

Charging Fee for Guarantee (*al-Kafalah bi al-ajr*) and its Application by Deposit Insurance Corporation Malaysia (PIDM) for Takaful Benefits Protection Scheme

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Takaful and Insurance benefits protection scheme is a new innovative product introduced by PIDM to provide takaful certificate and insurance policy owners with an explicit protection against the loss of part or all of their benefits in the event of an insurer member failure. The main objective of takaful and insurance benefits protection is to promote public confidence in Malaysia's financial system by protecting takaful certificate and insurance policy owners against the loss of their benefits. This initial study will investigate the validity of an applied Shariah instrument of al-kafalah bi al-ajr i.e. charging fee for a guarantee and explore other possible viable alternative instrument in compliance to Shariah principles. Any criticisms and suggestions in this paper are part of academic exercises for the positive and constructive improvement of Islamic finance industry, with the hope that the paper will indulge the respected participants to express their scholarly opinions and deliberations.

1.0 Introduction

The Takaful and Insurance Benefits Protection System (TIPS) is the latest financial consumer protection scheme to be administered by Perbadanan Insurans Deposit Malaysia (PIDM). As part of an enhanced financial consumer protection package following the enactment of Akta Perbadanan Insurans Deposit Malaysia (PIDM Act), TIPS was implemented on 31 December 2010 to provide takaful certificate and insurance policy owners with an explicit protection against the loss of part or all of their benefits in the event of an insurer member failure. TIPS will also benefit the takaful and insurance industry by levelling the playing field with the banking industry, which is already covered by the deposit insurance system.

The takaful and insurance industry is an integral part of the financial system and the introduction of TIPS is consistent with international developments. A number of jurisdictions in Europe and Asia have established insurance compensation schemes in one form or another to protect policy owners, including the United Kingdom, France, Germany, Spain, Korea and Japan. The United States of America and Canada also have similar schemes.

TIPS was designed specifically to meet Malaysian needs. Among the unique features of the system is the coverage of both takaful and insurance benefits under the administration of one organisation. In line with its expanded mandate, PIDM will administer both TIPS and the deposit insurance system in an effective and efficient manner to promote public

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confidence in the financial system. TIPS will also be administered in a manner to promote sound risk management among takaful operators and insurance companies.

2.0 Perbadanan Insurans Deposit Malaysia

PIDM is a Government agency established in 2005 under Akta Perbadanan Insurans Deposit Malaysia (PIDM Act) to administer the national deposit insurance system aimed at protecting depositors. Beginning 31 December 2010, PIDM's role has been expanded to also administer TIPS to provide protection to owners of takaful certificates and insurance policies. PIDM also provides incentives for sound risk management in the financial system and promotes and contributes to the stability of Malaysia's financial system. PIDM is also known internationally as the Malaysia Deposit Insurance Corporation (MDIC).

2.1 Mandate of PIDM

PIDM's mandate is set out in the PIDM Act, and its objects are to:

- (a) administer a deposit insurance system and a takaful and insurance benefits protection system under the PIDM Act;
- (b) provide insurance against the loss of part or all deposits for which a member bank is liable and provide protection against the loss of part or all of takaful or insurance benefits for which an insurer member is liable, in the event of a failure of a member institution;
- (c) provide incentives for sound risk management in the financial system; and
- (d) promote or contribute to the stability of the financial system. In achieving its objects under paragraphs (b) and (d), PIDM shall act in such manner as to minimise costs to the financial system.

3.0 Membership of Takaful and Insurance Benefits Protection Scheme

3.1 Member Institutions

All takaful operators licensed under the Takaful Act to conduct family solidarity and/or general takaful business in Malaysia, as well as insurance companies licensed under the Insurance Act to conduct life and/or general insurance business in Malaysia are member institutions of PIDM. Membership in PIDM is compulsory as provided under the PIDM Act.

3.2 Non –Member Institutions

Institutions that are not insurer members of PIDM include:

- Reinsurance companies and retakaful operators
- International takaful operators licensed under the Takaful Act 1984
- Captive insurers and specialist insurers
- Danajamin Nasional Berhad
- Offshore insurance companies
- Other players in the insurance industry, such as insurance brokers, insurance adjusters and insurance agents or financial advisers.

