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Authors
Mohd Hawari Mohammad Hussin *Bachelor of Commerce and Management, Lincoln University; Senior Consultant, Instructional Design & Partnership – Takaful, IBFIM*
Ahmad Mahfuz Ismail *Fellow of the Chartered Insurance Institute (FCII) (UK); Executive Diploma in Shariah Studies, Universiti Malaya, Malaysia*
Jimmi Lim Kok Hooi *Bachelor of Economics (Hons), AAII*

Technical Reviewer
Charan Kaur *The Associateship of the Malaysian Insurance Institute (AMII);*
Associateship Chartered Insurance Institute (ACII, UK), Chartered Insurer, (UK)

Editor
Sudha Shenoy *Editorial Board, Academy of Professional Excellence Pty Ltd, Australia*

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1

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CHAPTER OBJECTIVE

To understand risk and insurance in the context of the insurance market.

LEARNING OUTCOMES

After completing this topic you should be able to:

- *Explain risk and how it relates to insurance.*
- *Identify the types of risk that can be insured and the types of risk that cannot.*
- *Describe how insurance operates as a risk transfer mechanism and by pooling of risks.*
- *Understand the risk from an Islamic perspective.*
- *Analyse the relationship between risk and takaful.*

1.1 WHAT IS RISK?

In insurance, the word "risk" refers to the likelihood of an event happening and the severity of the negative consequences of that event. In other words, it always involves the uncertainty arising from the possible occurrence of given events, the outcome of which could leave a person in a worse position compared to what one was in, prior to the event.

People are exposed to several kinds of risks and their consequent misfortunes in life. Misfortunes can arise from daily activities in a number of ways. Some examples of misfortunes are:

Example
A sole breadwinner of a family gets involved in an accident and dies prematurely. The dependents are then faced with two immediate obvious forms of loss, emotional and financial.
Factory premises might get destroyed by a fire. The owners of the factory face property loss, loss of income and loss of lives. Further, employees may lose their jobs.

Some misfortunes are worse-off, and may lead to financial losses, affecting people emotionally or causing trauma.

The subscription of insurance helps people to overcome many types of misfortunes. However, some forms of losses cannot be compensated for, such as self-inflicted injury or act of crime.

Under such circumstances, insurance can only provide compensation which will help alleviate the impact of financial losses consequent to an unfortunate event.

Insurance is the payment of a small predictable amount of money (premium) to protect a person against a larger unpredictable expense (loss/claim). This transfers the risk from the insured to the insurance company for a fee.

Risk usually comes in a form of peril, which is the main cause of loss. Examples of perils include fire, theft, accident, liability, sickness, and premature death. When a peril occurs, the property may be damaged, lives may be lost, and people may get injured.

Table 1-1 ***Types of perils and losses***

PERILS	TYPES OF LOSS
Fire	Property damage, loss of profit
Theft	Property stolen, damage to property due to attempted theft
Accident	Damage to vehicle, injury to persons
Liability	Injury due to negligence, property damage
Sickness	Medical costs
Death	Premature death

1.1.1 PERIL AND HAZARD

Table 1-2 ***Peril and hazard***

TERM	DESCRIPTION
Peril	The prime cause of loss. ***Example**: If a restaurant is destroyed in a fire, the fire is the peril.*
Hazard	The condition that increases the chance of loss. It influences the outcome of the loss. There are two types of hazard: 1) **Physical Hazard** relates to the physical or tangible aspects of risks, which are likely to influence the occurrence and/or severity of loss. An unfavourable physical hazard increases the frequency and severity of the loss. Good physical features are likely to reduce the frequency or severity of the losses. **Examples:** Defective wiring in a building that increases the chance of fire. 2) **Moral Hazard** relates to the attitude and actions of a person. Persons with bad moral hazard are considered bad risks and must not be considered for insurance. However, moral hazard is difficult to ascertain as it is generally difficult to see the character of a person until a loss occurs. **Examples:** • *Intentionally burning unsold merchandise that is insured to claim from an insurer/takaful operator.* • *Procrastination in replacing a worn tyre, which results in an accident.*

1.1.2 ISLAMIC PERSPECTIVE OF RISK

In general, then there are no striking differences in the beliefs or philosophical perspectives of risk whether it is **Islam** or other faiths. Universally, Muslims are guided by the *Holy Quran* and *Hadith* with clarity, that each person has an instinct of self–preservation and a duty to take appropriate precaution to the best of his knowledge and effort (*ikhtiar*) and submission wholeheartedly upon Allah SWT (*tawakkul*) for any possible outcome of such effort.

Some references to this point are:[1]

- *"And put all your trust [in Allah], if you truly are believers."* **Quran Al Maidah V.5:2–3**
- *"If you all depend on Allah with due reliance, He would certainly give you provision as He gives it to the birds who go forth hungry in the morning and return with full bellies at dusk."* **Hadith ~Al–Tirmidhi by Umar bin Khattab (rah)**
- *"One day, Prophet Muhammad (pbuh) noticed a Bedouin leaving his camel without tying it and he asked the Bedouin, "Why don't you tie down your camel?" The Bedouin answered, "I put my trust in Allah." The Prophet then said, "Tie your camel first, then put your trust in Allah."* **Hadith ~At Tirmidhi**
- *"...let them pray with you taking all precautions and bearing arms... but there is no sin on you if you put away your arms because of the inconvenience of rain or because you are ill, but take every precaution for yourselves."* **An-Nisa V. 4.102**

1.1.3 CHARACTERISTICS OF INSURABLE RISK

Risks that can be insured are required to have certain characteristics. Not all risks can be insured. The main characteristics of insurable risks are as follows:

Table 1-3 ***Characteristics of insurable risks***

<table>
<tr><th>INSURABLE RISK</th><th>DESCRIPTION</th></tr>
<tr><td>Financial Value</td><td>Insurable risks should have a monetary value as insurers compensate losses in the form of money. If the risk is not capable of being measured in monetary terms, the insurer will not be able to calculate the amount to pay to the insured in the event of a loss. Therefore, insurable risks should involve losses that are capable of being financially measured.
The following are some examples of such risks:
<table>
<tr><th>Risks</th><th>Financial Measurement</th></tr>
<tr><td>Damage to property</td><td>Cost of repairs</td></tr>
<tr><td>Injury to third parties</td><td>Court awards</td></tr>
<tr><td>Death of life assured</td><td>Sum assured which is determined by a person's ability to pay a premium which is based on the person's financial standing/earnings.</td></tr>
</table></td></tr>
<tr><td>Large number of similar risks</td><td>In order for the insurer to be able to predict losses and calculate a suitable premium accurately, there must be a large number of similar risks. Therefore, if there are a large number of similar risks, only then can the risk be classified as an insurable risk. If there are only a few similar risks, the insurer will not be able to calculate a suitable premium as the principle of losses of a few borne by many cannot be applied.</td></tr>
</table>

[1] Fisher, Omar Clark. "A Takaful Primer: Basics of Islamic Insurance." scribd. Apr. 2013, Dubai, www.scribd.com/document/348520472/Takaful-Report-Primer-2013.

Table 1-3 *Characteristics of insurable risks*

INSURABLE RISK	DESCRIPTION
Pure Risk	Insurers will only insure pure risks. This is because there is no element of gain. In a pure risk situation, one will suffer a loss or incur no loss. Hence, there is no possibility of profiting from a pure risk.
No catastrophic losses	Catastrophic losses can have a devastating effect on insurers as insurers may not be able to bear the heavy losses. A catastrophic loss arises when a large number of risks incur losses at the same time or when one huge loss takes place. A multiple of small losses or one huge loss will have the same impact on the insurer. Examples of catastrophic losses include losses arising from wars and earthquakes.
Fortuitous losses	The loss must be accidental or fortuitous in nature and should not be intentional. Insurance cannot function properly and efficiently if losses are intentionally or fraudulently carried out by the insured. In other words, all types of losses that will be covered by a policy have to be fortuitous.
Insurable interest	"Insurable interest" is defined as the legal relationship between the proposer and the subject matter of insurance. If an insured wish to enforce a contract of insurance before the courts, he must have an insurable interest in the subject matter of the insurance. This means that he stands to benefit from its preservation and will suffer from its loss. The existence of an insurable interest in contracts of insurance is one of the main factors that differentiate insurance from gambling.
Legal and not against Public Policy	The item to be insured should be legal and not against public policy. For example, a planned bank robbery by an individual is illegal in nature and hence cannot be insured. Fines and penalties imposed by law are also not insurable as they are against the law. The simple reason as to why these risks cannot be insured is because the public does not condone these activities as they bring more harm to the public than good.
Reasonable premium	The premium must be reasonable and be in relation to potential loss. Risks that have high frequency and severity will attract a much higher premium than risks that have low frequency and severity. The reasonability of premium will be based on the risk factors and the insurer's administrative expenses.
Not Against Shari'ah	For takaful contracts, the risk covered must not be contrary to Shari'ah Law.

1.1.4 FUNCTIONS OF INSURANCE

Insurance is a financial instrument which seeks to provide protection against the financial losses caused by fortuitous events. Insurance is defined as:

An economic institution based on the principle of mutuality, formed for establishing a common fund, the need for which arises from chance occurrences of nature, whose probability can be fairly estimated.

The insurance service, therefore, involves payment of contracted benefits or compensation to the insured or a third party against unforeseen losses. This section outlines the two functions of insurance.

Figure 1-1 ***Functions of insurance***

Functions of Insurance

PRIMARY FUNCTIONS

- Risk Transfer Mechanism
- Common Pool
- Equitable Premium

SECONDARY FUNCTIONS

- Cost Stabilization
- Peace of Mind
- Reduction of Losses
- Means of Savings
- Source of Capital for Investments
- Employment Opportunities

PRIMARY FUNCTIONS

The primary functions of insurance are *risk transfer*, *common pool* and *equitable premium*. The insurer collects an equitable premium (premium equal to the risk brought to the pool) from the proposer and transfers it to the common pool. All losses are compensated for using the funds in the common pool. The entire process is known as risk transfer mechanism.

Table 1-4 ***Primary functions of insurance***

Risk Transfer Mechanism	Insurance acts as a risk transfer mechanism where the insured, in exchange for protection, pays a sum of premium to the insurance company and transfers the responsibility of loss or damage to their property to the insurer. Upon acceptance of the risk, the primary insurer is in the same position as the insured, in relation to the various uncertainties associated with the risk. This is known as the risk transfer mechanism.
Common Pool	The concept of the common pool was introduced from the early days of marine insurance wherein the merchants contributed to anyone who suffered a loss during the voyage. Insurers today also have pools better known as a class of portfolio, e.g. fire, into which all the premiums collected for that class of business are placed. In the event of any loss suffered by anyone contributing to this pool, the loss amount will be paid out from this pool.
Equitable Premium	The premium each insured contributes to the pool has to be equal to the risk brought to the pool. In other words, although the class of insurance may be similar, each insured will pay a premium that will justify the level of risk brought to the pool. For example, a wooden house will contribute more premium for a fire risk than a house constructed of concrete as a wooden house is more hazardous than a concrete one. A house built of wood will burn faster and the outcome in the event of a fire will be more than often be a total loss as compared to a house made of concrete in which case the loss may only be partial.

SECONDARY FUNCTIONS

The following are the secondary functions of insurance:

Table 1-5 ***Secondary functions of insurance***

Cost Stabilisation	With insurance, business enterprises do not have to freeze capital to provide for financial protection against losses. Insurance therefore provides a means of stabilising the costs involved in managing risks by the payment of a premium to get compensation in the event of a loss or damage. Excess capital can thus be invested in the expansion of their business.
Peace of Mind	Insurance provides peace of mind to businesses by removing fears and worries of losses of individuals and business executives. The removal of fears and worries helps to establish confidence and enables forward planning of economic activities.
Reduction of Losses	Insurers have the experience of handling risks and improving them by providing recommendations. This is because insurers in their day-to-day activities come across a number of risks and types of losses. Insurers will pass this information to their customers. This will help reduce losses and will benefit both the insured and the insurer.
Means of Saving	Insurance acts as a means of committed saving, especially in the case of endowment insurance. The investment element of this type of insurance contract is a form of saving while the protection element provides compensation in the event of death or permanent disablement. Hence the policy provides protection and savings to the insured.
Source of Capital for Investment	The common pool accumulates large funds which insurers hold as custodians and out of which losses are met. Insurers will usually invest these funds in the public and private sectors to earn interest. These investments will in turn contribute towards the overall development and economy of the country.
Employment Opportunities	The insurance industry in Malaysia has created various categories of employment opportunities. A number of people are employed as insurance company staff, insurance brokers, adjusters, life agents and general agents.

1.1.5 RISK SHARING AND TAKAFUL (MUTUAL INDEMNIFICATION)

In takaful, the risk from individuals or organisations is spread or shared with other individuals or organisations that form part of the takaful scheme. Individuals or organisations that participate in the scheme make a contribution to the takaful fund. In the event of the risk occurrence, the participants receive the proceeds from the takaful funds which help them to minimise their losses.

A takaful scheme is operated by a regulated institution called a 'takaful operator' who executes a "***mudharabah***" (profit sharing) or a "***wakalah***" (representative) contract between the takaful operator and the participants of the takaful scheme, or other suitable contracts that fits a particular scheme. This is to avoid *gharar* (uncertainty), *maisir* (gambling), and *riba* (usury), resulting from the utilisation of the buy & sell contract (risk transfer), which is currently being used in conventional insurance transactions.

1.1.6 RISK MANAGEMENT

Risk Management is a systematic approach to dealing with risks that threaten the assets and earnings of an individual or a business enterprise.

Risk Management involves the following steps:

- Risk Identification
- Risk Evaluation
- Selection
- Implementation
- Risk Control

The steps in risk management must be carried out one step at a time, beginning with risk identification. A wrongly identified risk may render the entire risk management process wrong or ineffective, and it may be of no value or even have an adverse effect.

RISK IDENTIFICATION

The first step in risk management is risk identification. This process takes a look at all the pure risks to identify:

- any physical damage to property,
- business interruption losses,
- possibility of liability lawsuits,
- losses arising from crime,
- moral hazards of key employees.

Loss exposures can be identified with the help of questionnaires, financial statements, flow charts and personal inspection of facilities.

RISK EVALUATION

Once the potential risk exposures are identified, the next step is to evaluate the possible losses. First, a Quantitative Analysis is used wherein numbers such as severity and frequency of risk exposure are identified. This is further supported by a Qualitative Analysis which uses workflow, open-ended questionnaires or verbal structure interviews to establish information.

SELECTIONS

The selection process includes:

- **Risk Avoidance** – For example, selling off the property
- **Loss Control** – Risk Managing methods to control losses
- **Risk Transfer** – To transfer the risk to an insurer
- **Risk Retention** – To set aside some funds to manage losses internally

The selection process is based on the financial impact on the profitability of the organisation as well as humanitarian aspects and legal requirements.

IMPLEMENTATION

Once the organisation takes a decision on the selection process, implementation automatically follows. The selection process may include the most appropriate technique or a combination of techniques.

RISK CONTROL

After implementation, a risk management programme has to be consistently monitored for its outcome, to ensure its effectiveness. Risk Management is a dynamic programme. Changes can be made whenever necessary to the implemented programme so that the results are positive and there is no redundancy or ineffectiveness.

2

CHAPTER 2 PRINCIPLES OF INSURANCE (CONVENTIONAL AND TAKAFUL)

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CHAPTER OBJECTIVE

To understand the legal principles of insurance & takaful and their application to insurance policies and takaful certificates.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Describe the essentials of a valid contract of insurance.*
- *Appreciate the principle of insurable interest.*
- *Explain when insurable interest needs to exist.*
- *Know what is meant by the principle of utmost good faith.*
- *Outline the consequences of non-disclosure of material facts.*
- *Recognise what is meant by the principle of indemnity.*
- *Identify the essential elements of Takaful.*
- *Acknowledge the Takaful business and operations.*

2.1 OFFER AND ACCEPTANCE

To obtain insurance coverage, the proposer has to complete a proposal form. The proposal form is a legal binding document between the proposer and the insurer. It is necessary that there is an element of insurable interest and the proposer declares all material facts.

Insurance is an agreement that consists of an offer made by an indication of one person (the "Proposer") to another (the "Insurer") of the proposer's willingness to enter into a contract on certain terms without further negotiations. The sum insured required for coverage must be adequate to protect the proposer against underinsurance and the average clause as the insurance policy operates on an indemnity basis (for most general insurance policies except personal accident and life insurance) Personal Accident and Life policies are known as benefit policies.

Both the parties to a contract must have the contractual capacity at the time of entering into a contract. Contractual capacity is the legal capability of a person to form a binding contract or the ability of a person to enter into a contract. A number of classes of people lack contractual capacity; and these include minors, the mentally challenged, those under the influence of an intoxicating substance, and incarcerated convicts.

All contracts are governed by the general principles of the Law of Contract as specified in the *Contracts Act 1950*.

2.2 LAW OF CONTRACT

A contract (*aqad* in Arabic) may be defined as a legally binding agreement between two or more parties, intended to have legal consequences, i.e. one which the law will enforce and recognise. It is a meeting of minds (*consensus ad idem*) signifying that the parties have agreed together about the same thing.

