming the general and regulatory challenges of the nascent *Takaful* industry in Nigeria does not claim

[1114] Nigerian Insurance Statistics Directory Publication of the Statistics Unit, Directorate of Research and Statistics, National Insurance Commission (2011), at p. 9.
[1115] See the new Malaysian Islamic Financial Services Act (IFSA), 2013, which effectively repealed the 1984 *Takaful* Act. The new Act is contained in a new legislation that combines the *Takaful* Act 1984 and Banking Act 1983 in a single Act.

exclusivity in the realm of solutions. However, it is submitted that the findings of the study are clear pointers to positive outcomes of the research conducted in a quest to play a part in finding solutions to the insurance industry's numerous challenges. The most important findings of the research are summarized below:-

This research revealed the imperative for a *Takaful* legislation in Nigeria similar to the *Takaful* Act in Malaysia[1116] to cater for *Takaful* insurance in a comprehensive manner. The thesis established that there was no provision or express mention of Islamic insurance or *Takaful* in the Insurance Act 2003. The Act, which is the primary legislation regulating insurance business in Nigeria makes no mention at all of such an important component of insurance practice recognized the world over. Section 1 of the Act[1117] delineates its area of regulation by limiting its operations to all insurance businesses and insurers other than the insurance business carried on or by insurers known as friendly societies and company or persons established outside Nigeria to engage solely in reinsurance business. A careful perusal of the provision shows an express omission of the term *Takaful* or Islamic insurance. This absence of mention in insurance legislation is a grave error that is bound to lead to ambiguities in the complex application of *Takaful* under conventional insurance. The draughtsmen probably did not envisage that *Takaful* would gain such prominence and importance within a short period of time in the global insurance terrain hence their misjudgement in specifically not providing for it. *Takaful* is not the same thing as conventional insurance and as such should have been expressly mentioned alongside conventional insurance. The resultant ambiguity is bound to make potential investors and participants consider the situation as too risky to invest their hard earned capital into high levels of uncertainty. Furthermore,

[1116] Malaysia now has a new legislation on *Takaful*. The Islamic Financial Services Act, 2013 (Act 759) came into force on June 30, 2013. It is a lengthy statute that repealed two important Acts which governed Islamic finance in Malaysia, namely the Islamic Banking Act 1983 (Act 276) and *Takaful* Act, 1984 (Act 312) ('TA 1984'). The IFSA was passed by the Parliament of Malaysia [House of Representatives (Dewan Rakyat) on 28 November, 2012 and House of Senate (Dewan Negara) on 19 December, 2012. The Federation of Malaysia practices a bicameral legislative system where the House of Representatives serves as the Lower House and House of Senate functions as the Upper House in passing the laws] together with its sister legislation, the Financial Services Act, 2013 (Act 758) ('FSA 2013'). Both Acts officially came into force on June 30, 2013. See Abd Hamid, M.H. & Hassan, R., (2014), Islamic Financial Services Act 2013: A Preliminary Note on its Impact on *Takaful* Industry, *Malaysian Law Journal*, p. lxv.

[1117] Insurance Act 2003

Takaful operators might be reluctant to invest more on marketing and product development since there are no express legal guarantees. Lack of regulatory clarity erodes trust and confidence.

The study recognized that since *Takaful* insurance is relatively new in Nigeria there is the need for adequate implementation of *Takaful* Operational Guidelines, 2013, if the nascent industry is to thrive. It is paramount that the operational requirements be adequately enforced by the National Insurance Commission (NAICOM) which is the chief regulating body and other relevant agencies involved in insurance regulation. There is the need to set out clear principles on how to manage *Takaful* funds and how *Takaful* business should be taxed.

Equally important is the essential need to create a regulatory regime that does not treat *Takaful* less favourably than conventional insurance in Nigeria. This is necessary to promote virile *Takaful* practices that are consistent with *Shari'ah* principles and NAICOM regulations in Nigeria.[1118]

The thesis established that there is an urgent need for regulatory clarity because the *Takaful* Operational Guidelines are already in conflict with some provisions of the Insurance Act[1119] thereby stalling the effectiveness and efficiency of the application of *Takaful*. Clear regulatory and supervisory guidelines have the propensity to clear foggy areas for all stakeholders. This view corroborates that of Saad, Gambo and Kassim who stated that potential investors will question the nature of murky Nigerian insurance legislation[1120] towards the application of *Takaful*.