4.0 Coverage for the Takaful and Insurance Benefits Protection Scheme

All types of insurers, whether groups or individuals policies either in life or general takaful or insurance benefits, are protected. The maximum limit of coverage is up to RM500, 000 per insurer policy holder per member institution. To be eligible for protection under TIPS, the takaful certificate or insurance policy must be issued in Malaysia by an insurer member and be denominated in Ringgit Malaysia. The Malaysian deposit insurance system provides separate coverage for conventional and Islamic deposits. For more elaborative and further understanding refers to the below provided table.

Table 1: Protected Benefits for Family Solidarity Takaful and Life Insurance

TABLE 1	
FAMILY SOLIDARITY TAKAFUL/LIFE INSURANCE	
Benefits Protected	Maximum Limit (Individual or Group Policies/Plans)
Death and related benefits	RM500,000
Permanent disability	RM500,000
Critical illness	RM500,000
Maturity value (excluding unit portion of investment-linked policies)	RM500,000
Surrender value	RM500,000
Accumulated cash dividends	RM100,000
Disability income	RM10,000 per month
Annuity income	RM10,000 per month
Medical expenses	100% of expenses incurred
Refundable prepaid premiums	100% of amount prepaid

Table 2: Protected Benefits for General Takaful and General Insurance

TABLE 2	
GENERAL TAKAFUL/INSURANCE	
Benefits Protected	Maximum Limit (Policies/Plans)
<p>Loss of or damage to property in relation to:</p> <ul style="list-style-type: none"> an immovable property located in Malaysia a motor vehicle registered in Malaysia or a foreign registered vehicle insured to drive in Malaysia a ship, aircraft or other movable property insured by a citizen or resident of Malaysia, permanent establishment or embassies in Malaysia 	RM500,000 per property
Death and related benefits	RM500,000
Permanent disability	RM500,000
Critical illness	RM500,000
Disability income	RM10,000 per month
Medical expenses	100% of expenses incurred
<p>In relation to indemnification against claims by a third party:</p> <ul style="list-style-type: none"> • loss of or damage to eligible third party immovable or movable property • death and related benefits • permanent disability • illness or bodily injury • disability income • medical expenses 	<ul style="list-style-type: none"> • RM500,000 per property • RM500,000 • RM500,000 • RM500,000 • RM10,000 per month • 100% of expenses incurred
Refundable prepaid premiums	100% of amount prepaid

5.0 Obligation of the PIDM

The PIDM is to cover takaful certificate holders the takaful benefit in case of failure of the takaful operators. This Takaful and Insurance Benefits Protection System (TIPS) recently has been introduced by the Government in order to protect the interests of takaful certificates and insurance policies in the above said case. The takaful operators and insurance companies which are member institutions of PIDM are also referred to as 'insurer members' in this system. All takaful operators licensed under the Takaful Act 1984 to conduct family and/or general takaful business in Malaysia, as well as insurance companies licensed under the Insurance Act 1996 to conduct life and /or general insurance business in Malaysia are member institutions of PIDM. Membership in PIDM is compulsory as provided under Akta Perbadanan Insurans Deposit Malaysia. Thus, to be eligible for protection under TIPS, the takaful certificate or insurance policy must be issued in Malaysia by an insurer member and be denominated in Ringgit Malaysia. This system was brought into effect on 31 December 2010 and is administered by Perbadanan Insurans Deposit Malaysia (PIDM).

6.0 PIDM makes payments to takaful certificate or insurance policy owners'

In the event of an insurer member failure which necessitates a payment for the protected benefits, PIDM will make payment to takaful certificate or insurance policy owners upon occurrence of the claims event, maturity or surrender of the takaful certificate or insurance policy provided the claims are made within a specified time frame, under the following circumstances:

- **Obligatory payments** – where a winding-up order has been made in respect of the insurer member.
- **Discretionary payments** – with the Minister of Finance's approval, where:
 - (i) The insurer member that issued the certificate or policy is unable to make payment for the protected benefits because of:
 - a court order;
 - an action taken by a regulatory body or PIDM; or
 - an action taken by a receiver and/or manager while the insurer member is in receivership;
 - (ii) A petition for winding up against the insurer member has been presented to the court; or
 - (iii) The insurer member has its PIDM membership cancelled or terminated.