The parties to the contract must understand that the agreement shall be legally enforceable. Every contract is an agreement; but not every agreement is a contract. Agreements which are not legally binding are therefore not contracts.

The factors essential for the formation of a valid contract are:

Table 2-1 ***Elements of a valid contract***

Offer and Acceptance	There must be an offer by one party (offeror) and an acceptance of it by the other (offeree).
Intention to create legal relations	It is essential that parties to an agreement intend to be legally bound; otherwise, there would not be a contract between them. This intention may be inferred from the terms of their agreement, their conduct and surrounding circumstances.
Capacity of the parties	Each party must have the legal capacity to make the contract e.g. insurable interest, minors or infants.
Consent must be genuine	The consent must not be obtained by fraud or duress.

Consideration must be present	• In insurance and takaful contracts, the consideration is the premium/contribution provided by the insured/participant.
	• The Insured/Participant Pays Contribution
	• Parties must give consideration before an agreement can be legally binding. A consideration is a benefit which one party gives to another or a burden which one undertakes for the other.
	• The Insurer/Operator Indemnifies or Pays the Agreed Sum Assured
	• In general and family solidarity takaful contracts/insurance, the insured's consideration is to provide/pay or promise to provide/pay a contribution. The consideration by the operator/insurer, in the case of:
	  ○ General insurance/ takaful scheme certificate/policy is to promise to indemnify the insured when an insured loss occurs;
	  ○ Life insurance/ family solidarity takaful certificate/policy is to promise to pay the insured the sum assured and additional benefits, if any, when an insured event occurs.

Legality of Object	The object of the contract must not be one of which the law disapproves. In addition to these general characteristics, there are other elements that must be present for an insurance policy to be valid.

2.3 LAW OF TORTS

A *tort* has been defined as *"a civil wrong for which the remedy is a common law action for unliquidated damages, and which is not exclusively the breach of a contract or breach of a trust or merely equitable obligation"*. (*Salmond: Law of Torts*). Thus, a tort is a breach of an obligation, which is owed to persons as a whole, and is a breach of the general civil law.

2.3.1 NEGLIGENCE

Negligence is one of the most important in common laws of torts. For a person to sue another for negligence, it is necessary to prove that:

- the defendant was under a duty of care to that plaintiff;
- there has been a breach of that duty;
- The plaintiff has suffered damages as a result.

Example

Duty of care

- **Employers' liability** – An Employer owes a duty of care to employees as he is expected to provide a reasonably safe system of work, reasonably safe machinery and competent fellow employees.
- **Professionals' duties** – Doctors, surgeons, dentists, solicitors and other similar professionals owe a duty of care in the discharge of their duties to their clients or other persons with whom they are in a professional relationship.

2.3.2 STRICT LIABILITY

Strict liability is said to have come into force when a person is held responsible for an act even though he has not done it deliberately, recklessly or negligently.

Example

Negligence vs. Strict liability

Mr A had employed independent contractors to construct a reservoir on his land and to use the water power for his mill. During the construction, the contractors came across some unused mineshafts and passages filled with earth and mire which, unknown to them and the defendant, communicated with Mr B's mines. When the reservoir was filled with water, the water escaped through the shafts and flooded Mr B's mine. It was found that Mr A had not been negligent; nevertheless, Mr A was held liable.[2]

2.3.3 VICARIOUS LIABILITY IN TORT

Vicarious liability arises when one person is held liable for the torts of another, even though he (the person liable) is not a party to the tort or has not committed the tort in question.

Where A instructs B to commit a tort against C, A is liable, whatever liability may be attached to B. A is said to be vicariously liable and may be sued for the act which he himself ordered, even though he did not commit the tort, e.g. master-servant relationship.

[2] Rylands v. Fletcher [1868].

2.4 BASIC PRINCIPLES OF INSURANCE

The following are the fundamentals of insurance:

- Insurable Interest
- Utmost Good Faith
- Proximate Cause
- Indemnity
- Contribution
- Subrogation

2.4.1 INSURABLE INTEREST

An insurance policy does not carry with it the right to recover losses from a policy just because there is a loss. The insured must have an insurable interest to be able to recover the benefits of the policy.

What is insurable interest? Insurable interest means any legal right, title or interest in a property, life or liability in a manner that the policyholder suffers a financial loss by a misfortune happening on the subject matter.

Only a person who has the legal right on the subject matter at the time of inception of the policy and throughout the policy period has an insurable interest to insure the said subject matter under his or her name and is thereafter known as the insured or the policyholder.

When must Insurable Interest arise in respect of different Classes of Insurance?

- Life insurance - at inception of insurance
- General Insurances – at all times from inception until renewal as well as during currency of policy
- Marine Cargo insurance – at time of claim

SUBJECT MATTER OF INSURANCE

The subject matter of insurance may be any property of intrinsic value or any event, the happening of which is likely to cause the loss of a legal right or the creation of a legal liability.

Given below are some examples of the subject matter of insurance in some types of insurance.

Table 2-2 ***Types of insurance and their subject matter***

Motor	Car, motorcycles, etc.
Marine	Ship, cargoes
Personal Accident	Life, limbs, etc.
Aviation	Aeroplanes, passenger liability, etc.
Fire	Buildings, stock, etc.

DIFFERENCE BETWEEN THE SUBJECT MATTER OF INSURANCE AND THE SUBJECT MATTER OF THE INSURANCE CONTRACT

The subject matter of insurance should not be confused with the subject matter of the insurance contract. The subject matter of the insurance contract is the financial interest of an insured in the subject matter of insurance. For example, if a house is insured for RM100,000 the house is the subject matter of insurance and RM100,000 is the subject matter of the insurance contract.

PARTIES THAT HAVE AN INSURABLE INTEREST

In property insurance, persons such as owner, trustee, mortgagee, hirer or agent have an insurable interest on the property owned, held in trust, mortgaged, hired and held in trust or on commission. With regard to life and personal accident insurance, a person has unlimited insurable interest in his own life and limbs.

2.4.2 UTMOST GOOD FAITH OR *UBERRIMA FIDES*

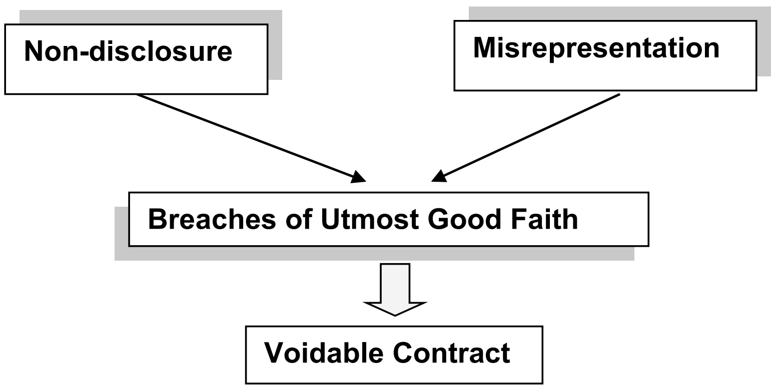
The insurance contract is not subject to the general rule of *caveat emptor* (let the buyer beware). It requires both the insurer and the insured to exercise utmost good faith or *uberrima fides* in their negotiation. The duty of utmost good faith can be defined as the positive duty to disclose fully and accurately all material facts related to the proposed risk that a proposer knows or is reasonably expected to know. A material fact is a fact that influences a prudent underwriter in deciding the acceptance of the risk or the premium to be charged. The materiality of a fact depends on the nature of the proposed insurance.

> ***Uberrima Fides***: *Perfect good faith; abundant good faith. This phrase is used to express that a contract must be made in perfect good faith, concealing nothing; as in the case of insurance, the insured must observe the most perfect good faith towards the insurer.*[3]

MATERIAL FACT

A fact that can bring about changes or increase the risk factor so much that it may influence the manner in which a prudent underwriter evaluates the risk is called a material fact. This information may be critical in determining whether a risk is acceptable or any additional consideration is required in underwriting the risk.

Figure 2-1 ***How a contract becomes voidable***



[3] The Free Dictionary by Farlex.

Table 2-3 ***Legislative requirements of the duty of disclosure***

Schedule 9 of the *Financial Services Act 2013* (FSA)	Sets out the pre-contractual duty of disclosure and representations for a contract of insurance:
	• It states that before a contract of insurance is entered into, a proposer shall disclose to the insurer all matters that
	  ○ he knows to be relevant to the decision of the insurer on whether to accept the risk or not and the rates and terms to be applied, or
	  ○ a reasonable person in the circumstances could be expected to know to be relevant.
	• It also states that the duty of disclosure does not require the disclosure of a matter that
	  ○ diminishes the risk;
	  ○ is of common knowledge;
	  ○ the insurer knows or in the ordinary course of his business ought to know; or
	  ○ in respect of which the insurer has waived any requirement for disclosure.
	• It further states that if the insurer does not pursue blank answers, incomplete or irrelevant answers given by the insured to the questions in the proposal form, compliance with the duty of disclosure in respect of the matter shall be deemed to have been waived by the insurer.

Schedule 9 Section 12 of the FSA	*Knowledge of, and statement by insurance agent* *12. (1) A person who is authorized by a licensed insurer to be its insurance agent and who solicits or negotiates a contract of insurance in that capacity shall be deemed, for the purpose of the formation or variation of the contract of insurance, to be the agent of the insurer and the knowledge of that insurance agent shall be deemed to be the knowledge of the insurer.* *(2) A statement made, or an act done, by the insurance agent shall be deemed, for the purpose of the formation or variation of the contract of insurance, to be a statement made, or act done, by the licensed insurer notwithstanding the insurance agent's contravention of subparagraph 11(1) or any other provision of this Act.* *(3) Subparagraph (1) shall not apply—* *(a) where there is collusion or connivance between the insurance agent and the proposer in the formation or variation of the contract of insurance; or* *(b) where a person has ceased to be an insurance agent of a licensed insurer and the insurer has taken all reasonable steps to inform, or bring to the knowledge of policy owners of the fact of such cessation.*

Table 2-3 ***Legislative requirements of the duty of disclosure***

	• The duty of disclosure of all materials facts will arise: ○ At the inception of the policy ○ At renewal ○ During the currency of an insurance. • When a breach of utmost good faith takes place, the insurance contract becomes voidable irrespective of whether the breach has been committed innocently or fraudulently. However, concealment and fraudulent misrepresentation may further entitle the insurer to sue for damages.
Section 141 (4) of the *Islamic Financial Services Act 2013* (IFSA)	• Sets out the duty of the proposer to disclose the material fact. Before a contract of takaful other than a consumer takaful contract is entered into, varied or renewed, a proposer shall disclose to the licensed takaful operator a matter that: ○ he knows to be relevant to the decision of the licensed takaful operator on whether to accept the risk or not and the Page 167 of 187 rates and terms to be applied; or ○ a reasonable person in the circumstances could be expected to know to be relevant. • It further states that the duty of disclosure shall not require the disclosure of a matter that: ○ diminishes the risk to the licensed takaful operator; ○ is of common knowledge; ○ the licensed takaful operator knows or in the ordinary course of his business ought to know; or ○ in respect of which the licensed takaful operator has waived any requirement for disclosure.

2.4.3 PROXIMATE CAUSE

When a loss occurs, the onus of proof of loss rests on the insured. If there is only one cause, the decision is quite straightforward with the insurer determining whether the said cause is insured under the policy. However, in the event of a loss or accident where there is more than one possible cause, the insurer will have to establish the initial cause or the efficient cause which brought about the loss without having any intervening cause that breaks the chain of events.

The proximate cause is also known as the root cause or main cause of a loss. The insurer is only liable for losses proximately caused by an insured peril.

The doctrine of proximate cause is based on the maxim *causa proxima non remota spectatur* which means that the proximate cause must be looked at and not the remote cause. So in the event of a loss where there are many causes, the proximate cause or the dominant or effective cause must be identified and attributed as the cause of the loss.

CHAIN OF EVENTS

When there is an unbroken chain of events, the insurer will be liable for the losses insured under the policy from the insured peril onwards, provided no excluded peril precedes an insured peril.

CONCURRENT CAUSE

When two or more perils occur concurrently, including the one that is insured, the following rule applies:

a) For losses that can be separated
    - The insurer is liable only for the losses caused by the insured peril.

b) For losses that cannot be separated
    - The insurer is liable for the full amount provided there are no excluded perils involved.

If there are excluded perils involved, the insurer will not be liable for the loss.

Example
Proximate Cause
• A shop and its contents were insured under a fire policy. A tank of acetylene gas used for welding exploded and caused the fire to a motor repair shop. The explosion of gas used for commercial purpose was an excluded peril. If the explosion occurred before the fire, the insurer would not be liable for the loss. However if the explosion happened after the fire, the insurer would be liable for the loss.
• An insured was involved in an accident and hospitalised but subsequently died of a disease unrelated to the accident. In this event, the insurer would only be liable to pay weekly hospital benefits arising out of the accident. No death benefits would be payable under the personal accident policy because the death was caused by an excluded peril, i.e. a disease.
• A life assured was accidentally knocked down by a vehicle while he was crossing the road and died as a result. The accidental collision resulting in the death was the proximate cause of the loss and the insurer would be liable for the death claim.

2.4.4 INDEMNITY

General insurance follows the rule that there must not be any profit gains from a loss. The principle of indemnity requires the insurer to restore and compensate the insured to the same financial position which the insured had enjoyed immediately before the loss, subject to any limitations under the policy. It is therefore important that insurance is estimated taking the market value into consideration and the sum insured is constantly reviewed so that in the event of a claim, there is no question of overinsurance or underinsurance.

Where a claim is valid, the insured can be indemnified (at the insurers' option) by way of cash payment, repair, replacement or reinstatement subject to the policy conditions. The maximum amount recoverable under any policy is limited by the sum insured or the limit of indemnity. However, the amount payable is also subject to the following clauses:

a) **Average Condition** – If the property sum insured is of lesser value than the market value, the insured shall be considered as being his or her own insurer for the difference and shall bear the rateable proportion of the loss accordingly.

b) **Excess/Deductible** – This is the first amount of a loss, which must be borne by the insured before the policy begins to pay. This amount is listed in the policy.

c) **Limits** – Certain perils/clauses carry a limit or maximum amount of compensation in the event of a loss due to the said peril or under the said clause.

Where the insurable interest is unlimited or cannot be defined, e.g. for items such as life, limbs, other physical attributes, personal accident and income benefit type of risks, the policies are subject to the principle of indemnity.

The methods used to indemnify the insured include:

- replacement cost less depreciation or the market value,
- amounts awarded by courts for liability cases,
- financial loss suffered by the insured under a money insurance,
- financial loss suffered as a result of an employee's or employees' dishonesty under fidelity guarantee insurance.

AGREED VALUE

An Agreed Value policy is a policy which undertakes to pay a specific sum that has been pre-agreed by both the insured and the insurer as the value of the subject matter at the inception of the risk. It does not take into account the market value at the time of the loss (both in terms of depreciation and appreciation). It is not permissible to issue an Agreed Value policy for motor insurance except for vehicles that are designed for private use only. This concession cannot be published in any prospectus or otherwise. Agreed valued policies are suitable for items such as antiques, priceless paintings, and jewellery.

2.4.5 CONTRIBUTION

When there is more than one policy on a said property, each participating insurer is liable for a portion of the loss. The compensation is usually made by an insurer indemnifying the insured and thereafter calling upon other insurers to contribute proportionately to the cost of the indemnity payment. This practice has changed now, and every insurer pays the portion of the share directly to the insured once the claim is assessed by the insurer against whom the claim was initiated. The process ensures that the principle of indemnity is always maintained and the insured does not gain from claims made against various insurers.

The contribution is applicable only when the following conditions are met. Policies are required to cover the same interests, perils, or subject matter of insurance, and there is an overlap between one policy and another. For contribution to apply, it is required that:

a) Two or more policies of indemnity exist and are in force.
b) The policies cover a common interest.
c) The policies cover a common peril, which gave rise to the loss.
d) The loss must involve a common subject matter covered by the policies.

The market practice of calculating contribution: *Property policies (not subject to average).*

The market agreement for calculating contribution in property policies (not subject to average) is:

$$\frac{Sum\ insured\ by\ particular\ insurer}{Total\ of\ sums\ insured\ by\ all\ insurers} \times \frac{Loss}{1} = Liability$$

Example

Market agreement for calculating contribution in property policies (not subject to average)

A insures	RM6,000
B insures	RM4,000
Loss	RM1,000
A pays	$\frac{RM6{,}000}{RM10{,}000} \times RM1{,}000 = RM600$
B pays	$\frac{RM4{,}000}{RM10{,}000} \times RM1{,}000 = RM400$

This principle does not apply to personal accident insurance, where a person may claim the full sum payable under several policies with different insurers. It is, however, customary for insurers to require a proposer to disclose in the proposal form details of any other personal accident policies held. Some offices include a policy condition rendering the insurance void if the insured has affected insurance with another insurer, without the written consent of the original insurer.

2.4.6 SUBROGATION

Subrogation is the right of one person to stand in the place of another and avail himself of all the rights and remedies of that other, whether enforced or not. The principle states that an insurer, having indemnified a person, will be entitled to exercise the insured's rights to claim from any negligent third party. The insured must assist the insurer in providing all information and documentation required by the insurer to exercise their subrogation rights.

