

Difference between takaful and conventional insurance economics essay



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Takaful is an Arabic word which explains as “ guaranteeing each other” (Tan Kin Lian, 2006). Haemala Thanasegaran (2008) also defined Takaful as mutual insurance in the Islamic system with compliant with principles of Shariah which is known as Islamic law. Shariah is attributing to direct Muslims by following principle which is: (W. Jean Kwon, 2007)

Fard or wajib also known as halal which is obligation strictly enforced by Islamic law.

Haram or mamu related to absolutely prohibition or unlawful activities.

Mandub or mustahub which means that what is suggested or the activities that individuals are ought to do as own advantages.

Makruh refer to what is discouraged or the activities that individuals are need to deny due to own benefits.

Muhab is about permissibility or the activities that under the Islamic law is neutral.

Besides, Alsadek Gait & Andrew Worthington (2008) agreed that Takaful is a type of collaborate self-help program. Moreover, Ramin Cooper Maysami & W. Jean Kwon (1999) who are stated that Takaful is establish on “ the law of large number” whereby in the form of joint guarantee insurance mechanism. It means that a flock of public gathers their capital resource to prevent certain risk of losses.

Takaful is an arrangement among a group of people with collective interests which aim to insure or defend each other from certain regulation of

misfortunes instance of premature death, disability and property damages (Obaidullah, 2005). Therefore, Faizal Manjoo (2007) said that Takaful is elicitation by the ' aqilah and diyah systems which is someone who is among a group of people are aim to financial salvage is possibility confronted with unexpected liability instance of paying for the blood money which means diyah.

Takaful is an alternative form of financial instrument to guarantee assets, liabilities and other interests of individuals and organizations. (Zuriah Abdul Rahman, 2009) Therefore, Muhammad Ayub (2009) supported that the alternative of Takaful is according to the concept of social solidarity, cooperation and at the same time indemnification the losses of participants. Indeed, Haemala Thanasegaran (2008) pointed out that Takaful is similar with conventional insurance which is include the distribution of the risk and it is become play an important role as part of our professional and livelihood.

As a result, Jamie Reid (2008) suggested that Takaful become a significant role to worldwide financial institution which is widely establish in Asian and Middle East currently and also has an opportunity advance to the western country. Present years, there are a lot of international insurance industries are interest participate in Islamic insurance market.

Although, Takaful insurance is mainly expanded at Islamic countries for the sake of the advent of Islamic banking and it has presented its potential as an innovation financial instrument over the past decade. (Haemala Thanasegaran, 2008) Whereas, Ramin Cooper Maysami & W. Jean Kwon (1999) examined that Takaful has also grown on religion principle which

processes unique characteristic besides grown as an innovation financial instrument.

2. 1. 1 Concept of Takaful

The concept of Islamic insurance which is known as Takaful was first introduced in Sudan in 1979 and the main concept is an alternative to conventional insurance whereas according to principle of Shariah. (Kassar, 2008)

Takaful as a concept compliant the principles of Shariah which is Islamic law thereby it is essentially to a system of mutual help which refers to the pooling of resources to help the needy (Browne and Kim, 1993).

Therefore, according to Tan Kin Lian (2006), who is examined that before the advent of Islam 14 centuries ago there is possibility that the concept of mutual cooperation among tribal members in the Arabian Peninsula already started. The instance in pre-Islamic history which to prove the argument is:

A'qila which is the Pooling System

“ Daman Khatr Al-Tariq” defined as Surety System

Al Hlif which is utilized by Trade Alliance Confederation

Nevertheless, Catherine Stagg-Macey (2007) summarize that Islamic insurance also known as Takaful is a mutual insurance that establish with the concept of tabarru' (donation) which means that everyone will be take advantage from a share of investment returns since they are contributes to a

fund. It is the combination of guaranteeing each other and mutual or cooperative insurance and there are necessarily to including in Takaful.

However, Dawood Yousef Taylor (2005) stated that according to Fiqh Academy in 1985 who judged that conventional commercial insurance was haram (forbidden) which contravened the rules of Shariah and Islamic insurance which is Takaful was halal (acceptable).

Accordingly, Haemala Thanasegaran (2008) pointed out that the reason is the operation of conventional insurance is against the principle of Shariah which is involve the elements of Al-gharar (uncertainties in the operation of the insurance contract), Al-maisir (gambling as a consequence of the presence of uncertainty), and Al-riba (interest).