7.0 The Benefits of TIPS;

7.1 Takaful Certificate and Insurance Policy Owners Benefits

- PIDM provides explicit protection for takaful certificate and insurance policy owners against the loss of eligible takaful or insurance benefits should an insurer member fail.
- Protection is provided automatically and no application is required.
- There is no charge to takaful certificate and insurance policy owners.
- Should an insurer member fail, PIDM will make payment on eligible takaful and insurance benefits following the occurrence of a claim event, on maturity or on surrender of the takaful certificate or insurance policy provided the claims are made within a

specified time frame. Alternatively, PIDM may take measures to secure continuity of coverage for certificate or policy owners by transferring the takaful certificates or insurance policies to another insurer member.

7.2 Financial System Benefits

- Promotes public confidence in Malaysia's financial system by protecting takaful certificate and insurance policy owners against the loss of their benefits.
- Reinforces and complements the existing regulatory and supervisory framework by providing incentives for sound risk management among takaful operators and insurance companies.
- Minimises costs to the financial system by finding least cost solutions to resolve non-viable insurer members.
- Contributes to the stability of the financial system by dealing with non-viable insurer members expeditiously.

8.0 List of Takaful Operators registered under Takaful and Insurers Protection Scheme (TIPS).

- 1-AIA AFG Takaful Berhad
- 2-CIMB Aviva Takaful Berhad
- 3-Etiqa Takaful Berhad
- 4-Great Eastern Takaful Sdn. Bhd.
- 5-Hong Leong MSIG Takaful Berhad
- 6-HSBC Amanah Takaful (Malaysia) Sdn. Bhd.
- 7-MAA Takaful Berhad
- 8-Prudential BSN Takaful Berhad
- 9-Syarikat Takaful Malaysia Berhad
- 10-Takaful Ikhlas Sdn. Bhd.
- 11-ING PUBLIC Takaful Ehsan Berhad²

9.0 Shariah Compliance Structure of PIDM

The Council of Shariah Advisory Board of Bank Negara Malaysia (Central Bank) in its 26th meeting held on 26th June 2002 / 15th Rabiul Akhir 1423 resolved that the deposit insurance scheme in Islamic banking is permissible based on the concept of mutual guarantee among the Islamic financial institutions as participants in the scheme. The implementation of the deposit insurance scheme does not contradict with the Shariah principles since its objective is to protect public interest, especially the depositors and the banking industry as a whole. Nevertheless, there is a need to separate the funds in the operation of the deposit insurance scheme for Islamic banking to ensure that the funds of Islamic deposit insurance scheme are invested in Shariah compliant instruments.³

² <http://www.pidm.gov.my/Takaful---Insurance-Protection/Member-institutions-of-PIDM-%E2%80%93-Insurer-Members-%28Tak.aspx>

³ Resolutions of Shariah Advisory Council of Bank Negara Malaysia, BNM/RH/GL/012-2, p22

9.1 Latest Resolution of Shariah Advisory Council BNM

The Shariah Advisory Council of BNM in its 54th meeting held on 27th October 2005 / 23rd Ramadan 1426 and in its 55th meeting held on 29th December 2005 / 27th Zulkaedah 1426, resolved that the above Islamic guarantee (by charging guarantee fee) mechanism provided by the credit guarantee company to the Islamic financial institutions offering Islamic financing products to customers is permissible.

Nevertheless, the SAC of BNM in the 80th meeting, dated 7th January 2009 resolved that PIDM operation in managing insurance for Islamic deposits can be operated based on the principle of *kafalah bi al-ajr*. The premiums paid by the member institutions to PIDM are regarded as *ujrah* or fee for service and as such shall belong to PIDM. Since it is a compensation for the service (protection), PIDM can structure the charges either at a lump sum payment or by instalments.⁴

10.0 Revisiting Shariah Issue of Charging Fees for Guarantee

The major Shariah issue is the question of whether charging a fee (*kafalah/* guarantee) is allowable. Among the legal consequences is that all the premiums paid by the member institutions will be treated as considerations for the protection and guarantee of the deposits. In other words, the fees paid by the members are actually compensations against the guarantee. As such, all the accumulated payments belong to PIDM. The Shariah basis for this is *kafalah bi al-ajr*.