The common law of the right of subrogation does not arise until the insurers have admitted liability with regard to the insured claim and paid for it. Due to problems arising from this doctrine, insurers place a condition in the policy giving themselves subrogation rights before a claim is paid (with the exception of marine insurance) but the insurer must take action in the insured's name.

Subrogation may arise from:

a) **Tort** – An act of negligence which is covered by the insured's liability policy as well as the compensation from legal standing.
b) **Contract** – A loss covered under a specific contract, e.g. money policy as well as under the contract entered by the insured and a third party who could be a professional security company carrying the money for the insured. The insurer will pay the insured and then seek recovery from the security company for their negligence.

c) **Statute** – A loss covered under the insured policy as well as under statute requirement.
d) **Subject Matter** – For a loss covered under the policy, the salvage of the subject matter is considered as exercising subrogation rights. Once the insurer makes a total loss payment, the insurer is entitled to the salvage which can be sold to reduce the losses.

2.5 TAKAFUL IN PRACTICE

Takaful is the Islamic alternative to conventional insurance protection. While both carry the same objectives of providing protection, the underlying intent and practice of takaful differ from that of conventional insurance.

2.5.1 OVERVIEW OF TAKAFUL

The teachings of Islam encourage peace, brotherhood, and economic security. Islam teaches that people help each other regardless of faith. When one is facing a misfortune, others should come and help to minimise the misfortune both emotionally as well as financially.

The primary concept of insurance works in the same manner where contributions from many are used to compensate the unfortunate few. This concept is accepted by Muslim jurists and does not contradict with the Shariah. In essence, the primary concept of insurance is synonymous with a system of mutual help. Similarly, takaful is also based on mutual assistance.

Takaful is a noun stemming from the Arabic verb *kafala,* meaning ‘to protect or to guarantee’. Thus, takaful means mutual help among a group to support the needy within the group through a fund contribution by group members.

The concept of takaful already existed during the times of the Prophet when Muslims contributed to a fund under the system of *aqila* for the purpose of helping members who were liable to pay “blood money” or *diyat* in a situation where a person was murdered unintentionally, or to pay ransom to release war prisoners.

2.5.2 TAKAFUL AND INSURANCE

Although the primary concept of insurance does not contradict the practices and requirements of the Shariah, there are certain elements which differentiate the current systems of insurance practices. While insurance works on the concept of the uncertainty of risk and investment of funds to achieve higher yields, the Takaful system is against:

a) ***Gharar*** – the element of uncertainty in the existing contract of insurance.
b) ***Maisir*** – the element of speculation/ gambling as the consequence of the presence of uncertainty.
c) ***Riba*** – usury earnings of interest on its investment activities.

The takaful system promotes cooperation among members, contributions to a certain fund for sharing responsibilities, assurance, protection and assistance between group members or takaful participants.

Conventional insurance is a risk transfer contract based on the buying and selling of "described risk" and uses the premiums paid by policyholders to pay claims, staff salaries, marketing, management expenses and investment. As the ownership of premium is transferred from the insured to the insurer, any excess or profit from the transactions belongs to the insurer. On the contrary, in the takaful system, takaful participants collectively own the fund and appoint an institution known as the takaful operator to manage the fund based on certain agreed terms and conditions. The sharing of profit or surplus is made after meeting the obligation of assisting fellow participants who are in need.

2.5.3 ESSENTIAL ELEMENTS OF TAKAFUL

The essential concepts that drive the acceptance of the takaful system include:

a) **Piety** – Devoutness or individual purification. All persons are accountable to Allah, and their success in the hereafter depends on their performance in this life on earth.
b) ***Ta'awun*** – Brotherhood or mutual assistance. Cooperation for common good.
c) ***Tabarru'*** – Donation. Every certificate holder donates his or her contribution to help those in need.
d) **Mutual Guarantee**.
e) **Self–sustaining operations as opposed to profit maximisation** – Losses are divided and gains are distributed according to an agreed takaful model.

TABARRU'

The takaful contract involves the concept of *tabarru'* (to donate for the benefit of others as opposed to paying a premium as in conventional insurance) and mutual sharing of losses.

By definition, *tabarru'* is the agreement by participants to hand over a donation of a certain portion of the takaful contribution that they agree or undertake to pay, thus enabling them to fulfil their obligation of mutual help and joint guarantee, should any of their fellow participants suffer a defined loss. The concept of *tabarru'* eliminates the element of uncertainty in the takaful contract.

SHARIAH COMMITTEE

The Islamic Financial Services Act 2013 contains a provision that requires all takaful operators to establish a Shariah Committee. This requirement complements the roles played by the Shariah Advisory Council (SAC) of Bank Negara Malaysia.

Shariah Advisory Council (SAC) of Bank Negara Malaysia

The Shariah Advisory Council of Bank Negara Malaysia (SAC) was established in May 1997 as the highest Shariah authority in Islamic finance in Malaysia. The SAC has been given the authority for the ascertainment of Islamic law for the purposes of Islamic banking business, takaful business, Islamic financial business, Islamic development financial business, or any other business, which is based on Shariah principles and is supervised and regulated by Bank Negara Malaysia. As the reference body and advisor to Bank Negara Malaysia on Shariah matters, the SAC is also responsible for validating all Islamic banking and takaful products to ensure their compatibility with the Shariah principles. In addition, it advises Bank Negara Malaysia on any Shariah issue relating to Islamic financial business or transactions of Bank Negara Malaysia as well as other related entities.

In the recent 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 Shariah matters pertaining to Islamic banking, takaful and Islamic finance. While the rulings of the SAC shall prevail over any contradictory ruling given by a Shariah body or committee constituted in Malaysia, the court and arbitrator are also required to refer to the rulings of the SAC for any proceedings relating to Islamic financial business, and such rulings shall be binding.

Consisting of prominent Shariah scholars, jurists and market practitioners, members of the SAC are qualified individuals and have vast experience in banking, finance, economics, law and application of Shariah, particularly in the areas of Islamic economics and finance.

At the takaful operator level, the duties of the Shariah Committee, among others include the following:

- To provide objective and sound advice to the TO to ensure that its aims and operations, business, affairs and activities are in compliance with Shariah;
- To provide a decision or advice to the TO on the application of any rulings of the SAC or standards on Shariah matters that are applicable to the operations, business, affairs and activities of the TO;
- To provide a decision or advice on matters which require a reference to be made to the SAC;
- To provide a decision or advice on the operations, business, affairs and activities of the TO which may trigger a Shariah non-compliance event;
- To deliberate and affirm a Shariah non-compliance finding by any relevant functions;
- To endorse a rectification measure to address a Shariah non-compliance event.
- To develop a reasonable understanding of the business and operations of the TO and keep abreast with relevant market and regulatory developments

SURPLUS–SHARING

What is surplus? While it is not entirely unique to Takaful because mutual insurance and some cooperative forms of life insurance (i.e. with profit plans) practice surplus sharing, it is a fundamental feature of any Takaful model. In practice, modes of calculation of surplus, the timing of distribution, even the split between reserves and payouts to participants are supervised by the SSC, which clearly differentiates Takaful surpluses from the treatment of conventional surplus.

How is surplus distributed? Any remaining funds from annual operations of the Takaful model forming the surplus should be treated in one of three approved ways.

a) Surplus may be distributed to all policyholders equally on a pro-rata basis to their original contributions.
b) Surplus may be distributed to all policyholders except those who were awarded claims settlement compensation.
c) Surplus may be adjusted so that any claims settlements are offset to each certificate holder's surplus allocation prior to distribution.

QARD AL–HASAN (BENEVOLENT LOAN)

Only one type of loan is permitted under Islamic principles, which is a **Qard al-Hasan** (literally benevolent loan). To avoid Riba, a lender of money may not demand any fixed charge or premium above the actual amount loaned out.

As mentioned in the *Holy Quran*, *Qard al-Hasan* is purely a philanthropic gesture whereby the reward is meant for the hereafter and not to attract any premium or surplus capital above that which was provided in the first place. Instructions especially encourage the extension of time if the borrower has difficulty in repayment, or forgiveness of the capital sum itself as being more praiseworthy. However, it is difficult to comprehend in today's regulated insurance world how shareholders could 'forgive' *Qard al-Hasan* without attracting significant criticism.

Qard al-Hassan will be applied in the situation when the takaful fund is depleting, it is obligatory for the shareholders of the takaful operator to 'lend' their money to the takaful fund, at zero interest/ charges on the loaned money.

ZAKAT

The purpose of Zakat as an annual charge on a person's wealth is two-fold:[4]

a) individual purification through acts of charity to benefit the poor and disadvantaged, and
b) protection and purification of the remaining portion of wealth.

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[4] Fisher, Omar Clark. "A Takaful Primer: Basics of Islamic Insurance." scribd. Apr. 2013, Dubai, www.scribd.com/document/348520472/Takaful-Report-Primer-2013.

The payment of Zakat is obligatory as one of the five pillars of Islam. Zakat is a major economic means for establishing social justice and leading the community towards shared prosperity and security. To calculate the appropriate amount due, the wealth must exist for one lunar year, exceed a *nisab* (minimum amount) and adhere to specific regulations pertaining to the classification of that wealth. As applies to the common 'hybrid' Takaful model, participants will not be charged for Zakat on their donations to the Takaful risk pool. However, the accumulated savings in their individual investment accounts linked to Takaful risk-sharing are Zakatable whether payment is made annually on the incremental gains in wealth, or upon withdrawal of the entire principal amount.

2.5.4 THE TAKAFUL CONTRACT

The Takaful contract between the participants and the takaful operator is based on the principle of Mudharabah, Wakalah or Wakalah-Mudharabah models. The IFSB – 8: Guiding Principles on Governance for Takaful (Islamic Insurance) Undertakings which was issued in December 2009, affirmed, at the time of preparing the standard, that these are the most commonly used models worldwide.

Mudharabah Model

Mudharabah is defined as the contract between the rabb-ul-mal (capital providers - participants) with the mudharib (entrepreneur – takaful operator). The participants provide the capital and the takaful operator provides the skills in the business venture. When there is profit and/or underwriting surplus, it is shared between the participants and the takaful operator in a pre-agreed manner. The takaful operator will accept payments of tabarru' (donations) from the participants to manage and invest. Any financial losses shall be solely borne by the participants, unless the losses are attributable to the takaful operator's misconduct or negligence.

Wakalah Model

Wakalah is based on the wakalah contract (representative / agency contract) between the takaful operator and the participants. Here, the takaful operator is an agent of the participants. Under this contract, the takaful operator charges wakalah fee for administrating and managing the funds for the participants, usually a percentage of the contributions paid. The wakalah fee must be pre-agreed and stated in the takaful contract. Certain wakalah models allow 'performance fees' where the underwriting surplus are shared (apart from the wakalah fee) with the takaful operator.

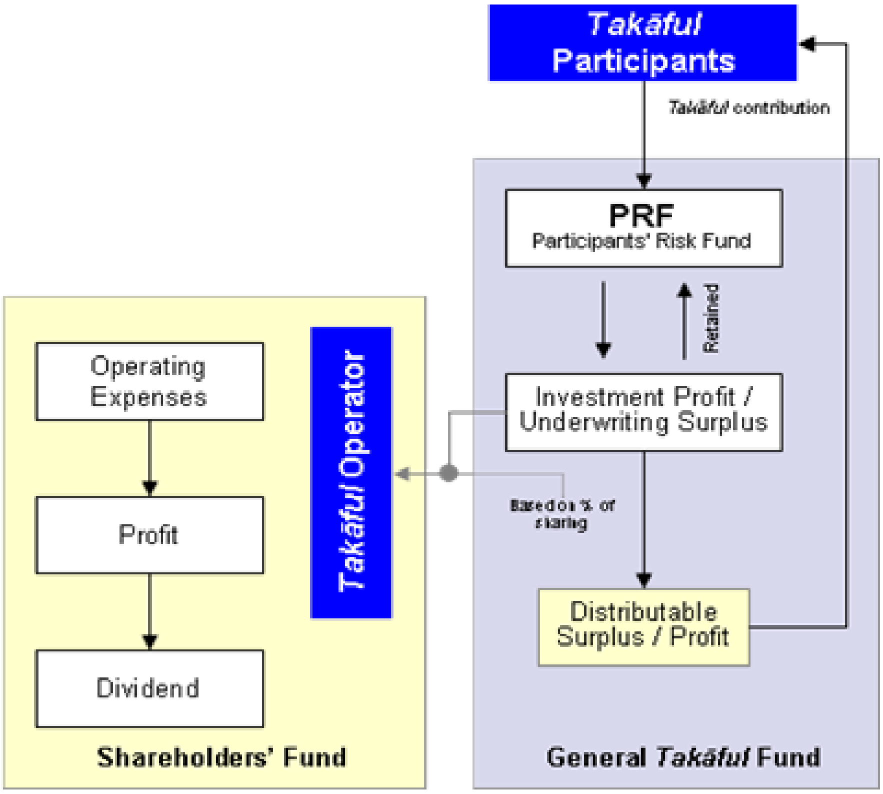
Wakalah-Mudharabah Model

Under a wakalah-mudharabah model, the wakalah contract is adopted for underwriting activities while the mudharabah contract is adopted for the investment activities.

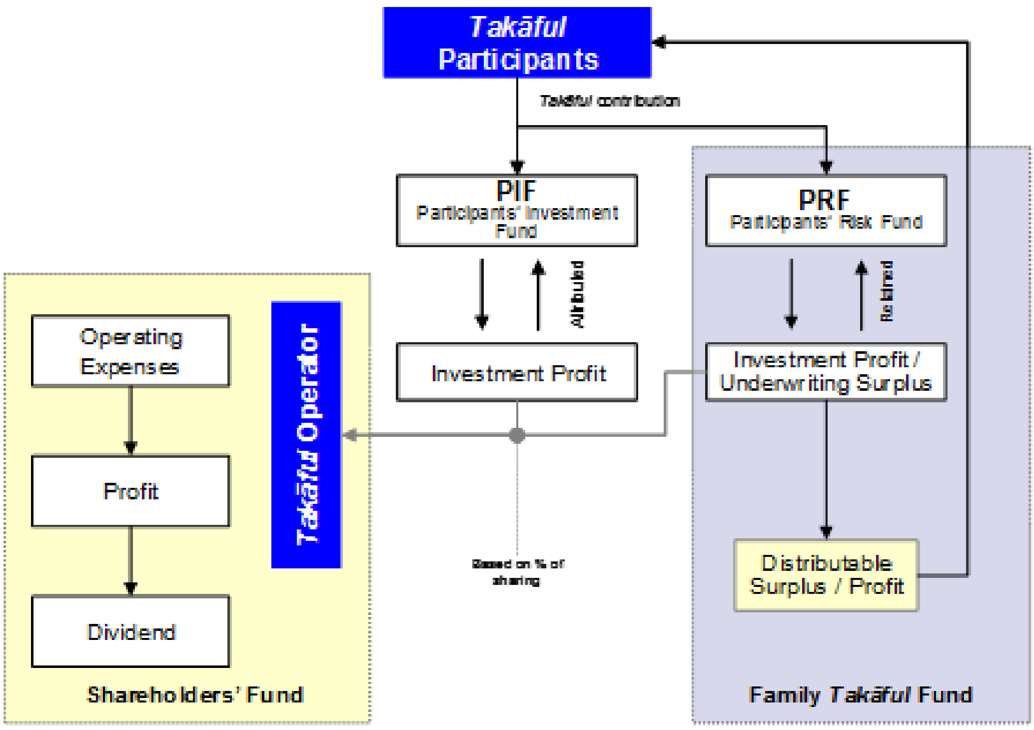
(You may refer to the supplementary notes for the illustration of how the above models work. These models are generic in nature and may differ between different takaful operators)

Below are the illustrations of how the Takaful models works, which most commonly used worldwide.