[1118] Fadun, O.S. *op cit*, . 22.
[1119] Insurance Act 2003.
[1120] Gambo, G., Saad, N. & Kassim, S., (2014), ''Assessing the Impact of Islamic Micro-Finance on Poverty Alleviation in Northern Nigeria. *Journal of Islamic Economics, Banking and Finance*, Vol. 10, No. 4, October-December, 2014. Available at http;//ibtra.com/journal_current_issue.php.

The research also discovered that there is a need for clarification of the provisions of Section 9 of the Insurance Act[1121] which provides for minimum paid up capital for insurance companies in Nigeria but was relaxed in the *Takaful* Guidelines to scale down the minimum paid up capital. This accommodation of *Takaful* is however, controversial as the Commission's power under the Act relates only to upward review of the minimum paid-up capital of an insurance company and not its downward scaling.[1122] It remains arguable whether the power to increase paid-up share capital vested in the Commission would accommodate the discretion to decrease the prescribed minimum share capital.

Closely connected to the above issue, the study revealed that there is an imperative to make clear the provisions of Section 10 of the Insurance Act[1123] which requires an insurer/*Takaful* operator intending to commence business to deposit the equivalent of fifty per cent of the paid-up share capital with the Central Bank of Nigeria (CBN) as its statutory deposit. However, after registration, eighty per cent of the statutory deposit would be released to the insurer/*Takaful* operator with interest not later than sixty days after registration. The Section further stated that in the case of an existing company, ten per cent of the paid-up share capital shall be deposited with the CBN attracting interest rate at CBN on the 1st of January each year. The issue of interest (*Riba*) is what is unacceptable to a *Takaful* operator because it clearly violates *Shari'ah* principles.

The thesis recognized the prerequisite for harmonization and standardization of the provisions of Section 25 of the Insurance Act and the *Takaful* Guidelines on investment portfolio. The basic requirements of investment in *Takaful* are its compliance with *Shari'ah* principles. This presupposes that the investment must be devoid of the *Shari'ah* prohibitive elements. The *Takaful* Operational Guidelines require the operator

[1121] Insurance Act 2003.
[1122] See Section 9(4) Insurance Act 2003.
[1123] Section 10 of Insurance Act 2003.

to establish investment policies according to the two separate funds. However, Section 25 of the Insurance Act provides for investment by an insurer in a totally different way from the provisions of the *Takaful* Guidelines. The thesis established that there was no express exemption of *Takaful* from the requirements of Section 25 of the Act. Furthermore, interest (*Riba*) is a key component of admissible assets under Section 24(13) of the Insurance Act, while under *Takaful* interest is a prohibitive factor in the transaction. What remains unclear is whether Section 25 of the Act will apply to *Takaful* insurance. If the provisions of the Act apply besides the requirements of *Takaful* investment in the Guidelines, the *Takaful* operator must also meet the requirements of Section 25 of the Law. The supremacy of the Act in regulating insurance business in Nigeria has been clearly stated in Section 100 of the Act.[1124]

The study discovered the necessity for clarification on civil jurisdiction and laws in matters affecting *Takaful* contracts that are to be enforced. *Takaful* contracts are supposed to comply with *Shari'ah* principles and rules, as well as laws of the civil jurisdiction. This is a potential area of friction because of the fundamental differences in Islamic and conventional laws. The issue of jurisdiction is critical here because there is no exclusive clause in the *Takaful* Guidelines safeguarding the application of pure *Shari'ah* rules and principles in *Takaful* matters.

The study established the requirement for strengthening the *Shari'ah* Advisory Council by the National Insurance Commission (NAICOM) which is the chief regulator, to enhance the role and function of the Council. It should be accorded the status of the sole *Shari'ah* authority in *Takaful* matters in Nigeria. In the event there are disputes involving *Shari'ah* issues, the court or arbitrator will refer to SAC to resolve the matter.