11. Juristic Opinions on the Rule Regarding Charging Fees for Guarantee

First View: Those who allow charging Fee for Guarantee

The great majority of Islamic jurists have always considered it unlawful to charge a fee for a guarantee. They are the jurists from Hanafites, Shafiites, Malikites and also Hanbalites who claimed that it is unlawful to charge fee against a guarantee⁵. They hold that it is permissible to give guarantee; however, to take any rewards from it is prohibited. There are evidences and justifications that show why such charges are not permissible as follows:

⁴ Bank Negara Malaysia, Resolusi Shariah Dalam Kewangan Islam, 2010. pg. 175.

⁵ Al-Buhuti, Mansur ibn Yunus ibn Idris, *Kashshaf al-qina' an matan al-iqna'*, Dar al-Fikr : Beirut, 1982, v3, p206, Ibn Qudamah, Muhammad Muwafiq al-Din ibn Abdullah , *Al-mughni*, Dar al-Fikr: Beirut, v6, p441, *al-Mudawwanah* li al-Imam Malik, v5, p283.

The First Item of Evidence

Al-Kafalah is a *tabarru'* contract, however if it is associated with a fee imposed by the guarantor, it becomes a contract of commercial exchange (*mu'awadhah*) which is not allowable.⁶

The meaning of *tabarru'* is to exchange something not for the purpose of exchange in return for something. For instances a gift, present, and any free offering for which no exchange is taken. Therefore, in the case of guarantee, the party which is guaranteed donates his money to the guarantor, and thus cannot get back what he has given. This case is evidenced in the practices of the prophets' companions Ali bin Abi Talib and Abu Qutadah who guaranteed and paid the debts of a deceased man, their guarantee at that time was for charity and was not for any return⁷.

The Second Item of Evidence

The reward or financial compensation is only applicable when it is exchanged against performance of a service or against the exchange of valuable goods. But, as far as guarantee is concerned it is neither performance of an act of service nor an exchange of goods. Therefore any charge for a guarantee is similar to eating up people's property unjustly or an act of bribery.⁸ Al-Hamawi argues: "Perhaps the reason for the prohibition of charging a fee is the fact that issuing a guarantee is not an act of service which deserves rewards."⁹ Al-Mawardi argues that the reward is permissible for the exchange of services, but giving guarantee is not a service, hence it does not deserve any rewards¹⁰. Al-Dardir also added that the reason for prohibiting taking reward for a guarantee is that when the debtor pays the debt to the creditor, the reward (for the guarantor) is not justified, it is taking people's money unjustly (*bi al-batil*).¹¹

The Third Item of Evidence

The condition of charging a fee for a guarantee will amount to uncertainty (*gharar*) which is unlawful¹².

⁶ Nazih Hammad,, "*Mada jawaz akhzi al ujr 'ala al-Kafalat fi al Fiqhi al-Islami*.,published in Journal of King Abdul Aziz University, Islamic Economy, 1997, p97.

⁷ Sahih al-Bukhari, v5, p56, Sunan al-Bayhaqi,v6, p72.

⁸ al-Dusuki, Samsuddin ibn Muhammad, *Hashiyah al-dasuki `ala sharh kabir*, Isa al-Babi al-Halbi wa al-Syarikah : Beirut, v3, p341.

⁹ Ahmad al-Himawi, Ghamz 'Uyun al-Basa'ir, Beirut. Dar al-Kutub al-Ilmiyyah, 1985, v3, p154.

¹⁰ al-Mawardi ,al Hawi al Kabir, v8,p 121.

¹¹ al Dardir, Al-Sharh al-Soghir, v3,p 442.

¹² Nazih Hammad,, "*Mada jawaz akhzi al ujr 'ala al-Kafalat fi al Fiqhi al-Islami*, p114.

The Fourth Item of Evidence

The guarantor who guarantees the debt of another person for a fee will engage in *riba* by asking the guaranteed person to pay back more than what he owed which is the debt in full plus the fee for the guarantee.¹³ This is clearly understood through the saying of the Prophet (PBUH) “Any debt that generates benefit is considered *riba*”. According to Ibn Abidin, a guarantor gives loan against the financial obligation, when a consideration is required along with the full amount of debt, it is as if the creditor demands more than the amount of debt which amounts to injustice and *riba*.¹⁴ This is because the additional amount paid is considered as *riba* which is prohibited in Islam.