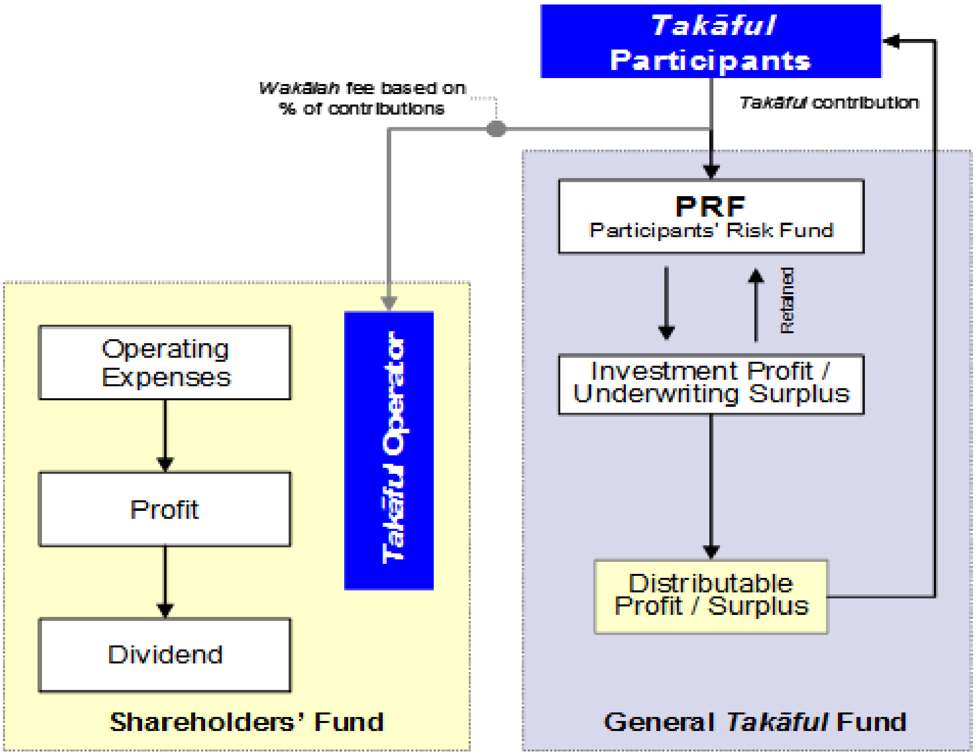
(a) Muḍārabah-based Takāful Contract – General Takāful



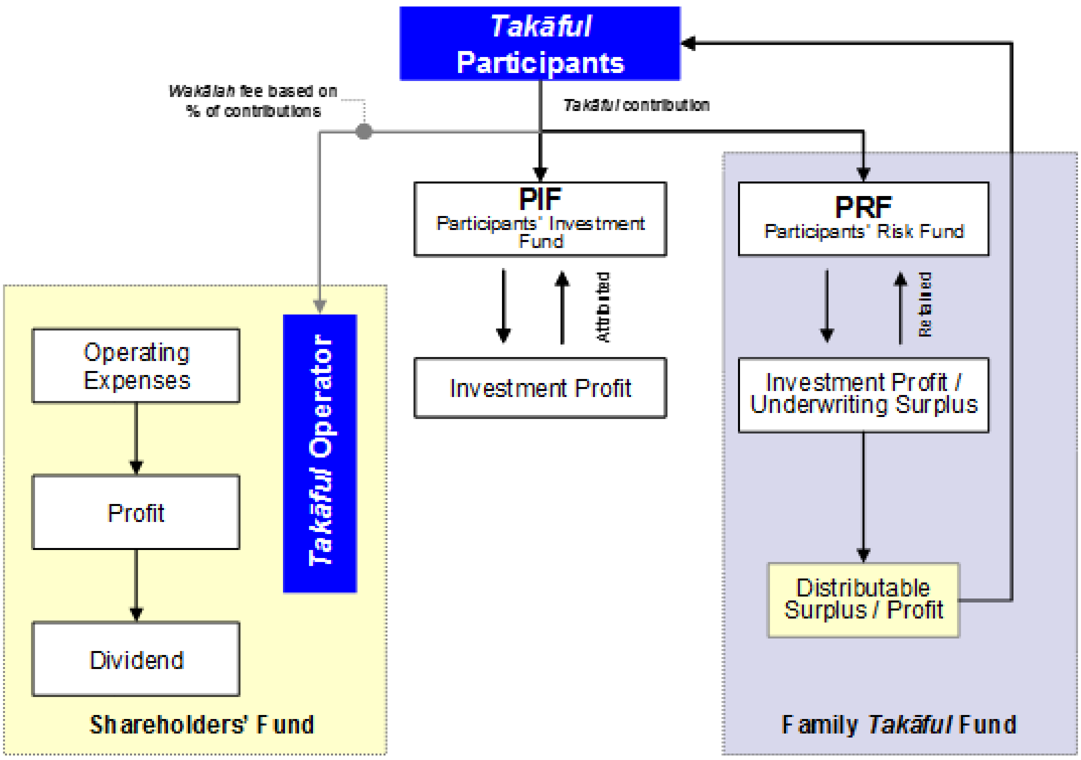
(b) Muḍārabah-based Takāful Contract – Family Takāful



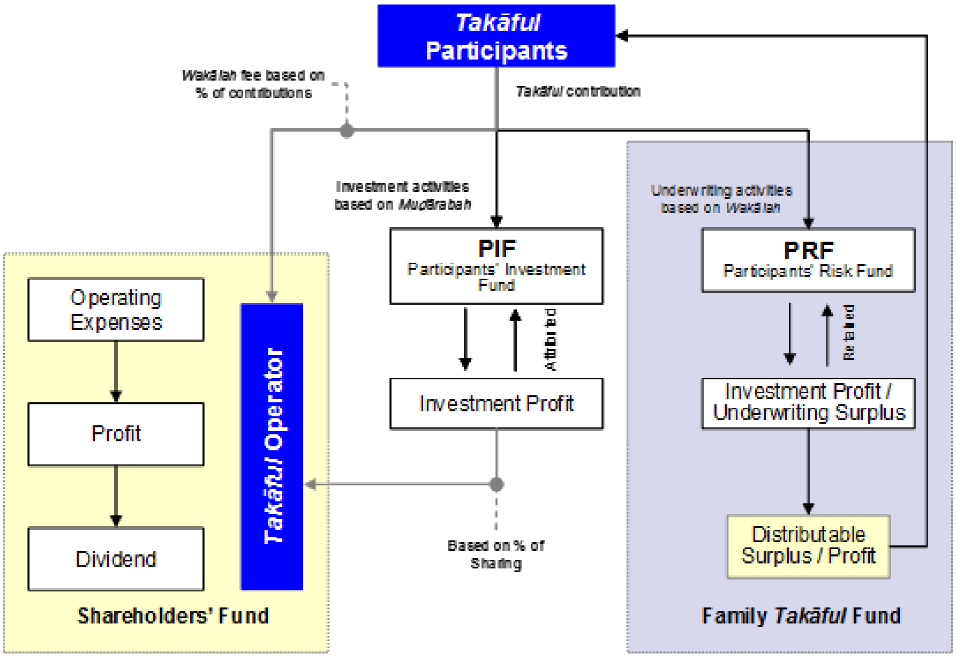
(c) Wakālah-based Takāful Contract – General Takāful



(d) Wakālah-based Takāful Contract – Family Takāful



(e) Wakālah–Muḍārabah-based Takāful Contract – Family Takāful



Notes:

1) *In Malaysia, mudharabah model was first adopted by Syarikat Takaful Malaysia Berhad (STMB) in 1984 and then by MNI Takaful Sdn. Bhd. in 1993. This model is no longer issued for new certificates.*

2) *Now all Malaysian Takaful Operators use wakalah model with some variations which allow performance fee (ju'alah) as a percentage of surplus for managing the Participant Risk Fund. Some use a combination of Wakalah and Mudarabah for different purposes and funds (PRF, PIF Investment).*

2.5.5 ASPECTS OF TAKAFUL OPERATIONS

The important aspects of takaful operation are as follows:

a) The takaful operator provides various takaful plans to cover risks, namely business risks and pure risks, which are allowable by the *Shariah*. Persons who enter these plans are known as takaful participants.

b) The takaful business is not a contractual transfer of risk. The takaful company does not assume the risk. It is the group of members or participants of takaful plans who agree to jointly guarantee against loss or damage that may fall upon any of them.

c) The takaful operator acts as an asset manager and profit distributor on behalf of all the participants. In the takaful business venture, profit sharing follows the principle of *mudharabah*. The distribution of profit follows a pre-agreed ratio.

d) Participants of takaful plans make donations (*tabarru'*) or instalments that are accumulated in the Takaful Fund. This fund may be invested in areas acceptable to the *Shariah*. Payments of all takaful benefits are made by the fund.

e) In order to fulfil the obligations of mutual help in the concept of takaful, participants make an *aqad* (agreement) at the outset, to pay part or the whole of the takaful contributions as *tabarru'*. The agreement shall be an *aqad* of helping and cooperating and not an *aqad* of buying and selling. However, the tabarru' proportion defines the participant's share of the risk computed using the same actuarial principles as in conventional insurance.

f) The *Islamic Financial Services Act 2013* divides takaful into two broad business categories of family takaful and general takaful.

2.5.6 TYPES OF TAKAFUL BUSINESS

The takaful businesses carried on by Malaysian takaful operators are broadly divided into family takaful business and general takaful business.

FAMILY TAKAFUL BUSINESS

A family takaful plan is a combination of long-term investment and a mutual financial assistance scheme. The objectives of the plan are:

a) To save regularly over a fixed period of time;
b) To earn investment returns in accordance with Islamic principles; and
c) To obtain coverage in the event of death prior to maturity from a mutual aid scheme.

Each contribution paid by the participant is divided and credited into two separate accounts, namely:

a) **The Participants' Special Account (PSA)** – A portion of the contribution is credited into the PSA on the basis of *tabarru'*. The amount depends on the age of the participant and the cover period.
b) **The Participants' Account (PA)** – The balance goes into the PA, which is meant for savings and investments.

Examples of covers available under the family takaful businesses are:

- Individual family takaful plans,
- Takaful mortgage plans,
- Takaful plans for education,
- Group takaful plans, and
- Health/medical takaful.

GENERAL TAKAFUL BUSINESS

The general takaful scheme is purely designed for mutual financial help on a short-term basis, usually 12 months. The scheme provides compensation to its participants for any material loss, damage or destruction that any of them might suffer, arising from a misfortune that might inflict upon their properties or belongings. The contribution that participants pay into the general takaful fund is solely on the basis of *tabarru'*.

At the end of the period, if there is a net surplus in the general takaful fund, it shall be shared between the participants and the operator in accordance with the principle of *Mudharabah*, provided the participant has not incurred any claim and/or not received any benefits under the general takaful certificate.

Examples of covers available under general takaful provided by takaful operators include:

- Fire Takaful Scheme,
- Motor Takaful Scheme,
- Accident/Miscellaneous Takaful Scheme,
- Marine Takaful Scheme, and
- Engineering Takaful Scheme.

3

CHAPTER 3 THE MARKETPLACE

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CHAPTER OBJECTIVE

To understand how the insurance/takaful market operates.

LEARNING OUTCOMES

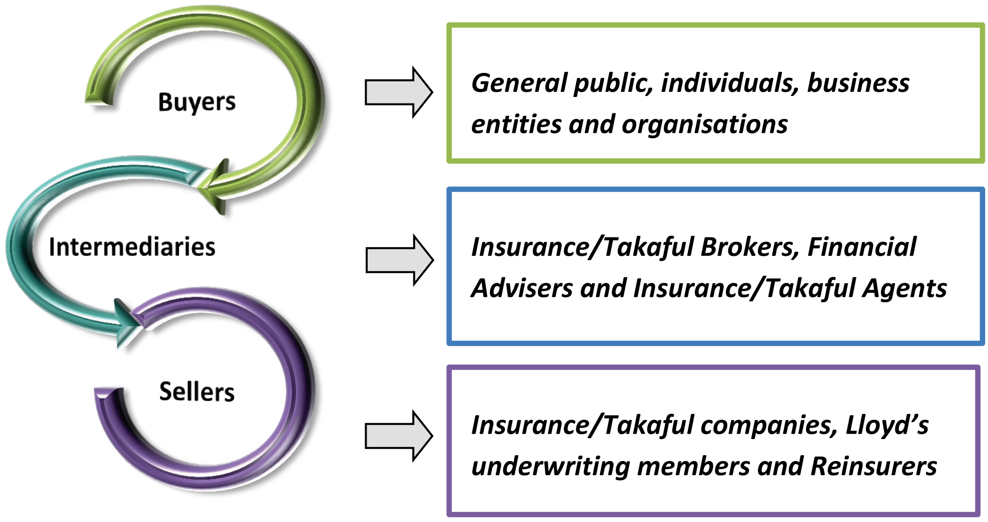
After you complete this chapter, you should be able to:

- *Identify the key players in the insurance/takaful marketplace.*
- *Differentiate between direct and intermediated distribution channels.*
- *Know the various insurance/takaful professionals, their respective roles and responsibilities.*
- *Appreciate the various insurance/takaful associations in Malaysia, their roles and objectives.*

3.1 THE INSURANCE AND TAKAFUL MARKETPLACE

The insurance and takaful industry, a service industry, is recognised as being part of the financial services sector of the economy. As in any typical industry, the insurance and takaful industry comprises buyers (the public, individuals, business entities and organisations), intermediaries (insurance/takaful brokers, financial advisers and agents), and sellers (insurance/takaful companies and Lloyd's underwriting members), as shown in the following figure.

Figure 3-1 ***Insurance and takaful industry participants***



3.1.1 THE BUYERS

Individuals may purchase personal insurance such as a motor, medical, mortgage protection or life assurance, while industrial and commercial enterprises require insurance coverage for protection from property and liability risks. Some forms of insurance are compulsory by law. For example, in Malaysia, motor insurance is mandatory under the *Road Transport Act 1987.* It is also mandatory for employers to insure foreign workers with an approved insurance scheme under the *Amended Workmen's Compensation Act 1952*.

Insurance regulations in Malaysia (Section 127 of the *Financial Services Act 2013* and Section 139 of the *Islamic Financial Services Act 2013*) prohibit obtaining general insurance/takaful outside Malaysia without the prior written approval of Bank Negara Malaysia. Buyers are therefore compelled to seek a licensed general insurer/takaful operator in Malaysia to purchase general insurance/takaful according to their insurance needs.

3.1.2 THE INTERMEDIARIES

The services of an intermediary may be required when a buyer is dependent on some expert advice to assess the risks they have and to match their needs with the best seller of insurance in the marketplace. An intermediary helps to match the insurance needs of a buyer with the most appropriate product or products available and supplied by the seller. This brings together the buyer and the seller, for which the intermediary earns a commission if he is an agent or brokerage if he is an insurance/takaful broker.

INSURANCE/TAKAFUL

Agents

As defined under the *Financial Services Act 2013* and *Islamic Financial Services Act 2013*, an "insurance agent" or "takaful agent" is a person who does all or any of the following:

a) solicits or obtains a proposal for insurance /takaful certificate on behalf of an insurer /takaful operator;
b) offers or assumes to act on behalf of an insurer/takaful operator in negotiating a policy/certificate; or
c) does any other action on behalf of an insurer/takaful operator in relation to the issuance, renewal or continuance of a policy/certificate.

In the event a person (the buyer) is induced to enter into, vary or renew a contract of insurance/takaful by misleading, false or deceptive statements, the contract of insurance/takaful shall be voidable and the person (the buyer) shall be entitled to rescind it.

In addition, a person who is authorised by a licensed insurer/takaful operator to be its insurance/takaful agent and who solicits or negotiates a contract of insurance/takaful in that capacity shall be deemed, for the purpose of the formation or variation of the contract of insurance/takaful, to be the agent of the insurer/takaful operator and the knowledge of that insurance agent shall be deemed to be the knowledge of the insurer/takaful operator.

An insurance/takaful agent must be registered with a licensed insurer/takaful operator and disclose the name of the licensed insurer/takaful operator (life, general or takaful business) he represents.

INSURANCE/TAKAFUL BROKERS

As defined under the *Financial Services Act 2013* and *Islamic Financial Services Act 2013*, an "insurance broker" or "takaful broker" means a person who, as an independent contractor, carries on insurance/takaful broking business and includes a reinsurance/retakaful broker. "Insurance broking business" or "takaful broking business" means the business of soliciting, negotiating or procuring a policy/certificate with an insurer/takaful operator or the renewal or continuance of the policy/certificate for a policy/certificate owner other than for himself, and includes reinsurance/retakaful broking for an insurer/takaful operator.

In Malaysia, an insurance/takaful broker is a person approved by Bank Negara Malaysia to carry on insurance/takaful broking business, and must have at all times in force a professional indemnity insurance or takaful of such amount as may be specified by the Bank (section 11 of the *Financial Services Act 2013* and the *Islamic Financial Services Act 2013* respectively).

It is mandatory for insurance/takaful brokers to be members of the Malaysian Insurance and Takaful Brokers Association (MITBA), and to continuously enhance insurance/takaful brokers' professional skills and maintain the professional competency of their employees.

LLOYD'S BROKERS

Lloyd's is the world's specialist insurance market. Unlike many other insurance brands, Lloyd's is not a company; it is a market where the members join as syndicates to insure risks.

The Lloyd's broker carries out the same function as an insurance broker but if one wishes to insure at Lloyd's, the business must be placed through Lloyd's broker. The Council of Lloyd's registers broking firms to act as Lloyd's brokers. Those wanting to be Lloyd's brokers must satisfy the Council as to their expertise, integrity and financial standing. The Lloyd's broker represents the insured in transactions with the underwriter.

