Protecting Takaful consumers: Regulations and dispute resolution

The Islamic insurance model, Takaful, was introduced as an alternative to conventional insurance which is considered forbidden under Islamic law or Shariah law by Muslim jurists, and operates on the principles of risk-sharing, solidarity and mutual cooperation, which are based on Shariah law. While the global Takaful industry has grown exponentially in recent years, given the low base, the fact remains that Takaful premiums still account for less than 1% of the world's insurance premiums. ALI ASGHAR BHURIWALA and MUHAMMAD SHAHZAIN FARID delve further.


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The Takaful industry, like any other, is regulated by laws and regulations that are designed to protect consumers. These regulations aim to ensure that Takaful companies adhere to ethical and Shariah compliant business practices, provide adequate disclosure and transparency and resolve disputes in a fair and efficient manner.

The major challenge a consumer faces in the Takaful industry arises from asymmetric information. A typical insurance contract comes with many features and conditions for which consumers mostly lack the ability to assess and negotiate favorable terms. In the case of Takaful, contracts may be more complex in comparison with conventional insurance products. Also, Takaful products are usually being offered from the same intermediaries as conventional insurance products. This potentially leads to the consumer being vulnerable to price discrimination.

The biggest Takaful markets are the MENA region and Malaysia, while Takaful also has a decent footprint in Africa. In most jurisdictions, the Takaful industry is regulated by central banks/insurance regulatory authorities, and Shariah supervisory boards. These regulatory bodies protect consumers by ensuring that the Takaful insurer acts in accordance with Shariah law and other relevant regulations.

Regulation on consumer protection

Regulations on consumer protection vary within countries in the MENA region. In the Kingdom of Saudi Arabia, the regulatory authority, Saudi Central Bank (SAMA), has provided consumer protection principles which are to be observed by financial institutions while dealing with consumers. The principles include fair and equitable treatment of consumers and also ensure disclosure and transparency in the form of information about the product being offered. Furthermore, the insurer must protect the privacy of the consumer, and the consumer itself against fraud.

Similarly, the Central Bank of the UAE (CBUAE), the regulatory authority in the UAE, has also provided consumer protection standards for all licensed financial institutions. Moreover, the CBUAE has also provided regulations on Shariah compliance. The regulations direct Takaful insurers to educate consumers on the differences between conventional and Takaful products. They also stress upon insurers to provide consumers with adequate information regarding the product. Additionally, insurers must communicate to consumers the legal consequences of their choices.

Bank Negara Malaysia being the regulatory body for the Takaful industry in Malaysia plays a pivotal role in ensuring the compliance of Takaful insurers with Shariah law and other relevant regulations. Takaful insurers in Malaysia are required to share comprehensive information with consumers about their products, including the potential risks, terms and conditions applicable, and fees.

Market practice on consumer protection

The Takaful market has naturally adopted practices that are leading to the protection of consumers. Takaful insurers are using the risk-based approach to determine the extent of coverage required by consumers. Coverage requirement is being determined by algorithms which use risk profiles as input.

Moreover, products have being introduced in the market which provide protection against fraud and abuse by Takaful insurers. The insurer of these products further pushes the market to abide by standards when handling transactions related to consumers. This nudge further limits the chances of consumers falling victim to theft or fraud by the intermediary.

The development of the Takaful market in the MENA region has led to an increase in competition between the insurers, which in turn has benefited consumers with better products. With alternative Takaful products being available, consumer protection against exploitation has also increased.

Regulations and market practice on dispute resolution

In the UAE, Takaful companies have an internal complaint handling process to address customer grievances. The CBUAE has a consumer protection department that further investigates any complaint escalated to it. The regulator also has a consumer protection fund to compensate customers in the event of a company insolvency or default. In practice, an insurance dispute committee is responsible for hearing and resolving disputes. Initially, an attempt is made to resolve the dispute amicably between both parties. If the initial attempt is not successful, the committee will decide on the dispute. However, within a period of 30 days, the committee's decision is appealable to the competent First Instance Court.

In the case of Saudi Arabia, legislatures have developed a mechanism to resolve insurance disputes which is independent of the judiciary. Judicial authority has been granted to committees which are operating under the supervision of SAMA.

In Malaysia, Bank Negara Malaysia, being the regulator, has established the Financial Mediation Bureau. The Financial Mediation Bureau through its cost-effective mechanism resolves disputes between Takaful insurers and their customers.

Currently, in practice, there are two leading methods of dispute resolution. The first being mediation which involves assistance from an independent third party to reach an agreement without going to court. The second being arbitration, where both parties agree to resolve their dispute via a third party who will rule on the dispute based on rules agreed upon in advance.

Conclusion

While a lot of consumer protection and dispute resolution rules in insurance extend to Takaful as well, the effectiveness of these depends on several factors such as the local regulatory framework, the quality of Takaful operators and the level of consumer awareness.