Gharar (uncertainty)

Gharar is means that uncertainty or ambiguity of the theme of the contract by the insured such as the occurrence of indemnity, the sources and the amount for compensation and the timing of uncertainty (Anwar, 1994).

Maisir (gambling)

Islamic law is prohibiting speculation or receiving return without effort. Since the policy holders of insurance are look like to bet premiums on the condition that the insurer will make compensation when arise specified accident thereby it is forbidden based on principle Shariah. (Anwar, 1994)

Riba (usury or interest)

Riba is prohibit by Islamic law which refer to unequal exchange of the same things and also can defined as difference amount and quantity between insurer and insured when transactions. (Anwar, 2004)

2. 1. 2 Type of Takaful

In Malaysia, there is providing two different types of Takaful insurance services which consist of General Takaful and Family Takaful.

Family Takaful

The family Takaful is a long-term investment and saving. The function of family Takaful is providing protection to the participant's family by mutual fund while participant involve in the event of death. Furthermore, the goal of designed this plan is to:

Regularity save the contribution of fund during a fixed period which is long term

Utilize fund that contribution by participant as investment to gaining profit or return under the rule or principle Shariah, and

Assistance in financial while unexpected death of participant prior to the maturity of the plan

Commonly, family Takaful can recognize to several form such as:

Ordinary family which is composing from endowment, temporary, medical and health. Takaful endowment is same kind with the life insurance.

However, there is also has combine with education plan which respond by public is enthusiastically.

Investment-linked Takaful is providing participant protection and also get chance earn profit or return in future depend on value underlying assets.

Takaful Annuity is attribute to guarantee participant future retirement life by provide periodic income.

(Hendon Redzuan, Zuriah, Sharifah Sakinah, 2009)

On the other hand, Haemala Thanasegaran (2008) stated that maturity period, amount and the frequency of annual contribution of family Takaful are determinant by participant as well as the fund contribution will save into the Participants' Account (PA) which is for savings and investment and the Participants' Special Account (PSA) which is for Tabarru or donation.

General Takaful

A general takaful plan is commonly standing in the period of 12 months which is known as short term mutual financial help. Generally, it is assuring for property, engineering, miscellaneous accident, marine, motor and others. Moreover, general takaful attribute to scheme that purpose to provide compensation to someone who is suffering losses such as destruction or disaster inflicted upon asset of the participant. Method of payment for general takaful is based on tabarru' which is donation aim to mutually help and jointly guarantee each others with using the fund compensate for participants who are facing losses. (Hendon Redzuan, Zuriah, Sharifah Sakinah, 2009)

Although, Mohd. Ma'sum Billah (1996) suggest that general Takaful should identify as al-Musahamah (contribution) which replace al-Tabarru' (donation) due to aim the participant has no against the rule of Shariah which in the risk on the theme of the policy while make a claim. In other words, participants are making a claim or gain return over their own contribute fund. As evidence, under Quran sanction of mutual co-operation has described that " Help you another in righteousness and piety".

2. 2 Development of Takaful Malaysia

Islamic insurance which is also known as Takaful is a new industry compare with conventional insurance. Despite the origin of Takaful was beginning from 14 centuries ago, the first time that Malaysia started operating Takaful was in 1984 which is Syarikat Takaful Malaysia Bhd. (Dawood Yousef Taylor, 2005)

Whether or not, Sudan was the first introduced the modern Islamic insurance initially based on cooperative model which similar with conventional mutual insurer in 1979. However, majority of the countries include Malaysia and Saudi Arabia implemented commercial models of Takaful afterward. (IFSB & IAIS, 2006)

Ma'sum Billah (1996) concluded that Takaful in Malaysia is currently thrives.