3.1.3 THE SELLERS

Suppliers of insurance/takaful come in various forms – Insurance Companies, Takaful Operators Lloyd's, Mutual Indemnity Associations (similar to Takaful Operators), Captive Insurance Companies, the State (Government Compensatory Schemes) and Reinsurance Companies, Retakaful Operators as shown below:

Figure 3-2 ***Suppliers of insurance/takaful***

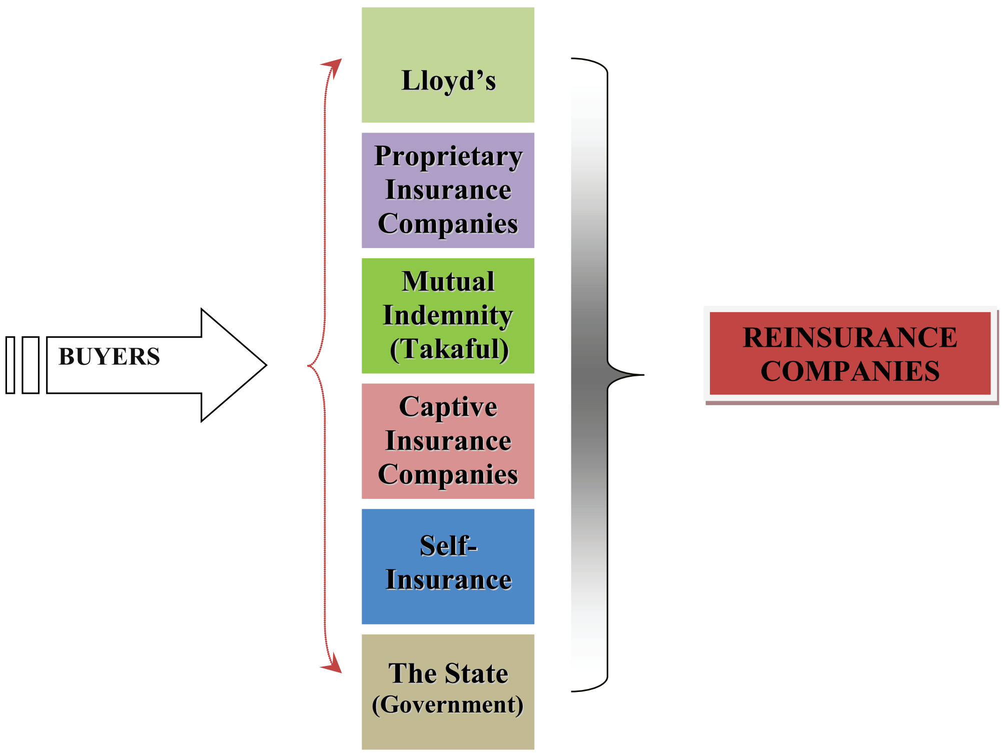


Table 3-1 ***Suppliers of insurance/takaful***

Insurance Companies / Takaful Operators	In a broad sense, insurance may include private insurance, government compensatory schemes and takaful business. The sellers of private insurance are the insurance companies, which are classified in accordance with their legal form or structure as follows: **1) Proprietary Companies** • A proprietary company is a limited liability company with a subscribed or guaranteed capital. Any profits made by the operations of a proprietary company belong to its shareholders who are the proprietors of the company. • In Malaysia, domestically incorporated or foreign incorporated companies may transact insurance business but they must be a public company incorporated under the *Companies Act 1965*. The company is liable for its debts and if the solvency margin cannot be met, the company will go into liquidation. Licence or approval to carry on insurance business is granted only if the prescribed minimum capital funds (for a company) or surplus of assets over liabilities (for a Malaysian branch of a foreign institution) is maintained at all times. **2) Mutual Companies** • A mutual company is a cooperative incorporated as a company owned by the policyholders and profits earned may be shared by policyholders or used to build up the surplus of the company. In Malaysia, there was a cooperative insurance society (established in 1954) which carried on life

Table 3-1 ***Suppliers of insurance/takaful***

	and general insurance business but because of the insurance regulations that came into force in 1997 (the *Insurance Act 1996*), it had to transfer its business to a public company in 1998. • The concept of mutual insurance originated in England in the late 17th century to cover losses due to fire. The mutual/casualty insurance industry began in the United States in 1752 when Benjamin Franklin established the *Philadelphia Contributionship for the Insurance of Houses from Loss by Fire*. • The global trade association for the industry, the International Cooperative and Mutual Insurance Federation (ICMIF), represents the cooperative and mutual insurance sector. ICMIF aims are to promote and work with the cooperative and mutual insurance sector globally by providing valuable, cutting-edge information and services to members and by representing the interests of the global cooperative and mutual insurance sector. As in 2014, ICMIF represents over 220 of the leading cooperative and mutual insurers from more than 70 countries.

Captive Insurance Companies	• Captive insurance is a tax-efficient method of transacting insurance, which has become more common in recent years among large national and international companies. The parent company forms a subsidiary company to underwrite certain of its insurable risks.
	• The main incentives to set up a captive insurance company are to:
	    ○ obtain the full benefit of the group's risk control techniques;
	    ○ pay lower premiums based on its own experience and avoid contributing to the direct insurer's overhead expenses and profit margin;
	    ○ obtain reinsurance directly at a lower cost;
	    ○ be able to insure risks that otherwise may not be easily obtained;
	    ○ retain profits within the group.
	• In Malaysia, the *Labuan Financial Services and Securities Act 2010* (LFSSA) issues captive insurance licences to Labuan companies incorporated or registered under the *Labuan Companies Act 1990*. A Labuan captive insurer may underwrite direct insurance or reinsurance (general or life) business risks:
	    ○ of their own Group; or
	    ○ third party risks subject to Labuan Financial Services Authority's (LFSA) approval.
	• A Labuan captive insurer may obtain reinsurance coverage from any insurance company in or outside Labuan irrespective of whether it is licensed under LFSSA. Worldwide, many captives are operated from offshore locations like Bermuda, Guernsey and the Isle of Man to tap into all the necessary and ancillary services such as investment management, banking, and accounting, while reducing the volume of paperwork involved in registering as an insurer.

Table 3-1 ***Suppliers of insurance/takaful***

Self-Insurance	• As an alternative to purchasing insurance in the market or as an adjunct to it where the first layer or proportion of a claim is not insured in the commercial market, some public bodies and large industrial concerns set aside funds to meet insurable losses. • There is a distinct difference between "self-insurance" where a conscious decision is made to create a fund and "non-insurance" where either no conscious decision is made at all, or where no fund is created. A major disadvantage in self-insurance is in the unlikely event of a catastrophic loss, the fund can be wiped out and the company forced into liquidation.
The State (Government)	• In Malaysia, the government acts as an insurer to provide social security in certain contingencies under the Employees' Social Security Act 1969. The Social Security Organisation (SOCSO/PERKESO) was set up to administer, enforce and implement contributions payable to the organisation by the employer and payment of compensation for employment injuries in respect of an insured employee. • SOCSO originally covers Malaysian workers whose monthly wages do not exceed RM 3,000 and whose age is **below 60 years**. However, with the amendment to the Employees' Social Security (Amendment) Act 2015, contribution has been made compulsory for all employees. Certain categories of employees are exempted from the coverage of the Employees' Social Security Act, 1969. They are as follows: i) Federal and State Government permanent employees ii) Domestic servants iii) Self-employed iv) Spouses of a sole proprietor or a partnership owner v) Spouse/s of a sole proprietor or partners vi) Foreign workers

Table 3-1 ***Suppliers of insurance/takaful***

Lloyd's	• In 1871, the *Lloyd's Act* created the Corporation of Lloyd's in the UK to provide premises, services and assistance to its Underwriting Members. The capital supplied by investors called Names or Underwriting Members had to be individuals investing in their personal capacity. In January 1994, corporate members were admitted to Lloyd's for the first time. • Both individual and corporate members are grouped into syndicates and each syndicate appoints a managing agent to manage its affairs and this agent appoints professional underwriters on behalf of the syndicate. Unlike corporations with limited liability status, individual Lloyd's Names or Underwriting Members are personally liable to the full extent of their means in respect of that share of the insurance business underwritten on their behalf. Business at Lloyd's must be placed only through Lloyd's broker.
Reinsurance Companies / Retakaful Operators	• An insurer who provides reinsurance cover to a ceding company is called a reinsurer. A reinsurer can be a direct insurer or a professional reinsurer. A professional reinsurer is one who accepts only reinsurance business and does not transact direct business with the insuring public. • Professional reinsurers specialise in general, life/family and a combination of risk management and other insurance support services.

3.2 DISTRIBUTION CHANNELS

3.2.1 DIRECT MARKETING

Throughout the 20th century, business models have continued to evolve in tandem with the higher levels of financial literacy, rising consumer expectations and advancements in technology. As competition compressed margins, there was a migration beyond tied-agency and commission-based distribution models to include fee-based financial advisers and direct marketing.

As an alternative distribution channel, direct marketing mainly caters for personal insurance such as motor vehicle, home contents, personal accident and health. The challenge is in the innovation of products and services, and in ensuring that they are transparent in their dealings with consumers so that customers have ready and easy access to make informed decisions to suit individual needs.

Advantages

- A closer relationship between policyholder and insurer with higher renewal retention.
- More effective management of customer complaints and feedback on customer satisfaction levels.
- More cross-selling opportunities to increase premium growth.

Disadvantages

- High start-up cost in the development of infrastructure and systems in tandem with technological advancement.

- Insurers need to grow and sustain a reasonably large volume of business to justify the initial capital outlay.
- Independent assessment and advice from an expert (insurance broker or financial adviser) is necessary for complex and large risks which entail risk management or financial planning.

3.2.2 INTERMEDIATE CHANNEL

The intermediated channel has enabled a much wider and deeper penetration of insurance in Malaysia, and over the past decade, the number of life policies to the total population increased significantly. In 2011, 67 out of 100 Malaysians had some form of life insurance or family takaful coverage as compared to only 59 out of 100 Malaysians in 2006.

The prominence of the agency force as a delivery channel of choice for the distribution of life insurance business is evidenced from the more than 10% growth in the number of life insurance agents enrolled between 2006 and 2011. Consistent with the increase in the agency force, the expenditure dedicated to maintaining this delivery channel also remained significant, with commissions and agency remunerations consistently accounting for more than 70% of the net investment income of the industry.

The remarkable growth in the life insurance sector can be attributed to the diversification of the distribution system from one largely dominated by the agency force to the introduction of Bancassurance in late 1993 and licensed Financial Advisers in 2005.

a) **Bancassurance** is the collaboration between banks and insurers to distribute insurance products to bank customers. At the end of 2004, Bancassurance had evolved into a primary distribution channel for life insurance, capturing 48% of new life premiums written.
b) **Financial Advisers** form a new category of intermediaries who provide independent financial advisory services. Their services are: insurance, trust funds, wills, investments and other financial services. Financial Advisers represent the customer, can transact with any financial institutions in Malaysia and are remunerated by the financial institution. Financial advisers are qualified by examinations and licensed by Bank Negara Malaysia.

3.2.3 INSURANCE PROFESSIONALS AND ORGANISATION STRUCTURE

Table 3-2 *Insurance professionals*

Actuary	• An actuary is a business professional who analyses the financial consequences of risk. Actuaries use mathematics, statistics, and financial theory to study uncertain future events, especially those of concern to insurance and pension programmes. They possess analytical skills to determine appropriate pricing, the provision of adequate reserves and capital adequacy ratios for insurance companies. • An actuary is a Fellow of one of the professional societies by passing a series of examinations administered by them. The largest of the professional groups is the Society of Actuaries (SOA), the organisation for actuaries working in life and health insurance, employee benefits, and pensions.

Table 3-2 *Insurance professionals*

	• Every licensed insurer in respect of life or general business and takaful operator in respect of family or general takaful business shall appoint an actuary with the prior written approval of Bank Negara Malaysia (section 74 of the *Financial Services Act 2013* and section 83 of the *Islamic Financial Services Act 2013)*.
Risk Surveyor	• A risk surveyor conducts site visits to inspect the physical and moral hazards and performs an evaluation of the overall risk to gather relevant information for the underwriter to charge an appropriate premium in accordance with the risk classification or grade and to ascertain the amount to be retained by the company for its own account and for reinsurance. • There are risk surveyors engaged in aviation and maritime sectors to inspect cargo (pre- and post-loading) and in some instances a marine surveyor can also act as an adjuster of maritime losses to investigate the cause and circumstances of a loss. The risk surveyor also recommends risk improvement measures as a pre-acceptance condition or as a value-added service to the client.
Underwriter	• The underwriter evaluates and selects risks based on the information at hand and decides whether to accept or reject the proposal for insurance. If the risk is accepted, the underwriter decides on the level of premium to be charged and the terms and conditions of the insurance coverage. • Underwriting is more of a science based on experience with premium rating models developed to match risk exposure with the probability or chance of loss. Risk assessment is performed either on a whole account of a large corporation or a portfolio of business such as motor, fire and marine whereby underwriting guidelines are designed to avoid anti-selection by the client against the insurance company.
Reinsurer	• Reinsurance is the sharing or spreading of risk. The ceding company (insurance companies, including Lloyd's and Captives) enters into a reinsurance agreement which details the conditions upon which the reinsurer would pay a share of the claims incurred by the ceding company. • The benefits of reinsurance are: o The direct insurer can issue policies with higher limits than would otherwise be allowed, enabling the insurer to take on more risks by transferring a portion of those risks beyond its own capacity to the reinsurer. o It provides capital to replace large claim pay-outs as a result of losses caused by the accumulation of risks. o It stabilises the direct insurer's financial results caused by severe fluctuations. • A reinsurer has become much more reliant on actuarial models to review the ceding company's financials in conjunction with the experience of the proposed business to be reinsured. The reinsurer also evaluates the competence of underwriters, rates and underwriting guidelines applied by the ceding companies.

Table 3-2 ***Insurance professionals***

<table>
<tr><td>Claims Handler</td><td>The settlement of claims constitutes one of the important functions in an insurance company and the payment of claims may be regarded as the primary service of insurance to the public. Prompt and fair settlement of claims is the hallmark of good service that enhances the reputation and goodwill of the insurance company.
The claims handler performs the following tasks:
Registers and processes payment of claims in accordance with established procedures and regulatory timelines;
Reviews checklists and receipts of relevant documents from claimants;
Provides adequate claim or loss reserves;
Appoints adjusters to conduct an investigation into the cause and circumstances of loss;
Safeguards against leakage and financial loss from fraudulent claims;
Provides relevant feedback on risk improvement measures to underwriters.</td></tr>
<tr><td>Loss Adjuster</td><td>The business of investigating the cause and circumstances of a loss and ascertaining the quantum of the loss in relation to insurance and takaful claims is entrusted to an independent professional called a loss adjuster. Such loss adjusting business must be registered with Bank Negara Malaysia and with the Association of Malaysian Loss Adjusters (AMLA).
The role of the Loss Adjuster is to:
immediately go to the site and make preliminary enquiries on the cause and extent of loss;
report back to the insurer with a ‘preliminary loss advice’ for the purpose of claim registration and creation of a provisional reserve;
check on the adequacy of the sum insured;
take necessary action and/or provide timely advice to prevent aggravated damage;
request relevant documents necessary to substantiate the claim;
submit a full and final report on liability for the insurer’s decision.</td></tr>
<tr><td>Panel of Repair Workshops</td><td>A panel of repairers approved by the General Insurance Association of Malaysia or Persatuan Insurans Am Malaysia (PIAM), also known as the PIAM Approved Repairers Scheme (PARS), was first introduced in 1983. The main objective is to enhance the standard of service, quality and professionalism of workshops involved in the repair of accident vehicles in Malaysia. As at 2012, the scheme operates with 682 workshops nationwide.
The benefits of insurers having their own panel of repair workshops are to:
review performance on a more regular basis;
weed out the bad and reward the good;
attain a better geographical spread to facilitate proximity to claimants across the country;
own better-negotiating powers over the pricing and use of genuine parts to control claim costs;
provide a warranty period (normally up to 6 months) on the parts installed and workmanship after the insured has taken delivery of the vehicle.</td></tr>
</table>

3.2.4 INSURANCE AND TAKAFUL ASSOCIATIONS

(a) ISLAMIC FINANCIAL SERVICES BO

The Islamic Financial Services Board (IFSB), which is based in Kuala Lumpur, was officially inaugurated on 3rd November 2002 and started operations on 10th March 2003. It serves as an international standard-setting body of regulatory and supervisory agencies that have vested interest in ensuring the soundness and stability of the Islamic financial services industry, which is defined broadly to include banking, capital market and insurance. In advancing this mission, the IFSB promotes the development of a prudent and transparent Islamic financial services industry through introducing new, or adapting existing international standards consistent with Shariah principles, and recommend them for adoption.

To this end, the work of the IFSB complements that of the Basel Committee on Banking Supervision, International Organization of Securities Commissions and the International Association of Insurance Supervisors. As at April 2019, the 182 members of the IFSB comprise 79 regulatory and supervisory authorities, 8 international inter-governmental organizations, and 95 market players (financial institutions, professional firms, industry associations and stock exchanges) operating in 57 jurisdictions.

Malaysia, the host country of the IFSB, has enacted a law known as the Islamic Financial Services Board Act 2002, which gives the IFSB the immunities and privileges that are usually granted to international organizations and diplomatic missions.

(b) INTERNATIONAL CENTRE FOR EDUCATION IN ISLAMIC FINANCE (INCEIF)

INCEIF was set up by Bank Negara Malaysia in 2005 and has been mandated to develop and nurture talent and experts in the Islamic financial services industry. As a university, INCEIF offers postgraduate studies in Islamic finance.

INCEIF aims to be the knowledge leader in Islamic finance through providing excellent teaching, research and thought leadership. In achieving this vision, it is important for INCEIF to bridge both academia and industry. This is translated into its academic syllabus which is structured based on the inputs from industry players as well as having faculty members who are globally respected in both Islamic finance academia and Islamic finance industry. The faculty, coupled with continuous support from the regulators and key industry players, provides INCEIF students with strong mentoring relationships and opportunities for professional development.

Today, there are 1,747 INCEIF alumni from over 72 countries around the world. Some are already making meaningful contributions to the advancement of Islamic finance at all levels be it product development, policy framework and implementation; regulation and enforcement; and innovation.