[1124] Section 100 of the Insurance Act 2003.

Its decisions should be binding on all. This exclusive authority needs to be inserted in the Insurance Guidelines.[1125]

The thesis acknowledged the prerequisite for adequate and effective legislative framework for insurance practice because the current provisions look good on paper but lack strong enforcement capacity. The National Insurance Commission (NAICOM) has no power of arrest irrespective of the fact that there are sanctions provided in the law. This area of administration and enforcement has been the bane of insurance practice in Nigeria and will impact negatively on *Takaful* if not checked.

The thesis also identified the imperative for clarity of responsibility in the event of a breach by a *Takaful* agent. A *Takaful* agent, as an intermediary, is a legal agent of a *Takaful* operator (as the principal). However, agents and principals are also bound by common law rules governing agency relationships. The complication, it was discovered, could arise where participants claim for their rights as a result of any misconduct of an agent. If proven that the agent acted beyond his powers, the *Takaful* operator or principal may deny liability.

The research established the necessity for supportive policy objectives and risk-based approach to supervision which will give the regulator the room to tailor supervisory activities to reflect the demand of a regulated entity (risk sensitivity). Sound regulatory and supervisory system is necessary for the maintenance of efficient, safe and sustainable *Takaful* industry. Supervisory objectives need to be clearly defined and religiously observed.

[1125] In the Central Bank of Malaysia Act 2009, the role and functions of the SAC was further reinforced, whereby the SAC was accorded the status of the sole authoritative body on *Shari'ah* matters pertaining to Islamic banking, *Takaful* and Islamic finance. While the rulings of the SAC shall prevail over any contradictory ruling given by a *Shari'ah* body or committee constituted in Malaysia, the court and arbitrator are also required to the rulings of the SAC for any proceedings relating to Islamic financial business, and such rulings shall be binding. See also Sections 54, 55(2)(a), 55(2)(b), 57 and 58 of CBMA 2009.

The study also acknowledged the requirement of having competent supervisory staff that are knowledgeable in the workings of *Takaful* and at the same time having in-depth knowledge of *Shari'ah* jurisprudence (*Fiqh*) and supervision expertise.

Closely tied to the above finding is the need for choosing an appropriate accounting standard platform like the Auditing and Accounting Organisation for Islamic Financial Institutions (AAOIFI) and International Financial Reporting Standards (IFRS). The support of the agencies to overcome the challenges of manpower, developing Islamic capital market, as well as *Shari'ah*-compliant investments is very much critical to the success of the nascent insurance industry.

The imperative to have adequate *Qard Hasan* (loan) fund in the early years of the *Takaful* practice in Nigeria was discovered to be a critical issue. In the same vein, there is the need for adequate regulatory mechanism to ring-fence and protect the reserve from abuse by *Takaful* operators through related party transactions.

The study established the fact that proper caution must be exercised in managing risks by participants and operators if the integrity of the nascent industry is to be preserved. Insurance in general is built on trust. Maintaining this trust is a major risk in insurance which must be properly managed. It is imperative that the transactions must be concluded in an Islamic manner. Insurance fraud results in reputational and financial damage as well as social and economic loss to the industry. The regulatory Commission therefore, has a major task of plugging possible areas of abuse by operators in the practice of *Takaful.*

The study found that there is a need for dynamic application of the provisions of the enabling insurance legislations by the regulator. It is also of significant effect for the regulatory framework to be applied dynamically to support outsourcing of relevant skills, develop effective internal control structure within the regulated *Takaful*

operators. There is an attendant need for the effective deployment of the Audit Committee, Risk Management Committee, Corporate Governance and the Advisory Council of Experts (ACE) in line with the enabling guidelines to engender the protection of the interests of the policyholders thereby discharging the Commission's responsibility under the law.[1126]

The imperative to employ positive steps developing reliable channels of marketing and distribution of *Takaful* products as well as adequate regulatory control mechanisms to avoid faking products and the abuse of public trust was adjudged by the thesis to be vital. The thesis further found the necessity to develop dynamic and boisterous *Takaful* markets through inter-regulatory synergy and collaborative efforts of the Commission and other key regulatory agencies. The contributions of CBN and SEC are crucial to the operations of *Takaful* particularly in the development of non-interest banking and investment portfolios on which the entire operational functions of *Takaful* are anchored. The imperative of this collaboration is not only limited to the issues of investment but also to engender a robust control cycle in order to create healthy growth of the *Takaful* industry within the legal framework of the entire financial sector.