Ibn Qudamah argues: “The guarantor is obligated to honour the payment of debt, when he pays it, it becomes the obligation of the guaranteed person, as such it becomes a debt. Hence, if the guarantor takes fee, it becomes a loan which generates profit to the creditor.”¹⁵

In the same vein, Al-Dusuqi of the Malikites argues: “The guarantor when he pays the debt to the lender, he will ask the debtor (under his guarantee) the same amount with addition to the fee. This is not allowable as it is a loan with extra payment.”¹⁶

The Fifth Item of Evidence

Islam encourages good deeds such as guarantee of others and giving loans to those in financial difficulties. Such deeds are only done for the pleasure of Allah and will be rewarded by Allah. These good deeds are considered one of the ways that strengthen the relationship between the people. On the other hand, charging fee for good deeds such as guarantee is considered as exploitation of people who are in need and thus prohibited¹⁷. It is narrated from Al-Abhari in the book of “*al-Taj wa al-Iqlil*” that imposing charges for guarantee is not allowable because giving guarantee is an act of a good deed. It is submitted that it is prohibited to take a fee from acts of good deeds like praying and fasting which are performed not for the worldly rewards¹⁸.

¹³ Al-Buhuti, *Kashshaf al-qina' an matan al-iqna'*, v3,p306.

¹⁴ Minhatul al-Khaliq a'la al Bahri ar Raiq li ibn A'bidin,v6, p242.

¹⁵ Ibn Qudamah, *al-Mughni*, vol.6, pg.441.

¹⁶ Al-Dusuqi, *Hashiyat al-Dusuqi 'ala al-Sharh al-Kabir*, vol.3, pg.341.

¹⁷ Hasyiat al Sowi 'ala sharh al Soghiri li al-Dardir,v3, p442.

¹⁸ Muhammad ibn Yusuf al-Abhari, *Al -Taj wa al-Iqlil li mukhtasar al-Khalil*,v5,p111.

Second View: Those who Allow Charging Fee for Guarantee

Among the contemporary scholars who allow charging fee for guarantee are Sheikh Yusuf al-Qaradawi, Sheikh Nazih Hamad, Sheikh Abdullah Mani' and Malaysian scholars at SAC Bank Negara Malaysia. The following are among their evidences (with special reference to Sheikh Nazih Hamad's Paper on the subject:

The First Item of Evidence

Possibility of Converting a *Tabarru'* Contract to *Mu'awadhat*

According to Sheikh Nazih Hamad, it is permissible to convert a *tabarru'* (donation based contract) to a *mu'awadhah* based contract (commercial exchange contract) with the consents of the contracting parties. According to him a guarantor deserves a good reward from the guaranteed person similar to his contribution for the guaranteed person or even more. This is for his commitment as long as the debt is settled immediately. Sheikh Hammad also makes analogy with *hibah* (a gift) when it is associated with the expectation of a reward i.e *hibah al-thawab* or *bi shart al-thawab*. Similarly a lending contract associated with a consideration will convert it to *ijarah*. The same is true with *wakalah* which can be converted to *wakalah bi al-ajr*.¹⁹

However, the above mentioned can be refuted that those contracts when associated with considerations (such as *kafalah* with a fee) are considered to be another different contract in which have different legal nature and consequence. Therefore "*hibah al-thawab* is not a real *hibah*, the confusion lies in its terminology by calling it "*hibah*" (because it is actually a *muawadhah* contract), and it is not regarded as an act of *tabarru'* (donation). As per *ijarah* converted from '*ariyyah* (lending), it is argued that if the lending is associated with a consideration it is regarded as a hire from the very beginning. The same is true with agency contract and agency with fee where they should not be treated as a conversion of the former to the latter.²⁰

The above reasoning can also be refuted by the fact that all those example of conversions of the contracts from *tabarru'* to *mu'awadah* are actually the established and known contracts which are recognized by Shariah. But what is the result of converting a guarantee to a debt from *tabarru'* to *mu'awadah*? It becomes lending or giving a loan with a fee. Charging a fee for a loan is nothing but *riba*.²¹

¹⁹ Nazih Hamad, *Mada jawaz akhz al-ajr ala al-kafalah fi al-fiqh al-Islami*, p99.

²⁰ Sheikh Mukhtar Sallami, Comments on Sheikh Nazih Hamad paper "*Mada jawaz akhz al-ajr ala al-kafalah fi al-fiqh al-Islami*" Journal of King Abdul al-Aziz, al-Iqtisad al-Islami, no. 9, 1997, p.126.