(c) INTERNATIONAL SHARI’AH RESEARCH ACADEMY FRO ISLAMIC FIANACE

ISRA has been established to promote applied research in the area of Sharî’ah and Islamic finance. It also acts as a repository of knowledge for Sharî’ah views (fatwas) and undertake studies on contemporary issues in the Islamic financial industry. ISRA contributes to strengthening human capital development in Sharî’ah expertise relevant to Islamic finance and provides a platform for greater engagement amongst practitioners, scholars, regulators and academicians via research and dialogue, in both the domestic and international arenas. Through pioneering research and rigorous intellectual dialogue, ISRA aims to promote innovation and dynamism and thus extend the boundaries of Islamic finance. It is envisioned that with greater research and dialogue, mutual respect and recognition will emerge within the global community of the Islamic financial industry. As a part of the International Centre for Education in Islamic Finance (INCEIF), ISRA is able to leverage on its infrastructure and facilities as well as to tap on the knowledge, expertise and resources of its academic faculty and postgraduate students. To provide input and assistance in the strategic direction of ISRA’s research, the Council of Scholars, a group comprised of eminent local and international Sharî’ah scholars, has been set up.

(d) CHARTERED INSTITUTE OF ISLAMIC PROFESSIONALS

CIIF was established in 2015 as a professional body for Islamic finance practitioners to support the capacity building agenda of the industry by setting professional standards to drive the next phase of Islamic finance human capital development.

In setting professional standards, the CIIF aims to support its members towards the continuous pursuit and development of cutting-edge knowledge in Islamic finance; upholding the highest levels of integrity in discharging their professional duties; and providing distinguished quality service in the execution of their professional duties.

It was formerly known as the Association of Chartered Islamic Finance Professionals (ACIFP), which was established in 2008. The ACIFP was specifically mentioned in the Bank Negara Malaysia (BNM) Financial Sector Blueprint 2011 - 2020, under Recommendation 5.3.2 as the "professional body responsible for global quality standards for Islamic Finance Professionals".

3.2.4 INSURANCE AND TAKAFUL ASSOCIATIONS

PERSATUAN INSURANS AM MALAYSIA (PIAM)

The association of licensed general insurers, including reinsurers, in Malaysia is Persatuan Insurans Am Malaysia (PIAM), which was formed in May 1979 in compliance with Section 3(2) of the *Insurance Act 1963* (replaced by Section 22 of the *Insurance Act 1996*).

A general insurance agent, whether individual or corporate, must register with PIAM after passing the Pre-Contract Examination for Insurance Agents (PCEIA) conducted by the Malaysian Insurance Institute through any two general insurance companies as Principal(s).

Key Objectives

- To promote sound insurance structure in Malaysia.
- To promote and represent the interests of members and render possible advice or assistance as may be deemed necessary and expedient.
- To circulate information likely to be of interest to members and to collect, collate and publish statistics and any other relevant information relating to general insurance.
- To work in conjunction with any legal body or any chamber or committee or commission appointed or to be appointed for consideration, framing, amendment or alteration of any law relating to insurance.
- To organise and manage arrangements and matters of common interest, concern or benefit to members or any group of members and to collect and manage funds for the same.
- To make rules, regulations and bye-laws in accordance with these articles in consultation with Bank Negara Malaysia.

LIFE INSURANCE ASSOCIATION OF MALAYSIA (LIAM)

Persatuan Insurans Hayat Malaysia
Life Insurance Association of Malaysia

The Life Insurance Association of Malaysia (LIAM) is a trade association registered in 1974 under the *Societies Act 1966* to form an association of licensed life insurers, including life reinsurers.

A life insurance agent must register with LIAM after having passed the Pre-Contract Examination for Insurance Agents (PCEIA) conducted by the Malaysian Insurance Institute through any one life insurance company as Principal.

Key Objectives

- To promote public understanding and appreciation for life insurance.
- To improve the image of the life insurance industry through self-regulation.
- To give support to the regulatory authorities in developing a strong and healthy industry.
- To enhance the professionalism of staff and agents through continuous training and education.
- To liaise and work with local and foreign life insurance organisations towards achieving common objectives and benefits.

MALAYSIAN TAKAFUL ASSOCIATION (MTA)

MTA is a trade body recognised as providing leadership on issues bearing on the takaful industry's collective strength and is dedicated to promoting the interest of its members and to supervising the exercise of self-regulation.

An Inter-Takaful Operator Agreement (ITA) was officially signed on 22 May 2008 to set a common standard to self-regulate and control matters related to the Pre-Contract Examination for Agents, the agency registration system and code of ethics, and the compliance with the general takaful tariff for motor and fire business. This is to streamline takaful market practice with that of conventional insurance, to strengthen the industry. A takaful agent must register with MTA after passing the Takaful Basic Examination (TBE) conducted by the Islamic Banking and Finance Institute Malaysia (IBFIM) through any licensed Takaful Operator (TO) as principal.

INSURANCE SERVICES MALAYSIA (ISM)

ISM was conceptualised in 1998 by PIAM as the Malaysian Insurance Rating Organisation (MIRO) to put in place databases to support pricing and reserving in a liberalised pricing environment. The project took shape in 2000 when PIAM established the MIRO department and over the years expanded its services and membership to takaful operators in 2003 and life insurers in 2004.

In 2005, ISM was incorporated as a company limited by guarantee with strategic objectives to build competencies in quantitative underwriting and technical pricing, and to increase efficiencies in operations by:

- Providing online access to shared information.
- The utilisation of information technology solutions.
- Providing effective fraud detection systems and capabilities.

Table 3-3 *Categories of services rendered to the insurance industry by ISM*

BUSINESS INTELLIGENCE	INFORMATION TECHNOLOGY	FRAUD PREVENTION
Databank	Central NCD System	
Insurance Statistics	Takaful Agency System	Claims Verification System
Automotive Business Intelligence	Circular Distribution System	

NATIONAL INSURANCE ASSOCIATION OF MALAYSIA (NIAM)

The National Insurance Association of Malaysia[5] (NIAM) or Persatuan Insurans Kebangsaan Malaysia was established in 1973 and registered under the *Societies Act 1966*.

Key Objectives

- To promote and safeguard the interests of members in all their activities.
- To facilitate joint action by members in respect of any matters that may affect a member.
- To promote or undertake any project which will enhance the standing and reputation of its members in society.
- To secure and support the promotion of Bills in Parliament which will protect the interests of or be advantageous to its members.

THE MALAYSIAN INSURANCE AND TAKAFUL BROKERS ASSOCIATION (MITBA)

MITBA

The Malaysian Insurance and Takaful Brokers Association[6] (MITBA), previously known as the Insurance Brokers Association of Malaysia (IBAM), is the only national body of insurance and takaful brokers. MITBA was registered with the Registrar of Societies on 3 December, 1974 and is the collective voice of the industry, advising members, the regulator, consumers, trade association and other stakeholders on key insurance issues.

Key Objectives

- To elevate the status, safeguard and advance the interest of its members as insurance brokers.
- To procure general efficiency and proper professional conduct of its members.
- To ensure that employees of insurance brokers are professionally qualified, conversant with insurance laws and practices and acquainted with current developments as they affect insurance brokers in particular and the insurance industry in general.

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[5] Website: http://www.niam.org.my
[6] Website: http://www.mitba.org.my

- To provide a platform for the promotion of discipline, professional conduct and etiquette.
- To promote the healthy growth of the insurance industry in line with national objectives.

ASSOCIATION OF MALAYSIAN LOSS ADJUSTERS (AMLA)

PERSATUAN PENYELARAS KERUGIAN MALAYSIA (1981)
ASSOCIATION OF MALAYSIAN LOSS ADJUSTERS (1981)

AMLA is the approved association of loss adjusters established in 1981 by Bank Negara Malaysia. Its members comprise registered adjusters.

Key Objectives

- To register licensed insurance adjusters and to regulate their practice of loss adjusting in Malaysia.
- To promote, develop and establish a sound loss adjusting profession in Malaysia.
- To cooperate with other similar associations in other parts of the world.
- To liaise, cooperate or affiliate with other insurance professional organisations in Malaysia.
- To represent its members in matters affecting their interests in the insurance industry.
- To circulate information likely to be of interest to members and to collate and publish statistics and any other relevant information relating to loss-adjusting.
- To work in conjunction with any legal body or association for the amendment or alteration of any laws relating to loss adjusting.

NATIONAL ASSOCIATION OF MALAYSIAN LIFE INSURANCE FIELD FORCE AND ADVISERS (NAMLIFA)

NAMLIFA was set up in 1978 as an association for life insurance and takaful agents and their supervisors. Its objective is to elevate the economic wellbeing, status and professionalism of life insurance professionals and financial practitioners, and to promote training and education to upgrade professional capability through relevant programmes and collaboration with similar organisations. As per 2012 figures, the number of NAMLIFA members stood at 7694.

MALAYSIAN FINANCIAL PLANNING COUNCIL (MFPC)

The Malaysian Financial Planning Council (MFPC) comprises office bearers elected by its members to provide leadership and direction. MFPC is a self-regulatory body to promote financial literacy and enhance the profession of Financial Planners through education and training.

The Registered Financial Planner (RFP) programme introduced by MFPC was launched by Bank Negara Malaysia (BNM) in November 2002. The RFP qualification signifies the twin pillars of professionalism in financial planning – Professional Education and Practice Excellence. The RFP and the Shariah RFP programmes are recognised by BNM and the Securities Commission as pre-requisite for the Financial Adviser's Licence and the Capital Market Services Representative Licence respectively.

In addition, MFPC has also established Best Practice Standards and the Code of Ethics for Financial Planners, which are continually reviewed and updated in line with changes in the legal and regulatory framework.

Key Objectives

- To certify financial planners and uplift their professionalism.
- To enhance the image of the financial planning profession.
- To set practice standards.
- To provide self-regulation in the financial planning industry.

NATIONAL INSURANCE & TAKAFUL CLAIMS SOCIETY (NICS)

nics
national insurance & takaful claims society

NICS was formed to develop best practices relating to the insurance claims processes of member companies and give greater recognition to the services of claims personnel. NICS has become an effective forum for members to exchange information and provide a platform for networking in the following areas:

- Best practices in claims handling and process.
- Fraud alert.
- Training in claims management.
- Empowering and award of recognition to claims personnel.

It was commissioned to conduct a comprehensive study on third-party bodily injury (TPBI) claims fraud in Malaysia. The aim of the project is to produce accurate information for insurers, intermediaries and supervisors so that the potential risk of fraud in the area of TPBI motor insurance claims can be identified and reduced as much as possible through the implementation of effective strategies to prevent, detect and remedy such frauds against insurers.

MALAYSIAN ASSOCIATION OF RISK AND INSURANCE MANAGEMENT (MARIM)

MARIM is a non-profit trade organisation which represents large corporations, public utility companies, and small and medium-sized industries. It is governed by an executive committee elected by its members and is dedicated to promoting, and raising awareness and standards of risk management in Malaysia.

Key Objectives

- Promote and foster the practice of Risk Management.
- Promote education and certification in risk and insurance.
- Provide a forum for the exchange of views and experience of those engaged in risk management.
- Provide consultancy to authorities/regulatory bodies in the areas of risk management.
- Cooperate with regulatory bodies, government agencies, industries, related associations, media and other stakeholders.
- Encourage and cultivate active engagement with members and chapters.
- Become a primary resource centre for risk management.

FIRE PROTECTION ASSOCIATION OF MALAYSIA BERHAD (FPAM)

FPAM is an independent non-profit organisation comprising a management council elected by members to govern the association. The council meets once a month at the office of the General Insurance Association of Malaysia at Wisma PIAM to make decisions on its operations and activities.

Key Objectives

- To improve the method of protection of persons and property on land, sea or air primarily against the risk of fire.
- To disseminate advice for the protection against, and the prevention of fire and related risks and publish information on these matters.
- To formulate problems of protection and prevention against fire and other risks, such as research, and to cooperate in research and to investigate the causes and spread of fire.
- To undertake propagation to the public of such knowledge as may be considered desirable in connection with the objectives of the Association.
- To exchange information and cooperate with other bodies or persons, and to institute or receive enquiries in connection with the objective of the Association.

3.2.5 PROFESSIONAL AND EDUCATIONAL ASSOCIATIONS

ACTUARIAL SOCIETY OF MALAYSIA (ASM)

ASM was founded in 1978 under the *Societies Act 1966* as the representative body for the actuarial profession in Malaysia to provide a platform for members of the actuarial profession to raise and discuss technical and public interest issues related to the practice of the profession.

Its primary objective is to promote study and research into actuarial subjects and allied aspects of life insurance, employee retirement benefits, finance and investment, and to give educational support to students taking up actuarial studies and professional development to qualified actuaries.

In 2003, ASM became a Full Member Association of the International Actuarial Association, and is committed to working towards becoming a full-fledged professional body with a recognised examination and accreditation system.

THE MALAYSIAN INSURANCE INSTITUTE (MII)

THE MALAYSIAN INSURANCE INSTITUTE

Founded in 1968 as a non-profit organisation, the Malaysian Insurance Institute[7] (MII) is a leading regional insurance education and training institution providing a professional qualification in insurance, risk management and financial planning.

Board members of the MII are represented by the chairpersons of the various insurance associations, namely PIAM, LIAM, MITBA and AMLA, including a representative from the regulatory authority, Bank Negara Malaysia. Other members appointed to the Board are industry leaders, including CEOs of insurance companies.

As the premier professional insurance education and training provider in Malaysia, MII works closely with insurance practitioners and BNM to ensure that the education and training programmes are relevant and in alignment with the ever-changing needs of the insurance industry.

[7] Website: http://insurance.com.my

ASIAN INSTITUTE OF FINANCE (AIF)

AIF
ASIAN INSTITUTE OF FINANCE

Established by the Central Bank of Malaysia (Bank Negara Malaysia) and the Securities Commission of Malaysia, the Asian Institute of Finance (AIF) focuses on developing human capital across the financial services industry in Asia.

FINANCE ACCREDITATION AGENCY (FAA)

FAA Finance Accreditation Agency

The Finance Accreditation Agency[8] (FAA) was formed as a division within the Asian Institute of Finance (AIF) to review the quality of programmes being offered by AIF-affiliated institutes. FAA is now an independent quality assurance and accreditation body for the Financial Services Industry (FSI).

FAA contributes to quality assurance initiatives within the FSI through intellectual engagement and in partnership with relevant stakeholders, including programme accreditation, institutional audits and programme evaluation.

FAA deploys its FAA Quality Framework (FQF) as the foundation for quality assurance and accreditation of adult learning as well as the point of reference for the criteria and requirements for qualifications in the FSI.

While the Malaysian Qualifications Agency (MQA) is responsible for monitoring and overseeing the quality assurance practices and accreditation of national higher education (academic programmes), FAA provides high-quality assurance practices and accreditation of professional learning programmes and qualification in FSI. This may include academic programmes related to Islamic Finance which seek professional recognition.

[8] Website: http://www.faa.org.my

IBFIM

IBFIM[9] is an industry-owned institute whose objective is to serve the needs of the Islamic finance industry stakeholders in talent and business development.

Since 2001, IBFIM has been conducting training programmes as well as extending business and *Shariah* advisory services. IBFIM's tagline, "Your Islamic Finance Business Partner" manifests its close rapport with the industry and its wide range of services.

As a market leader, IBFIM's certification programmes are developed, moderated and recognised by the industry. The programmes cover four disciplines: banking, Takaful, capital market and wealth management. IBFIM's Islamic Finance Qualifications are mapped out in an innovative Progression Route, to motivate industry personnel to enhance their competencies in moving up the corporate ladder.

[9] Website: http://www.ibfim.com

4

CHAPTER 4 LEGISLATION AND CONSUMER PROTECTON

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CHAPTER OBJECTIVE

To understand the legislation governing insurance & takaful and the insurance & takaful business in Malaysia

LEARNING OBJECTIVES

After you complete this chapter, you should be able to:

- *Outline the main functions of the Central Bank as the financial services regulator.*
- *Understand the need for insurance and takaful regulations and the main provisions of the Financial Services Act 2013 and IFSA.*
- *Describe the main provisions of the Anti-Money Laundering Regulations.*
- *Explain the need for security and the requirements for confidentiality of information, its use, storage and disclosure.*
- *Appreciate the role of the Malaysia Competition Commission (MyCC).*
- *Comprehend the existing complaints-handling procedures and the role of the Ombudsman for Financial Services (OFS) [formerly known as the Financial Mediation Bureau (FMB)].*

4.1 INSURANCE LEGISLATION

4.1.1 THE ROLE OF GOVERNMENT SUPERVISION

The government has played a major role in the activities of the financial services industry. More often, supervision has taken the form of legislation. In the past, direct intervention has been necessary to manage risk to financial stability and to promote the safety of financial institutions.

The powers and functions of the Central Bank of Malaysia or Bank Negara Malaysia are provided for under the *Central Bank of Malaysia Act 2009* and the *Financial Services Act 2013* to take on the role of supervisory authority with the following regulatory objectives:

a) To foster fair, responsible and professional business conduct of financial institutions; and
b) To strive to protect the rights and interests of consumers of financial services and products.

BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

The role of the Central Bank is to:

- keep a close watch on the solvency and market conduct to enhance professional standards and consumer confidence in the insurance industry; and
- promote monetary and financial stability conducive to the sustainable growth of the economy.

4.1.2 HISTORICAL DEVELOPMENT

In Malaysia, regulation of insurance business was achieved through the administration and enforcement of the *Insurance Act 1996* (which replaced the *Insurance Act 1963* effective 1st January 1997). The Act was supplemented by insurance regulations which prescribed the details of mandatory requirements contained in certain provisions of the Act and more importantly, it empowered Bank Negara Malaysia to specify matters pursuant to the provisions of the Act.

The *Insurance Act 1996* raised the solvency margin (surplus of assets over liabilities) from RM5 million under the *Insurance Act 1963* to RM50 million for each class of business (life and general), in line with the increase in the minimum capital requirement. In 2003, the minimum paid–up share capital was increased to RM100 million for all direct insurers (excluding reinsurers).

In 2005, the *Insurance Act 1996* was amended for the first time to put in place the legislative licensing framework for Financial Advisers by setting out the form of establishment (minimum capital requirements and licensing fees) and the type of activities that could be undertaken by them.

4.1.3 RISK-BASED CAPITAL FRAMEWORK

Effective 1st January 2009, as a licensing condition for insurers, the Minister of Finance imposed the Risk-Based Capital (RBC) Framework to determine the Capital Adequacy Ratio (CAR). The framework was formulated to conform to international trends towards risk-based capital frameworks (e.g. Solvency II and Basel II). Its aim is to better reflect the risk profiles of insurers. The framework applies to all insurers including reinsurers licensed under the Act, for business generated from within and outside Malaysia.

Under the framework, each insurer is required to determine the adequacy of the capital available in both its insurance and shareholders' funds. The capital adequacy ratio formula adopted under this framework preserves the fundamental principle that the valuation surplus of the participating life insurance fund should not be used to support the capital requirements of other insurance or shareholders' funds, to ensure that capital is available to protect policyholders.

The formula applied is:

$$Capital\ Adequacy\ Ratio\ (CAR) = \frac{Total\ Capital\ Available\ (TCA)}{Total\ Capital\ Required\ (TCR)} \times 100\%$$

The Central Bank has set a Supervisory Target Capital Level of 130 percent. Each insurer must set its own Individual Target Capital Level to reflect its own risk profile. The Individual Target Capital Level must be higher than the Supervisory Target Capital Level.

4.1.4 SUPERVISION OF INSURANCE AND TAKAFUL

NEW LEGISLATIONS

With the enactment of the *Financial Services Act 2013* (FSA) and the *Islamic Financial Services Act 2013* (IFSA), the regulation and supervision of financial institutions, payment systems and other relevant entities, and the oversight of the money market and foreign exchange market has been placed under a single legislative framework.

The FSA amalgamates several separate laws in respect of conventional financial services while the IFSA replaces the *Islamic Banking Act 1983* and the T*akaful Act 1984* accordingly.

REPEAL OF THE INSURANCE ACT 1996 AND THE TAKAFUL ACT 1984

The FSA replaces four existing Acts:

a) Banking and Financial Institutions Act 1989 (BAFIA)
b) Exchange Control Act 1953
c) Insurance Act 1996
d) Payment Systems Act 2003

IFSA replaces two existing Acts:

a) Islamic Banking Act 1983
b) Takaful Act 1984

PURPOSE OF THE NEW LAWS

a) Greater clarity and transparency in administration

This includes clearly defined regulatory objectives and accountability of Bank Negara Malaysia in pursuing its principal object to safeguard financial stability, transparent triggers and transparent assessment criteria for authorising institutions to carry on regulated financial business, and for shareholder suitability.

b) Clear focus on Shariah compliance and governance

IFSA provides a comprehensive legal framework that is fully consistent with the *Shariah* in all aspects of regulation and supervision, from licensing to the winding-up of an institution.

c) Provisions for differentiated regulatory requirements

These reflect the nature of financial intermediation activities and their risks to the overall financial system.

d) Provisions to regulate financial holding companies and non-regulated entities

These provisions were formed to take account of the systemic risks that can emerge from the interaction between regulated and unregulated institutions, activities and markets. The Minister of Finance may subject an institution that engages in financial intermediation activities to ongoing regulation and supervision by Bank Negara Malaysia if it poses or is likely to pose a risk to overall financial stability.

e) Strengthened business conduct and consumer protection requirements

These were formulated to promote consumer confidence in the use of financial services and products.

f) Strengthened provisions for effective and early enforcement and supervisory intervention

Bank Negara Malaysia has the ability to obtain information necessary for its supervisory purposes and can take a wide range of supervisory intervention actions at early stages to avert potential problems and impose penalties for non-compliance with regulatory and legal requirements.

4.1.5 FINANCIAL SERVICES ACT 2013 (FSA)

The relevant provisions of the *Financial Services Act 2013* (FSA) which came into force effective 30 June 2013 are summarised below:

Table 4-1 ***Provisions of the Financial Services Act 2013 (FSA)***

Section	The Law	Provision
10	Grant of Licence By Minister	Authorised business includes insurance business, insurance broking or financial advisory business
11 (3)	Approval by the Central Bank	Insurance broking or financial advisory business shall at all times have in force a professional indemnity insurance or takaful of such amount as may be specified
16 (1)	Licensed insurer to carry on Life *or* General Business	Licensed insurer other than a licensed professional reinsurer shall not carry on both life business and general business
17	Registered Business	Only a registered person can carry on registered business as a registered adjuster other than an advocate or solicitor, an aviation or maritime loss adjuster or an employee of a licensed insurer or takaful who in the course of his employment acts or assists in adjusting insurance claims
126	Financial Ombudsman Scheme	Ensures a fair, accessible and effective way of handling complaints and resolution of disputes in connection with financial services or products
127	Obtaining insurance outside Malaysia	No person shall enter into or cause to be entered into a contract of general insurance or takaful outside Malaysia without the prior written approval of Bank Negara Malaysia
128	Provisions relating to Policies	Schedule 8 sets out the provisions relating to life insurance policies

Table 4-1 *Provisions of the Financial Services Act 2013 (FSA)*

Section	The Law	Provision
129	Pre-Contractual Duty of Disclosure and Representations & Remedies for Misrepresentation	Schedule 9 (Part 2) sets out the duty of disclosure for insurance contracts other than consumer insurance contracts. Part 3 sets out on the non-contestability and remedies for misrepresentations
130	Payment of policy money under life and personal accident policy	Schedule 10 sets out the provisions relating to payment of policy money upon the death of a policy owner under a life policy including a life policy under section 23 of the *Civil Law Act 1956* and a personal accident policy effected by him upon his own life.
275	Savings & Transitional Provisions	(a) subsections 147(4) & (5) and sections 150 & 151 (b) sections 144 & 224 of the repealed *Insurance Act 1996* shall continue to remain in full force until such date to be appointed for the coming into operation of section 129 and schedule 9 of the FSA
276	Conversion to single insurance business	Composite insurers shall comply with subsection *16(1)* within five years, or such longer period as may be specified by the Minister, of the appointed date of the law

4.1.6 ISLAMIC FINANCIAL SERVICES ACT 2013 (IFSA)

The relevant and salient provisions/requirements of the *Islamic Financial Services Act 2013* (IFSA) which came into force effective 30 June 2013 are summarised below:

Table 4-2 *Provisions of the Islamic Financial Services Act 2013 (IFSA)*

Section	The Law	Provision
7	Powers and functions of Bank	The role, function and power of Bank Negara Malaysia have been expanded under the IFSA which Bank Negara Malaysia now has the power to issue directions to institutions including Takaful operators
10	Grant of Licence By Minister	Grant a licence to the applicant to carry on takaful business or international takaful business
11 (3)	Approval by the Central Bank	Takaful broking or Islamic financial advisory business shall at all times have in force a professional indemnity insurance or takaful of such amount as may be specified
16 (1)	Licensed takaful operator to carry on family takaful or general takaful business	A licensed takaful operator, other than a licensed professional retakaful operator, shall not carry on both family takaful business and general takaful business. The IFSA requires a Takaful operator (other than a professional retakaful operator) with a composite license to separate its Family business from its General Takaful business
29 (2)	Power of bank to specify standards on Shariah matters	Provides that Shariah Governance Framework (SGF) issued by Bank Negara Malaysia becomes a standard that shall be complied with by all Islamic Financial Institutions to ensure all their operations and business activities are in accordance with the Shariah.
138 (1)	Financial Ombudsman Scheme	Ensures effective and fair handling of complaints and for the resolution of disputes in connection with financial services or products

Table 4-2 ***Provisions of the Islamic Financial Services Act 2013 (IFSA)***

Section	The Law	Provision
139	Obtaining general takaful outside Malaysia	The prior written approval of Bank Negara Malaysia must be obtained for property or liability to be insured, with an insurer outside Malaysia
140	Provisions relating to takaful certificates	Schedule 8 sets out provisions relating to takaful certificates.
142	Payment of takaful benefits under family takaful certificate and personal accident takaful certificate	Schedule 10 sets out provisions for the payment of takaful benefits upon the death of a takaful participant under a family takaful certificate, and a personal accident takaful certificate, issued in respect of a contract of takaful entered into by the takaful participant upon his life
151	Restriction on use of certain words	Use of certain words (e.g. bank, insurance, takaful) capable of being construed as indicating the carrying on of businesses which are regulated under the IFSA is not allowed, except with the prior written approval of Bank Negara Malaysia

4.1.7 COMPANIES ACT 2016

The *Companies Act 2016* regulates the formation, registration, incorporation, management and dissolution of companies in Malaysia. The Companies Commission of Malaysia (CCM) or Suruhanjaya Syarikat Malaysia (SSM) is a corporate registry and regulatory authority that meets business needs through registration, information, regulation and advice.

There are two types of companies, namely:

a) An **unlimited company** – An unlimited company is incorporated in the same way as a company limited by shares. However, the difference is that for an unlimited company, the liability of its members must be stated in the Memorandum of Association as *'unlimited'*.
b) A **company limited by shares** – A company limited by shares is a company formed on the principle of having the liability of its members limited by the memorandum to the amount, (if any, unpaid) on the shares respectively held by them. A company limited by shares may be incorporated as:
   i) a **private company** (identified through the words 'Sendirian Berhad' or 'Sdn. Bhd.' appearing together with the company's name); or
   ii) a **public company** (word 'Berhad' or 'Bhd' appearing together with the company's name).

Insurance companies and takaful operators are required to be incorporated as a *public company*, whereas insurance brokers, financial advisers and registered adjusters are required to be incorporated as a *private company*. In the event of a conflict between the provisions of the *Financial Services Act 2013* and the *Companies Act 2016*, the provisions of the *Financial Services Act 2013* will prevail.

MAIN PROVISIONS OF THE COMPANIES ACT 2016

Annual returns

Profit and loss account (after provision for income tax), balance sheet and directors' report showing the state of the company's affairs as at the end of the financial year; and if the company is a holding company, a report in respect of the state of affairs of the holding company and all its subsidiaries.

Statutory report

Shares allotted and to the cash received in respect of those shares and to the receipts and payments on capital account to be examined and reported upon by the auditors.

Dissolution of a company

Where assets of a company are collected and realised, the proceeds collected are used to discharge the company's debts and liabilities and the remaining balance (if any) will be distributed amongst the contributors according to their entitlement.

For the winding up of an insurance company, the prior written approval of Bank Negara Malaysia is required in accordance with Section 165 of the FSA. Once it is obtained, the company must file an application to the High Court. The Court will then appoint a liquidator.

4.1.8 MALAYSIA DEPOSIT INSURANCE CORPORATION ACT 2011

PIDM

Perbadanan Insurans Deposit Malaysia (PIDM) is a statutory body established under the *Malaysia Deposit Insurance Corporation Act 2005* to administer the national deposit insurance system aimed at protecting depositors in commercial and Islamic banks.

The Act was later expanded by the Parliament to administer the **Takaful and Insurance Benefits Protection System (TIPS)** effective 31 December 2010 under the new *Malaysia Deposit Insurance Corporation Act 2011* to replace the Insurance Guarantee Scheme Fund (IGSF) for life and general insurance business.

4.1.9 WORKMEN'S COMPENSATION ACT 1952

With effect from 1 July 1992, Malaysian workers are no longer covered under the Workmen's Compensation Act 1952. They are to be covered under the Employees' Social Security Act 1969. However, the Act only covers Malaysian workers whose monthly wages do not exceed RM 3,000 and whose age is below 60 years. It does not cover government employees, domestic servants and self-employed persons.

Under the *Workmen's Compensation (Foreign Worker's Scheme) Order 1993*, it is mandatory for employers of foreign workers to insure all manual workers regardless of the amount of wages and others (non-manual workers) earning not more than RM 500 per month.

4.1.10 ROAD TRANSPORT ACT 1987

The primary source of law affecting motorists in Malaysia is the *Road Transport Act 1987*. Compulsory motor insurance is provided under Section 90 of the Act to ensure that all persons using a motor vehicle on road are capable of compensating victims of road accidents for physical injury or death.

Liability to passengers 'arising out of and in the course of employment' and liability to 'gratuitous' passengers (other passengers being carried for hire or reward) are not mandatory by law.

4.1.11 ANTI-MONEY LAUNDERING & ANTI-TERRORISM FINANCING ACT 2001 (AMENDED – 2003)

The *Anti-Money Laundering Act 2001* came into operation on 15 January 2002 and it was further amended to include Anti-Terrorism Financing in December 2003.

Money laundering is the process by which criminals convert money and/or properties derived from illegal means to make it legal. It includes a person who:

a) engages directly or indirectly in a transaction that involves the proceeds of any unlawful activity;
b) acquires, receives, possesses, disguises, transfers, converts, exchanges, carries, disposes of, uses, removes from or brings into Malaysia proceeds of any unlawful activity; or
c) conceals, disguises or impedes the establishment of the true nature, origin, location, movement, disposition, the title of, rights with respect to, or ownership of, proceeds of any unlawful activity where:
    i) the person knows or has reasons to believe that the property proceeds from any unlawful activity;
    ii) the person without reasonable excuse fails to take reasonable steps to ascertain whether or not the property proceeds from any unlawful activity.

There are three stages in money laundering:

1) **Placement** – physical disposal of proceeds derived from illegal activities;
2) **Layering** – separating the illicit proceeds from their sources through transactions that disguise the audit trail and provide anonymity; or
3) **Integration** – integrating the laundered proceeds into the economy as normal funds.

Some of the major sources involving illegal proceeds include drug trafficking, corruption, smuggling and fraud, forgery and cheating. Most of these activities are done through the banking system either using a nominee or family member, setting up front companies including the use of money changers and cash transactions to conceal the money trail.

To combat money laundering and financing of terrorism, two key initiatives have been taken. They are:

1) The obligation to report by financial institutions on suspicious transactions;
2) Freeze, seize and forfeit the proceeds derived from money laundering activities.

Roles and Responsibilities of Insurers

To comply with this Act, insurers must do risk profiling which includes the following:

a) To create a risk profile of a particular type of customer, which must include at least the following factors:
    i) the origin of the customer and the location of business;
    ii) the background or profile of the customer;
    iii) the nature of the customer's business;
    iv) the structure of ownership for a corporate customer; and
    v) any other information suggesting that the customer is at high risk.
b) To monitor continuously and regularly each customer's transaction, activity pattern and make sure it is in line with the customer's initial profile.
c) To reassess the profile when there are changes in their employment or nature of the business or any unreasonable differences.

The guidelines focus on actions that could alert the reporting institutions on deterring and detecting any money laundering activities; and to freeze, seize and forfeit proceeds derived from money laundering activities.

In executing its roles and responsibilities, an insurer must always sight the relevant documentation and details of customers, including verifying details against the original documents for policies with an annual insurance premium exceeding RM 50,000 under individual policies and RM 100, 000 for group policies.

Insurers should not commence any business relations or perform any transaction whenever a customer fails to comply with the requirements of the customer due diligence, and if it is an existing customer, the insurer should terminate the policy and lodge a Suspicious Transaction Report (STR) with the Financial Intelligence Unit in Bank Negara Malaysia.

4.1.12 COMPETITION ACT 2010

The *Competition Act 2010* came into force on 1 January 2012.

- Section 4 of the Act prohibits anti-competitive agreement**s** between enterprises, namely agreements which have the objective or the effect of significantly preventing, restricting or distorting competition in any market for goods or services (Chapter 1 Anti-competitive agreement); whereas
- Section 10 of the Act prohibits any abuse of an enterprise's dominant position in any market (Chapter 2 Abuse of dominant position).

The Act provides for avenues of relief against anti-competitive agreements. The Malaysia Competition Commission (MyCC), the body created by the *Competition Commission Act 2010*, is empowered to implement and enforce the Act. MyCC's Guidelines on Chapter 1 Prohibition states that this relief can be granted independently through:

a) The individual exemption under Section 6 of the Act; or
b) Block exemption under Section 8 of the Act; or
c) Invoking Section 5 of the Act.

The Act was drafted on a "broad-brush" approach. It did not cater for or take into account the specific nature and requirements of the various markets and industries that form the Malaysian economy. For example, the economic, social and technical factors relating to the financial services industry are different from that of the wholesale flower market.