The thesis also established the obligation to create general awareness about *Takaful* because the issue of awareness is of fundamental importance to its success. The imperative for high level customer awareness for *Takaful* and its products is fundamental for it to thrive. People need to be made aware that *Takaful* provides an acceptable religiously validated solution[1127] to the issue of insurance. There is also the need to overcome negative perceptions about *Takaful* and prove to the market that its

[1126] Section 7(h) NAICOM Act 1997.
[1127] Ismail, E., op cit, p. 126.

operators are capable of providing competitive services that are on par with other or better than conventional insurance companies.[1128]

The study discovered the need for a robust human resources development strategy to combat the dearth of *Shari'ah* and *Takaful* expertise. The Nigerian market faces severe shortage of qualified staff that have adequate knowledge and experience about *Takaful*, as well as understanding of Islamic finance.

The non-existence of uniform terminologies and the degree of unresolved *Fiqh* issues informed the finding of this research on the necessity of having in place, initiatives that will ensure that *Takaful* business can expand by providing rules and regulations that are acceptable to the majority of the populace. Differences in interpretation in Islamic finance are gaps that need filling or narrowed in other to overcome the challenges.

The research revealed the requirement for *Takaful* operators to sustain the momentum garnered by the introduction of *Takaful* with the initiative of constantly enhancing products innovation and providing excellent service delivery. This is what endears customers to become addicted. They must be able to understand evolving customer and market-specific needs and be willing to renew or re-engineer product design and consumer benefit packages, as well as expand customer reach across various distribution channels.[1129]

The study also recognized the importance for Nigeria to improve its information technology profile in order to get the best out of *Takaful*. The speed of technological development in the *Takaful* segment must be matched by such developments in the general market place. As such, a good and efficient information system is required should *Takaful* companies wish to be at par with the rest of the players currently in the

[1128] *Ibid*, p. 127.
[1129] Ismail, E., op cit, p. 126.

industry.[1130] The phenomenal growth of the internet has transformed society tremendously and this has changed the way people communicate, exchange information, sell products, etc. *Takaful* is no exception to this rule.[1131]

The thesis identified the need for the issue of re*Takaful*, which is a worldwide problem, to be ironed out immediately. Since the *Takaful* market in Nigeria is still very young, there is the need that adequate safeguards be put in place in anticipation of the rapid growth expected of *Takaful*. It is imperative for *Takaful* operators to collaborate to establish a re*Takaful* facility or pool in Nigeria.

The study acknowledged that it is incumbent for the Nigerian *Takaful* operators to adhere strictly to the issue of fund management and investments. As custodians of public funds, there is the need for *Takaful* operators to ensure that funds are not only soundly but more importantly safely managed. On investment portfolio, the thesis found that there is a need for all relevant stakeholders in the *Takaful* industry like government authorities in Nigeria and in Islamic countries, financiers, bankers including central bankers, *Takaful* operators, economists and *Shari'ah* scholars to study, develop and promote the diversity of investment instruments an products acceptable to *Shari'ah.*[1132]

The study also revealed that it is imperative for adequate infrastructure to be in place in order to guarantee the successful implementation of *Takaful*. Immature Islamic banking system and poor communications infrastructure are challenges that need to be tackled headlong. There is a need for availability of appropriate skills and resources to manage *Takaful's* teething problems.[1133]

[1130] Syed, A.M.S., *op cit*, p. 104.
[1131] Rahman, Z.A. & REdzuan, H., *op cit*, p. 84.
[1132] Ismail, E., *op cit*, p. 132.
[1133] Stagg-Macey, C., (2007), *An Overview of Islamic Insurance,* No. 8. sabbir@icmif,org.