Nevertheless, Malaysia is the leader which has the largest market in Takaful insurance among non-Arab countries. For instance, Takaful occupy 27% of the total insurance market in Malaysia parallel to Asia Pacific countries which have approximately 9% market, Europe and US are about 1% market and

Arab countries which is the head of Takaful insurance hold about 63% market. (Salihuddin Ahmad, 2007)

In the Far East, Malaysia was the forefront of Takaful development who conducted by Central Bank of Malaysia (BNM) enact Takaful regulations with separate regulations that enable the prosperity of Takaful insurance. Alter of the regulation is compulsory as to compete with conventional insurance industry. Thus, Malaysia administer Takaful compete with the conventional insurance impartiality. There is possibility that the changes of the Takaful Act and regulations in Malaysia bring on prosperous of Takaful Malaysia and Takaful Nasional which are two major composite Takaful operators. It is lead to development of general and life insurance rather than general Takaful insurance. (Dawood Yousef Taylor, 2005)

In addition, in term of Takaful in Malaysia successfully, there are new operators were intent to involve in Takaful industry on several countries such as:

Brunei - Takaful IBB Bhd and Takaful Taib Sdn Bhd

Indonesia

- PT Syarikat Takaful Keluarga which transacting in family (life) business
- PT Syarikat Takaful Umum which transacting in general business

Singapore - Islamic Insurance Pte

(Mohd. Ma'sum Billah, 1996)

Moreover, Takaful operators of Malaysia have established joint-ventures in Pakistan, Saudi Arabia and Sri Lanka which aim to provide technical expertise to the Asian countries especially Indonesia, Brunei, Australia, Lebanon, Bangladesh, Algeria and so on. (Yusof, 2001)

Nonetheless, Central Bank of Malaysia (BNM) and the Takaful operators continued struggling to expand Takaful industry as assumed in the Financial Sector Masterplan during 2002 which were focused on financial infrastructure development, institutional capacity enhancement as well as product and market development. (Central bank of Malaysia, 2002)

On the other hand, Takaful has gradually developed as a viable alternative to conventional insurance and may appeal to Muslim and non-Muslim which is a wide range of customers. (IFSB & IAIS, 2006) Therefore, Malaysia as a multi-racial country which has differences in religious and cultural was able to attract many consumers to purchase Takaful insurance. In Malaysia, Prudential BSN Takaful Berhad (PruBSN) has attracted more than 40% of non-Muslim customers among participants. (Mohamad Salihuddin Ahmad, 2007)

Nevertheless, the corporate sector and multinationals in Malaysia are also preferred to select Takaful compared with conventional insurance. Although, there is not enough to promote and expand Takaful thereby it was a challenge to the development and expansion of the local and global Takaful industry. (Mohamad Salihuddin Ahmad, 2007)

Takaful is now implemented by over 60 companies in 23 countries and is trending to promptly expand. Recently, Malaysia initially offered Re-Takaful services in <https://assignbuster.com/difference-between-takaful-and-conventional-insurance-economics-essay/>

Labuan and also significant develops Re-Takaful which is the equivalent of conventional reinsurance. Presently, majority of Takaful operators reinsure to conventional reinsurers despite it is considered acceptable as long as there is no feasible that Shariah obey alternative. (IFSB & IAIS, 2006)

Since February 2008, Malaysia already has eight Takaful operators with license which is Syarikat Takaful Malaysia Berhad, CIMB Aviva Takaful Bhd., Hong Leong Tokio Marine Takaful Bhd., MAA Takaful Berhad, Takaful Ikhlas Sdn. Bhd., Prudential BSN Takaful Bhd., HSBC Amanah Takaful (Malaysia) Sdn. Bhd. and Etiqa Takaful Bhd., as well as two Re-Takaful companies which is Munich Re and MNRB Holding Bhd. (Bank Negara Malaysia, 2006)

2. 3 Difference between Takaful and conventional insurance

Takaful

Conventional insurance

It is a co-operative institution according to the principles of contract which is mutual co-operation (ta'awun).

(Ahmad Ali Khan, 2003)

It is a business institutions operated upon the principles of contract which is exchange.

(Ahmad Ali Khan, 2003)

Based on the principle, participants as insured and insurers their own self.

Moreover, not insurance operators bearing the losses and risk of transfer whereas are shared by the participants each other.

(Ahmad Ali Khan, 2003)

The insured is uncertainly due to the transfer of the indeterminate fortuitous economic losses related with the prescribed risks in return for a pre-determined payment which is known as premium.

(Ahmad Ali Khan, 2003)

There are not endue with involve in the profits generated by the insurance operators.

(Ahmad Ali Khan, 2003)

Main objective is to gain profit or return from the insurance transactions for the shareholders.