²¹ Al-Sadiq Al-Darir, Comments on Sheikh Nazih Hamad's paper on "*Mada jawaz akhz al-ajr ala al-kafalah fi al-fiqh al-Islami*" Journal of King Abdul al-Aziz, al-Iqtisad al-Islami, no. 9, 1997, p97.

The Second Item of Evidence

It is allowable to charge a fee for a guarantee by comparing it with taking rewards for making other commitments which are permissible by Shariah.

Among the classic examples, according to the Malikites, it is allowable for a wife to take a promise from her husband not to practice polygamy where it is pursued against a consideration. Similarly the husband can buy a promise from his wife not to get married if he passes away. However when he wants to get married again with the second wife, he can compensate his commitment i.e. promise which is the right of the first wife with a financial consideration.²²

However, this can be argued by the fact that, in the case of the promise not get married without the consent of the first wife, it is about a compensation for dropping the right or “*isqat al-haq*” where a husband pays money to break his promise and it is not for making a commitment. The wife can also get married again if her husband passes away.²³

The Third Item of Evidence

It is allowable to charge fee for a guarantee by comparing it to the permissibility of taking rewards for some of the good deeds such as teaching Al-Quran, the remuneration of Imam and Muazzein. This is also supported with some events such as the companion who took a reward for “*ruqyah*” healing by using Al-Quran, which was approved by the Prophet PBUH.²⁴

²² Nazih Hamad., opcit.

²³ Sheikh Mukhtar Sallami, ibid.

²⁴ Hadith Narrated by Bukhari no 1670. Abu Sa’eed al-Khudri (may Allah be pleased with him) said: A group of the Companions of the Prophet (peace and blessings of Allaah be upon him) set out on a journey and travelled until they made came near one of the Arab tribes. (These people were either kaafirs or very stingy, as Ibn al-Qayyim mentioned in al-Madaarij). They asked them for hospitality but they refused to do so. Then the leader of that tribe was stung, and they tried everything but nothing helped him. Then some of them said, Why don’t you go to those people who are staying (nearby)? Maybe some of them have something. So they went to them and said, O people, our leader has been stung and we have tried everything and nothing helped him. Do any of you have something? One of them said, Yes, by Allaah. I will perform ruqyah for him, but by Allaah we asked you for hospitality and you did not give us anything, so we will not perform ruqyah for you unless you give us something in return. So they agreed on a flock of sheep, then he started to blow on him and recite Al-hamdu Lillaahi Rabb il-‘Aalameen. Then he recovered quickly from his complaint and started walking, and there was nothing wrong with him. Then they have them what they had agreed to, and some of them (the Sahaabah) said, Let us share it out. The one who had performed ruqyah said, Do not do anything until we come to the Prophet (peace and blessings of Allaah be upon him) and tell him what happened, and we will wait and see what he tells us to do. So they came to the Messenger of Allaah (peace and blessings of Allaah be upon him) and told him what had happened. He

12. General Observations

It is observed that the existing structure of PIDM is similar to the conventional insurance. The insured will buy a protection from the insurer and the insurer will own the payment of all the accumulated premiums and surplus. This is because the transaction is based on sale and purchase where the ownership is mutually exchanged and transferred. As far as Shariah compliance is concerned, the subject matter of the *aqd* or contract must be well defined and known to the contracting parties. Major uncertainty renders a contract void. In the conventional insurance, uncertainty is obvious since the counter value is not known. The unfortunate event is also a matter of gambling. It also involves *riba al-fadl* as it is an exchange of money with money (cash with cash). Such cash exchange must be at par, but it is clear in the case of fees charged by PIDM as compared to the sum insured that the counter values vary. This is among the reasons why conventional insurance has been declared impermissible (*haram*) by the Fiqh Academy and the majority of Muslims scholars.²⁵

It is suggested that the concept and structures of *takaful* should be studied as an alternative to *al-kafala bi al-ajr* to be the underlying contract of PIDM. It sounds weird if *takaful* concept and structure can be used, but still the conventional insurance model is preferred and adapted for the purpose of the protection of the *takaful* benefits. Ironically, *takaful* operators are backed by conventional structure. Why not similar *takaful* model? This definitely will raise endless criticisms from the public and the global community.