6.3 RECOMMENDATIONS

6.3.1 *Takaful* Act

This thesis recommends that an Act, similar to the Malaysian *Takaful* Act,[1134] titled ''***Takaful* Act''** be enacted by the National Assembly[1135] of the Federal Republic of Nigeria which should cover all direct and indirect issues raised in relation to the subject of this research. The proposed Act should harmonize all the statutory and regulatory discrepancies that are inimical to the successful application of *Takaful* inherent in all the enabling insurance instruments. The realization of the full potential of *Takaful* will only come about with the enactment of a comprehensive and robust legal framework to reflect its peculiarities, address areas of its challenges and create a level playing field for competition with conventional insurers.

6.3.2 Amendment of Insurance Act 2003

The thesis recommends the amendment of **Section 1 of Insurance Act, 2003**, to expressly reflect the mention of *Takaful* insurance or Islamic insurance. The effect of this express mention will have *Takaful* engrained and put at par with conventional insurance. It will effectively clear all ambiguities in the most important insurance instrument in the Nigeria insurance industry.

6.3.3 Amendment of all Existing Insurance Legislations to Expressly Include *Takaful*

The research recommends that all insurance legislations in Nigeria be amended to include *Takaful* in order to bridge the gap caused by legislative absence of *Takaful*

[1134] *Takaful* Act 1984, now Islamic Financial Services Act, 2013. It wouldn't be possible for Nigeria to have an Act exactly in the mould of the Islamic Financial Services Act, 2013 which lumped the Banking Act and the *Takaful* Acts together. In Nigeria, it is not the Central Bank or Bank Negara that is in charge of insurance in the country. The responsibility rests with the National Insurance Commission (NAICOM) which is the chief regulatory body. NAICOM in turn reports to the Federal Minister of Finance. The Central Bank of Nigeria CBN is solely in charge of all banking matters. Insurance is not under the regulatory precinct of banking legislations and control.

[1135] The National Assembly of Nigeria comprises of the Senate which is also known as the upper chamber and the House of Representatives which is known as the lower chamber. National Assembly members are evenly drawn from all the 36 states of Nigeria including the Federal Capital Territory.

mention in the insurance instruments. The recent emergence of *Takaful* as a commercial ethics-based insurance was never in the contemplation of the framers of most of the enabling insurance legislations that regulate the business of insurance in Nigeria. This has resulted in creating a gaping gap in the link between the *Takaful* regulations and the existing insurance frameworks. The holistic review of the enabling legislations is to identify *Takaful* as a full-fledged insurance business in Nigeria.

6.3.4 Regulatory Clarity in *Takaful* Guidelines

The thesis recommends that the *Takaful* Guidelines be amended and clarified where the provisions seem to be in conflict with those of conventional insurance. The need for regulatory harmonization cannot be over-emphasised as this will help assure the insuring public and investors alike. A good regulatory environment underscores the importance of having a well-functioning authority. This enhances trust and confidence in the industry.

6.3.5 Amendment of Sections 9, 10 and 25 of the Insurance Act

The research recommends the amendment of Section 9 of Insurance Act which allows for review of paid-up share capital. The provision of Section 9(4) only allows for upward review but the study found that the provision was breached to accommodate downward review of *Takaful* paid-up share capital. The provision here needs to be amended and harmonized to enhance regulatory clarity.

The thesis also recommends the amendment of Section 10 of the Insurance Act which requires an insurer/*Takaful* operator intending to commence business, to deposit the equivalent of fifty per cent of the paid-up share capital with the Central Bank of Nigeria (CBN) as its statutory deposit. The crux of the matter here is the annual interest which the deposit attracts in interest (*Riba*) at the beginning of each year which is inimical to the operations of *Takaful* because of strict *Shari'ah* requirement principles. The

provision should be amended to be in harmony with *Shari ah* requirements otherwise it is unenforceable under *Takaful.*

The research also recommends that amendment be made to the provisions of Section 25 of the Insurance Act which border on investments by insurers. The issue of investment is quite different from what obtains under *Takaful* as contained in the *Takaful* Operational Guidelines because the basic requirements are compliance with *Shariah* principles. There is no express exemption of *Takaful* from complying with investment provisions under the Act. The amendment is necessary to harmonize the provisions of both insurance legislations pertaining to investment portfolio.