(Ahmad Ali Khan, 2003)

All participants who pay a certain prescribed premiums are available to vote in the elections of the directors of the company or to check the company's annual accounts.

(Ahmad Ali Khan, 2003)

The policy-holder has no right to vote in the elections of the directors of the company or to check the annual accounts of the company.

(Ahmad Ali Khan, 2003)

Exchanging money with money in itself thereby no discrepancy in the amount or time.

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(Ahmad Ali Khan, 2003)

Contribution of participants is attributed to Tabarru which means donation.

(Mohd Tarmidzi, 2007)

Both premium and claim being exchanged are different and takes place at different times.

(Ahmad Ali Khan, 2003)

Contribution from participants is due to investment.

(Mohd Tarmidzi, 2007)

Surplus in the fund will be distributed to participants.

(Mohammed Musabah, 2008)

Surplus in the fund is belong company as profit.

(Mohammed Musabah, 2008)

2. 4 Perception

As to improve customers' perception, companies should frequently adopt customers oriented and considering customers need in their position.

Moreover, fully understand, elaborately configure, effectively manage, and exceed customers' expectations already as a significant key to improve customers' perception. (Frank Yao, 2007)

On the other hand, according to Mohd Tarmidzi (2007), who is suggested that Takaful operators need respect the perception of the customers whether their criticism is truth or not.

2. 4. 1 Services

Recently, providing better service quality already as a vital objective for companies to satisfy customers demand and compete with other same trade companies. (Izah & Nor Mazlina, 2007) Thus, there is importance of service quality perceptions and the relationship between customer satisfaction and service quality. (Haque, 2009)

Indeed, services are definitely related to the total quality management (TQM). Presently, a lot of global company services are adopted TQM as management paradigm since they realized that TQM also may effective in services as such in manufacturing. It is obviously that companies are emphasize to quality of services (Feng Jie, 2009)

Regarding to Frank Yao (2007), who is defined that customer perception is very important to measure qualified services such as in operation execution layer, business development layer and others. It is due to adopt customers' expectations and requirements will more efficiency to satisfy customers need. Thus, customer perception become a central topic and also as a key consideration.

However, Dagmar Recklies (2006) studied that companies only able to develop appropriate strategies as they understand features of the services that consumers need and expectation. Therefore, customers' perception considered as most important to the companies which is not merely
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strengthening relationship between customers but also achieves services improvement.

2. 4. 2 Reliability

According to Arasli (2005), he stated that customers' satisfaction may highest influence by the reliability of the products or services which priority had a statistically significant impact from customers' perception.

Furthermore, Haque (2009) concluded that reliability was primary related to the result of service. Despite, customers satisfaction not merely estimate on customers' experiences on service delivery process whereas also the exactitude and reliability of the delivered service.

Besides that, Asmak (2008) also suggested that majority of the customers while intend to purchase insurance, they will considered insurance companies in terms of assets and reliability. In the other words, customers' perception and decision adoption will influence by reliability of the specified company.

Syarikat Takaful Malaysia Bhd (STMB) stated that the reliability of the management information systems is very important which relying to Information System Security Policy (ISSP) Manual due to prevent unauthorized access, disclosure, duplication, negligence error, modification, diversion, destruction, loss, abuse or steal of STMB information systems. (Takaful Malaysia annual report, 2009)

2. 4. 3 Demographic

According to Wilkie (1990) indicated that demographic will affect what kind of products or services customer will purchase, how much that customer willing to pay as people achieve higher education. As a result, customer with higher education may enhance their ability to process more complicated information and decisions making.

Nevertheless, Asmak (2008) who is pointed out that the demographic characteristics of a customer which is knowledge regarding the policy, income status household and customer antipathy to risk may influence customer's decision or even indeed changing their policies.

Regarding to Schiffman and Kanuk (2000), conclude that customers with better education alike to income higher which may affect their expected life-style. Therefore, customers will more willing to consume because power purchasing of them are higher due to their level imposable income better than general labor.

Lastly, marketer may redesign, reposition and re-price the services in term of changing demographic attribute to fulfill customer requirement and satisfaction. (Kotler, 2000) In other hand, Lamb (2000) stated that income level which may give impact to customer consumption is significant in demographic variable due to segmenting market.