12. Defining the Contractual Relationship and the Payment of Premiums to PIDM

There is a substantial question? Who is in need of the protection of PIDM? The policy holders or the *takaful* operator? Who is accountable to pay the premiums for the protection? If the protection premium is paid by the *Takaful* operator from its own account which is reflected in the balance sheet, this would amount to issuing guarantee. The *wakeel* should not give any guarantee. This is against the principle of *wakalah* as a *wakeel* should not be held liable to guarantee any loss except because of his negligence or misconduct. It is submitted that most of *takaful* operators now are using *wakalah* model where the *takaful* operator is a *wakeel* (agent) appointed by the participants to manage their risks fund and investment.

It is suggested that the contractual relationship between the participants and *takaful* operator is clearly *mu'awadhah* contract (commercial exchange), but the subject matter is the services rendered in underwriting, managing the fund which includes investment activities and payment of claims. Hence, the subject matter of *mu'awadhah* is not the *takaful* benefits.

said, "How did you know that it is a *ruqyah*?" Then he said, "You did the right thing. Share them out, and give me a share." And the Messenger of Allaah (peace and blessings of Allaah be upon him) smiled.

²⁵(Resolution 9: 9/2) December 1985, *Majelle Majma' Fiqh al-Islami*, vol2, p 545.

12.1 Payments of Premium to PIDM

The takaful benefit is actually a mutual guarantee and indemnity made by the participants among themselves. The strength lies in their agreement and promise as stated in the takaful contract to provide the financial assistance to the participating members during misfortune. The pool of premiums/ the risk fund/tabarru' fund should be treated as an independent entity with separate financial and legal entity. The cost of the protections for this tabarru' should be borne by the fund itself. This should be reflected in its balance sheet as one of its expenses; as premiums to PIDM for the protection, not in the share holders' balance sheet.

It should always be clearly stipulated in the takaful contract and takaful certificate that the takaful operator only acts on behalf of the participants through the risks fund for the benefits of the participants. As such takaful operators may issue protection certificates or guarantees but it is on behalf of the participants, not from the shareholders' mandate.

This proposal is also matching with the PIDM policy to take over the responsibility of takaful operator in case failure to manage the payment of takaful benefit. This is so because the participants in the takaful scheme can appoint or hire any operator to manage the scheme. This is because the contractual relationship between the participants and the takaful operator is only to manage the fund, conduct a prudent underwriting and payment of claims, not a seller and buyer relation of the protection. In this case it is known to the participants that PIDM will be the successor to replace the insolvent operator.

12.2 Personal Investment Account Portion in Takaful Scheme.

It seems that the new PIDM product, i.e. Takaful and Insurance Benefits Protection System (TIPS) is not silent about the savings in the personal investment account which is part and partial of most of takaful family and takaful investment link products.

It is worth noting that the takaful benefits will lapse if no claim is made because no unfortunate event happens, but the savings and the investment which is totally owned by the participants will never lapse and will become due upon maturity. The maturity value and early surrender value represent the participants' individual investment savings. The former is payable after maturity whereas the latter can be made prior to maturity. The protection for both withdrawals is up to RM 500, 000.²⁶

The question is again who should bear the cost for the protection? Since takaful operator is only acting as an agent, it is suggested that the cost for the protection should be borne by the investment fund.

²⁶ It is suggested that if the maturity value is also taken from other participants' contributions (on the ground of *ta'awun*), apart from the particular individual savings, this should be clearly spelled out in the takaful contract to get their consent.

Conclusion

To conclude, the protection of takaful benefit is justified for the benefits of the takaful participants and for a prudent and robust Islamic financial system. But as far as Shariah compliance is concern, the structure of *kafalah bi al-ajr* contract perhaps needs reconsideration since it may look like conventional insurance model. The possible alternative is takaful tabarru' model.

As far as Takaful Benefit Protection scheme is concerned, it is suggested that the premiums payable to PIDM is directly borne by the Takaful Risks Fund which represents contributions of all participants for their mutual help and indemnification which is realized through takaful benefits. Therefore, the guarantee and protection actually come from the risk fund performed by Takaful operator on behalf of the fund. The takaful contractual relation clearly defines the position of the operator which is only an agent (wakeel), not a guarantor.

As for the takaful participant's personal investment account which is reflected in the early surrender value and maturity value, it is suggested that the cost for the protection should also be borne by the participants through the investment fund.

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