6.3.6 Clarification on Jurisdiction

The thesis recommends that the issue of jurisdiction be clarified on matters affecting *Takaful* application because *Takaful* is quite different from conventional insurance. Conflict of laws are bound to arise and the released *Takaful* Guidelines have been silent on the exclusivity of *Shariah* law application on *Takaful* practice contrary to what obtains in the laws of other *Takaful* operating countries.

6.3.7 Sole *Shari'ah* Authority on *Takaful*

The thesis recommends an amendment to the *Takaful* Guidelines to insert a provision making the *Shari'ah* Advisory Council (SAC) the sole authority in *Takaful* matters in Nigeria. In the event there are disputes involving *Shari'ah* issues, the court or the arbitrator will refer to SAC to resolve the matter. This is similar to what obtains in Malaysia. The Guidelines should also mention that SAC will act as an independent body to ensure high level of integrity among members of SAC, in order to obtain greater public confidence and trust.

6.3.8 Enforcement Mechanism

The thesis recommends effective enforcement machinery by NAICOM for it to enforce its provisions that are violated. The power of arrest and prosecution must be made abundantly clear in order to deter violators.

6.3.9 Clarifying Agent's Liability

The research recommends that clarification be made by the Commission on the liability of an agent in the event of a breach of agency under *Takaful*. In as much as *Takaful* is different from insurance, however, agents and principals are also bound by common law rules governing agency relationships. This needs to be clarified and harmonized because continued adherence to common law rules on the subject will work unfairness on *Takaful* operators and participants by eroding trust.

6.3.10 Supportive Policy Objectives

The thesis recommends the adoption of supportive policy objectives and risk-based approach to supervision which will give the regulator the room to tailor supervisory activities to reflect the demand of a regulated entity (risk sensitivity). Supervisory objectives are to be clearly defined and religiously observed.

6.3.11 Outsourcing of Competent Staff

The thesis recommends the outsourcing of competent staff that have in depth knowledge and vast experiences in the field of insurance and *Takaful* as well as *Shari'ah* jurisprudence (*Fiqh*) and supervision expertise.

6.3.12 Appropriate Accounting Standard

The thesis recommends the choice of the Accounting and Auditing Organisation for Islamic Institutions (AOIFI) as the default accounting standard for accounting in Nigeria because the International Financial Reporting Standards (IFRS) are too

complicated and controversial for an emerging *Takaful* market like Nigeria to contend with.

6.3.13 *Qard Hasan* (Loan)

The thesis recommends the ring-fencing and protection of this reserve fund by the regulators in order to forestall its abuse through related party transactions.

6.3.14 Developing Reliable Channels of Marketing and Distribution of *Takaful* Products

The thesis recommends the employment of positive steps to develop reliable channels of marketing and distribution of *Takaful* products as well as adequate regulatory control mechanisms to avoid faking products and the abuse of public trust. The thesis also recommends the development of dynamic and boisterous *Takaful* markets through inter-regulatory synergy and collaborative efforts of the National Insurance Commission (NAICOM) and other regulatory agencies.

6.3.15 Creating Awareness

The thesis recommends an aggressive enlightenment campaign drive on *Takaful* insurance practice. The issue of awareness is so critical to the success of *Takaful*. There must be high level customer awareness of *Takaful* and its products. The regulator is enjoined to employ the services of traditional rulers, religious leaders, community leaders, the National Orientation Agency, television jingles, rallies in market arenas on market days, drama shows, film shows, radio jingles, door to door campaigns, messages on billboards, posters, flyers etc, in order to reach out to the teeming customers out there that are yet to be tapped.

6.3.16 Robust Human Resources Development Strategy

The thesis recommends a robust human resources development strategy to overcome the crippling challenge of dearth of expertise and adequate human resources to man the *Takaful* industry. The *Takaful* operators will need to allocate sufficient funds specifically for this project. Special programs should be initiated to train the manpower not only on the technical aspects of insurance but also in areas covering finance and investment as well as the appreciation of *Shari'ah*. It is also suggestive for the National Insurance Commission of Nigeria (NAICOM) to encourage universities to restructure their syllabi to incorporate *Takaful* into the fold of insurance profession. The curriculum of Chattered Insurance Institute of Nigeria (CIIN) and West African Insurance Institute[1136] (WAII) should be expanded to offer training and professional certification in the field of *Takaful* and actuarial science to develop sufficient capacity for the entire insurance industry.

6.3.17 Harmonizing *Shari'ah* Interpretations

The thesis recommends that Islamic scholars must never feel subdued by the challenges of differences in *Shari'ah* interpretations in Islam. This is all part of the test by Allaah SWT. It is recommended that efforts should be doubled towards arriving at generally accepted standards of harmonizing differences in order to benefit the *Ummah*. Initiatives that will ensure that *Takaful* business can expand by providing rules and regulations that are acceptable to the majority of the populace, is the desire of this study. The research strongly recommends the narrowing of these gaps that threaten to derail *Takaful* practice.

[1136] WAII is the West African Insurance Institute situate in Banjul, Gambia, set up to train insurance professionals for West African States. The funding of the institution is provided under Section 19 of National Insurance Commission Act 1997.

6.3.18 New Products and Excellent Services

The study recommends that for the nascent *Takaful* industry in Nigeria to succeed, the *Takaful* operators always need to be one step ahead in product innovation and provision of exquisite services. This will endear the customers to the services of the *Takaful* industry. They must learn to withstand aggressive competition from conventional insurers and the best way to do this is to better their products and exceed their quality of service.

6.3.19 Information Technology Revolution

The research recommends a revolution in the tech industry to enhance the success of *Takaful*. The Nigerian government has a very important role to play in this area because the requirements are too massive for the regulators alone to bear. Information technology has largely been responsible for the success of conventional insurance. *Takaful* needs to pursue this recommendation will seriousness if it is to thrive. Nigeria has no choice but to vastly improve its information technology profile if it wants to get the best out of *Takaful*.

6.3.20 Re*Takaful*

The thesis recommends that the issue of re*Takaful* be addressed with dispatch in order to build confidence in the populace. It is also recommended that adequate safeguards be put in place in anticipation of the rapid growth expected of *Takaful* in Nigeria. To this end, it is imperative for *Takaful* operators to collaborate and establish re*Takaful* pool or facility in Nigeria.

6.3.21 Fund Management and Investment Recommendation

The thesis seriously recommends that Nigerian *Takaful* operators must adhere strictly to the issue of fund management and investments if the fragile industry is to be firmly

entrenched in the Nigerian insurance landscape. As custodians of public funds, operators must ensure that these funds are soundly and safely managed. That is the essence of trust which insurance is all about. It is a primary objective for *Takaful* operators and regulators to ensure that fund solvency is maintained at all times. Solvency makes the results of insurance transaction certain and predictable. That is the function of insurance whether conventional or Islamic.

Furthermore, the thesis recommends that all relevant stakeholders in the *Takaful* industry like the Financial Services Regulatory Coordinating Committee (FSRCC), other government authorities in Nigeria and in Islamic countries, financiers, bankers, including central bankers, *Takaful* operators, economists and *Shari'ah* scholars, to study, develop and promote the diversity of non-interest investment instruments in products acceptable to *Shari'ah*.

6.3.22 Infrastructure

This thesis recommends the provision of adequate infrastructure to guarantee the successful implementation of *Takaful*. Immature Islamic banking system and poor communications infrastructure must be tackled headlong. It is also recommended that appropriate skills and resources be made available to tackle the teething problems of *Takaful* in Nigeria.

Finally…

Low-level insurance penetration and the financial exclusion of the majority of the Nigerian populace have been largely responsible for the shift in paradigm in the Nigerian insurance terrain. The shift towards micro insurance[1137] segment of the

[1137] Micro-insurance is a novel term that appeared in the literature for the first time in the 1990s and it is derived from the micro-finance, with which it shares a similar target public. On account of its relatively recent advent, there is, as yet, no consensus on a single definition of the term. However, Wikipedia defines it as the protection of low-income people against specific perils in exchange for regular premium payment proportionate to the likelihood and cost of risk involved. The target population typically consists of persons ignored by mainstream commercial and social insurance schemes, persons who have not had access to appropriate schemes.

insurance industry, which also encompasses *Takaful* is hardly any coincidence because of its world-wide acceptance as an ethics-based underwriting practice that mirrors a human face. To those who may not be Muslims, the equity factor in which premium is returned at the end of the transaction, is not only attractive but a fair business deal.

However, is *Takaful* the panacea to the deluge of challenges and pervasive insurance gap facing the Nigerian insurance industry? Will *Takaful* make a difference in creating an inclusive insurance sector? The researcher believes the answers to these questions and many more can be found throughout the length and breadth of this study. The challenges in the application of *Takaful* within conventional insurance regulatory framework have been the main thrust of this study. Overcoming these challenges through a dynamic legislative enactment, amongst other solutions, is crucial to the success of *Takaful* insurance and the much taunted insurance penetration and financial inclusion of the generality of Nigerians. A legislative enactment would provide a host of positive implications for the insurance industry from increased public participation to greater governance mechanism.

This thesis began as an inquisitive, yet honest endeavour to investigate the challenges in the existing enabling insurance laws; and to determine if a legislative enactment would resolve existing key issues of ambiguity within the insurance framework of laws and policies and if some degree of harmony could be achieved through same.

To achieve this, the thesis considered and made reference to a number of jurisdictions in order to draw examples, lessons and parallels demonstrating the effect that such a legislative enactment could have for the Nigerian insurance industry.

The International Labour Organisation (ILO) defines micro-finance as a mechanism to protect poor people against risk (accident, illness, death in the family, natural disasters etc) in exchange for insurance premium payments tailored to their needs, income and level of risk. It is aimed primarily at developing world's low-income workers, especially those in the informal economy who tend to be underserved by the mainstream commercial and social schemes. *Takaful* stands for all the above objectives outlined in the various definitions of micro-finance as long as there is compliance with *Shari'ah* principles.

The investigation carried out for this thesis had demonstrated that the existing enabling insurance legislations in Nigeria suffer primarily from the absence of regulatory clarity and harmony, general uncertainty and lack of effective enforcement mechanism; all of which result in weak insurance governance and overall continued aversion to insurance practice by Nigerians.[1138]

This thesis submits that the Nigerian insurance industry could benefit immensely from a legislative enactment on *Takaful*; although it is emphasized that an enactment of this nature is not a panacea for all existing problems of the Nigerian insurance industry. A legislative enactment is a major factor and one factor amongst other key factors that must be present for an enhanced insurance penetration and financial inclusion. Whether or not it is the main factor is outside the purview of this thesis, although in the researcher's mind, it certainly is. It is on this premise (the imperative for a legislative enactment on *Takaful*) that the thesis is established.

[1138] A respondent, Mr Yekeen Abdul-Malik, a lecturer in University of Abuja, Nigeria, stated that he would not patronize *Takaful* for now because of how it is operated in Nigeria. He based his opinion on Islamic banking experience where deposits were taken by such banks and invested in conventional businesses. In his words, ''in my opinion I will not participate in *Takaful* for now and the reason is very simple, most of the people running *Takaful* may not necessarily know what it involves. That is exactly what happened when we had what we called Islamic banking windows before the approval of Islamic banking in Nigeria. Many banks in Nigeria like the then Bank of the North, Habib Bank Nigeria had what we call Islamic windows where they took deposit on non-interest basis and used it to do conventional business which is against Islam and that is why most Muslims who eventually discovered that withdrew from it and that was why it didn't work. So for now I don't think Nigeria has had enough legal foundation for *Takaful*. See Appendix 1.3.

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