Relief through individual and block exemptions is provided by the Act to cater for the specific requirements and factors of a particular market or industry. Agreements between parties in the market, either horizontal or vertical, may on the face of it be anti-competitive in order to achieve the necessary social benefits and efficiencies.

4.1.13 PERSONAL DATA PROTECTION ACT 2010

The *Personal Data Protection Act 2010* (PDPA) is an Act passed by the Malaysian government which came into force in November 2013 to regulate the processing of personal data in a commercial transaction.

PDPA applies to:

- Any person who processes or authorises the processing of any personal data in respect of commercial transactions;
- Personal data processed in Malaysia;
- Uses of equipment in Malaysia for processing personal data.

The purpose of PDPA is to:

- Protect personal data belonging to the public from being misused through commercial transactions;
- Protect sensitive data from being misused;
- Facilitate international trade;
- Protect consumer rights.

What is Personal Data?

Personal Data is:

- Any personal information in respect of commercial transactions;
- Any data that relates directly or indirectly to a data subject;
- Sensitive personal data e.g. physical or mental health, political opinions, religious beliefs, offences or any other data as the Minister may determine;
- Expression of opinion about the data subject.

Seven Principles of the Personal Data Protection Act 2010 (PDPA)

Table 4-3 ***Principles of the Personal Data Protection Act 2010***

1) General	**Personal data shall be processed if:** • the data subject has given consent • the processing is necessary for or directly related to that purpose • it is adequate and not excessive in relation to that purpose **Sensitive data shall be processed if:** • the data subject has given explicit consent • processing is necessary for employment, vital interest, medical, legal, administration of justice and others where Minister thinks fit • Information has been made public by the data subject

2) Notice and Choice	**Data subjects should be informed by written notice on:**
	• their personal data is being processed and a description of the personal data is provided
	• the purpose of the collection
	• the source of the personal data
	• their rights to:
	    ○ request access and correct
	    ○ contact the data user for enquiries and complaint
	    ○ be informed of the third parties to whom the data user discloses or may disclose the personal data
	    ○ limit the choices and means of processing personal data.
	Whether it is obligatory or voluntary for the data subject to supply the personal data:
	NOTICE shall be given soonest possible:
	• At the time the data subject is first asked by the data user to provide his personal data
	• At the time the data user first collect the personal data
	• Before data user uses the personal data or discloses to a 3rd party
	NOTICE shall be given in national and English language.

3) Disclosure	**No PERSONAL DATA shall be disclosed without the consent of data subject:** • for any other purpose(s) other than the purpose(s) it was collected, or a purpose directly related to the purpose the data was collected • to any other party

Table 4-3 ***Principles of the Personal Data Protection Act 2010***

4) Security	**A DATA USER needs to take practical steps to protect the personal data from any:** • Loss • Misuse • Modification • Unauthorised or accidental disclosure • Alteration or destruction **Need to consider the following:** • The nature of personal data • The harm that would result from such misconduct • The place or location where the personal data is stored • The security measures to ensure reliability and integrity • Measures taken to ensure the secure transfer of the personal data
5) Retention	• The personal data processed shall *not* be kept longer than necessary for the fulfilment of the purpose. • The data user must take all reasonable steps to ensure that all personal data is destroyed or permanently deleted if it is no longer required for the purpose for which it was processed.
6) Data integrity	**Data user shall take reasonable steps to ensure that the personal data is:** • Accurate • Complete • Not misleading • Kept up-to-date by having regard to the purpose of the data
7) Access	**A Data Subject shall be given their rights and access to:** • their personal data, and • the ability to correct that personal data if it is: o Inaccurate o Incomplete o Misleading o Not up-to-date

4.2 FINANCIAL CONSUMER LITERACY AND EDUCATION

4.2.1 INSURANCEINFO

The Consumer Education Programme (CEP) on insurance and takaful is known as *InsuranceInfo* and is a joint effort between Bank Negara Malaysia and the insurance and takaful industry. It is designed as a long-term programme to provide educational information to enhance financial literacy and awareness, with the following key objectives:

- To enable consumers to make well-informed decisions when purchasing insurance or takaful products;

- To assist consumers to be in a better position to select insurance or takaful products that best meet their needs;
- To understand their rights and responsibilities as consumers of insurance or takaful products and services.

4.2.2 CREDIT COUNSELLING AND DEBT MANAGEMENT AGENCY

AKPK

The Credit Counselling and Debt Management Agency or Agensi Kaunseling dan Pengurusan Kredit (AKPK*)* is an agency set up by Bank Negara Malaysia in April 2006 to help individuals take control of their financial situation and gain peace of mind that comes from the wise use of credit.

AKPK offers the following services to individuals, free of charge:

- Financial education on the responsible use of money and credit management skills;
- Counselling and advice on financial management;
- Debt management programme to assist consumers to regain financial control.

AKPK provides financial education materials on the proper use of credit and basic money management as well as tips on how to use credit responsibly.

4.3 FINANCIAL CONSUMER COMPLAINTS AND DISPUTES

There are various avenues for consumers to lodge a complaint in order to resolve a dispute with a Financial Service Provider (an insurance company or takaful operator) before taking the case to court. The following complaint mechanisms were implemented to provide consumers with easy access, speedy response and a fair and independent avenue to seek redress.

The following are the essential steps which a consumer must take in making a complaint:

Table 4-4 ***Making a consumer complaint***

4.4 COMPLAINTS UNIT OF FINANCIAL INSTITUTIONS

The Complaints Unit of the Financial Service Provider (FSP) must be easily accessible (via telephone, email or website) to customers and also be able to address complaints effectively and promptly. The FSP must provide a written acknowledgement within two working days, and the final decision or request for more information (if the case is complicated) must be done within two weeks of receiving the complaint.

If the complainant fails to respond within two weeks with the required information, the FSP must allow another two weeks' time for the complainant to respond and if there is still no response, the complaint can be treated as "No Further Action" and the complainant will be advised accordingly.

In all cases, the FSP will advise the complainant to submit the complaint to either the Financial Mediation Bureau (FMB) or Bank Negara Malaysia (BNM) if they are not satisfied with the outcome of the complaint resolution by attaching a copy of the decision letter of the insurance company or takaful operator.

4.5 OMBUDSMAN FOR FINANCIAL SERVICES (OFS)

OFS (formerly known as Financial Mediation Bureau) has been appointed by Bank Negara Malaysia as the operator of the Financial Ombudsman Scheme (FOS) in April 2016 pursuant to the *Financial Services Act 2013* (FSA) and the *Islamic Financial Services Act 2013* (IFSA). OFS is an independent body set up as an alternative complaint/dispute resolution body to assist financial consumers to resolve their complaints/disputes with the Financial Service Providers (FSPs) who are its Members.

Members of OFS include all:

- Licensed banks and Islamic banks.
- Licensed Insurers and Takaful Operators.
- Prescribed Development Financial Institutions.
- Approved Designated Payment Instrument Issuers and Designated Islamic Payment Instrument Issuers.
- Approved Insurance and Takaful Brokers.
- Approved Financial Advisers and Islamic Financial Advisers.

OFS Mandate

- To provide financial consumers with an avenue for effective and prompt resolution of complaints/disputes arising from products and services provided by its Members on "free of charge" basis.
- To resolve complaints/disputes in an independent, impartial and fair manner.
- To collaborate with Members in resolving complaints/disputes.
- To create awareness on matters of common interest to financial consumers and the financial industry.

OFS Jurisdiction

Table 4-5 *Jurisdiction of the OFS*

No	Type of complaint/dispute	Monetary Limit
1)	A complaint/dispute involving financial services or products or Islamic financial services or product, developed, offered or marketed by a Member, or by a Member for or on behalf of another person, other than a complaint/dispute under paragraphs 2 and 3. Types of disputes include: • Insurance/ Takaful • Life insurance claims • General insurance claims • Takaful family claims • Takaful general claims • Conventional/ Islamic Banking • Bancassurance/ Bancatakaful/ Investment–linked Insurance products/ Investment-linked Takaful products	RM 250,000.00
2)	A complaint/dispute on motor third party property damage insurance/takaful claims.	RM 10,000.00
3)	A complaint/dispute on: a) an unauthorised transaction through the use of a designated payment instruments or an Islamic designated payment instruments or payment channels such as Internet banking, mobile banking, telephone banking or automated teller machine (ATM); or b) an unauthorised use of a cheque as defined in section 73 of the *Bills of Exchange Act 1949* (Act 204).	RM 25,000.00 RM 25,000.00

Consumers are required to submit their complaints to OFS, within six months from the date of the final decision by the Member concerned, or after sixty (60) calendar days from the date of the complaint/dispute was first referred to the Member concerned in respect of which no response has been received from that Member.

Types of complaints *not* handled by OFS

a) A complaint/dispute that is beyond the maximum monetary limit;
b) A complaint/dispute on general pricing, product features, credit or underwriting decisions;
c) A complaint/dispute concerning the actuarial standards, tables and principles which a Member applies to its long-term insurance/takaful business for insurance or takaful claims;
d) A complaint/dispute relating to a contract of employment between a Member and its officers and employees or agency matters concerning a Member;
e) A complaint/dispute that has been filed in a court or arbitration or referred to arbitration or has been decided by a court or arbitrator;
f) A complaint/dispute that is referred to OFS after more than six months from the date the Member has provided its final decision;
g) A complaint/dispute that is time-barred under the *Limitation Act 1953* or Limitation Ordinance (Sabah) (Cap.72), or Limitation Ordinance (Sarawak) (Cap.49);

h) A complaint/dispute that had been previously decided by the OFS (including a complaint/dispute decided under the Predecessor Scheme) unless the new evidence, which are material facts that could change the earlier decision, is available for the OFS' consideration;
i) A complaint/dispute on the investment performance of a financial product except in relation to non-disclosure of facts or misrepresentation;
j) A complaint/dispute on capital market services and products offered or marketed by a Member;
k) A complaint/dispute that involves more than one Eligible Complainant and has been referred to the OFS without the consent of the other Eligible Complainant, and the OFS is of the view that it would be inappropriate to deal with the complaint/dispute without that consent;
l) A complaint/dispute involving claims arising from a third party bodily injury or death; and
m) A complaint/dispute relating to the payment of the policy money under life policy and personal accident policy or payment of takaful benefits under family takaful certificate and personal accident takaful certificate made in accordance with the provisions set out in Schedule 10 of the *Financial Services Act 2013* and the *Islamic Financial Services Act 2013* respectively.

The recommendation of the Case Manager is not binding on both parties. If either claimant or the Member does not accept the Case Manager's recommendation, the complaint/dispute may be referred to the Ombudsman for Adjudication within 30 days from the date of recommendation or by the date stipulated in the recommendation (whichever is later).

The decision of Ombudsman is final and is only binding on the Member if the complainant accepts that decision. However, if the complainant chooses not to accept the Ombudsman's final decision, the complainant is free to pursue the claim through any other means, including initiating a legal proceeding or arbitration.

4.6 BNMLINK

BNMLINK represents one of Bank Negara Malaysia's important points of contact with the public. It acts as a centralised point of contact to facilitate a rapid and effective response for members of the public, small and medium enterprises (SMEs) in matters related to the financial sector. BNMLINK, through its exhibitions, self-service kiosks and booklets also provide consumer financial education as well as awareness to the public on the role of Bank Negara Malaysia in nation-building.

Types of Complaints *not* handled by BNM

- Complaints that have been referred to OFS;
- Complaints that have been referred to and decided by OFS;
- Cases that have been referred to solicitors or legal actions have been instituted;

- Cases pertaining to institutions not under BNM's supervision, such as repair workshops and managed care organisations;
- Complaints made by agents against their principals or on employer/employee relationships or other matters not related to insurance or takaful.

PART B

5

CHAPTER 5 RETAKAFUL AND REINSURANCE

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CHAPTER OBJECTIVE

To understand Retakaful and Reinsurance with respect to general insurance and industrial insurance.

LEARNING OUTCOMES

After completing this topic you should be able to:

- *Learn how Reinsurance and Retakaful is an extension of the principle of insurance.*

5.1 UNDERSTANDING REINSURANCE/ RETAKAFUL

Reinsurance is an extension of the principle of insurance that risks should be shared or distributed as widely as possible so that the losses can be distributed and shared. This enables insurers to write various types of business, both big and small, as all claims will be shared between the primary insurer and the reinsurers.

Reinsurance is insuring again the risk that has been insured by way of ceding a percentage of the risk either to a reinsurer or another insurer. The process is a back-end operation that does not involve the insured. The insured will not be a party to the contract.

In reinsurance:

a) The original policyholder has no rights against the reinsurer, whatever the circumstances.
b) If the reinsurer becomes insolvent, the ceding company still remains liable for the full amount of the liability under the insurance contract with the policyholder.
c) If the ceding company becomes insolvent, the reinsurer is still liable under the ceding agreement.
d) The reinsurer has no contractual rights against any wrongdoing of the original policyholder.

5.1.1 FUNCTIONS OF REINSURANCE/ RETAKAFUL

The reasons for using reinsurance are:

a) **Flexibility** – Without reinsurance, insurers can only accept risks within their authorised capacity, within their resources. This would limit the ability to provide coverage to the public, especially if the risk is huge or risk exposure is high.
b) **Expansion** – Reinsurance can provide expertise to an insurer in areas where the insurer has limited experience, expertise or knowledge. By providing this assistance and accepting part or all of the risk, the reinsurer helps the insurer to grow its business.
c) **Accumulation** – Reinsurance helps the insurer in the event of catastrophic losses. By reinsuring, the insurer is able to limit the amount of exposure to a level that it is able to absorb.

5.1.2 RETAKAFUL AND REINSURANCE

This refers to a method where a single risk (on a case-by-case basis) is ceded to retakaful/ reinsurance and a proportionate share of the original takaful contribution/insurance premium shall be payable to the retakaful/reinsurance. Normally a certain commission will be levied on the retakaful operator/reinsurance company.

The retakaful operator/reinsurance company has the option to accept or decline such risk.

Below is an illustration of a risk placement done using the facultative method of retakaful/reinsurance:

- Takaful operator/insurance company X intends to accept a proposal of RM10 million
- Takaful operator/insurance company X Retention is RM1 million
- Balance to be ceded to retakaful/reinsurance is RM9 million
- Original takaful contribution/insurance premium is RM10,000

Takaful/Retakaful or Insurance/Reinsurance	Sum Covered / Share of Risk (RM)	% Share	Share of Contribution (RM)
Takaful Operator/ Insurance Company X	1,000,000	10 %	1,000
Retakaful Operator/ Reinsurance Company A	2,700,000	27 %	2,700
Retakaful Operator/ Reinsurance Company B	4,500,000	45 %	4,500
Retakaful Operator/ Reinsurance Company C	1,800,000	18 %	1,800
Total	10,000,000	100 %	10,000

5.1.2.1 METHODS OF REINSURANCE

RETAKAFUL

Takaful Operational Framework (TOF) of Bank Negara Malaysia requires takaful operators to fulfill the following requirements pertaining to its retakaful activities:

- A takaful operator must establish and implement a retakaful management strategy that is consistent with the risk appetite of its takaful business.
- A takaful operator shall only cede out takaful risks to other takaful operators or retakaful operators which may be a licensed takaful operator or foreign institution.

- Where risks are ceded to a takaful operator or retakaful operator which is a foreign institution, the takaful operator must ensure that such takaful operator or retakaful operator is conducting its business in compliance with Shariah.
- A takaful operator must not cede out risks to an insurer or reinsurer except under unavoidable circumstances, as per applicable rulings by Shariah Advisory Council.
- A takaful operator must establish and implement internal policies and procedures that clearly outline the unavoidable circumstances to allow cession(s) to an insurer or reinsurer which shall include the following:
    - no takaful operator or retakaful operator is known to accept the particular risk;
    - no takaful operator or retakaful operator has the capacity or expertise to accept the particular risk; or
    - a retakaful arrangement with takaful operator or retakaful operator creates potential detrimental effects to the takaful funds.
- A licensed takaful operator must not accept reinsurance inwards from an insurer or reinsurer except for risk that is permissible under Shariah and the inward arrangement is based on a retakaful contract between the licensed takaful operator and that insurer or reinsurer, as per applicable rulings by Shariah Advisory Council.

Sources: Bank Negara Malaysia Takaful Operational Framework. Applicable to: Licensed takaful operators including professional retakaful operators. Issued

Table 5-1 ***Reinsurance methods***

Facultative Reinsurance	The ceding company may offer the risk, or any part of it, to any reinsurer and the reinsurer is free to decide to accept it or not. Facultative reinsurance is done on a case by case basis as and when the need arises. It is generally used to enable the ceding company to dispose of a percentage of the risk, especially large risks beyond the scope of its treaty facilities and also those of extra hazardous nature. It has a number of disadvantages in that it is very time-consuming and hence expensive administratively.
Treaty Reinsurance	Treaty is an agreement between the insurer and a reinsurer, whereby the reinsurer will automatically accept any cessions falling within the terms of the treaty agreement. A cession is an amount ceded or given away to a reinsurer. The agreement or treaty will be for a time period and subject to restriction as to the type of risk or value involved. The treaty provides the automatic facility, arranged in advance and negotiations are normally only done at renewal each year.

TYPES OF TREATY REINSURANCE

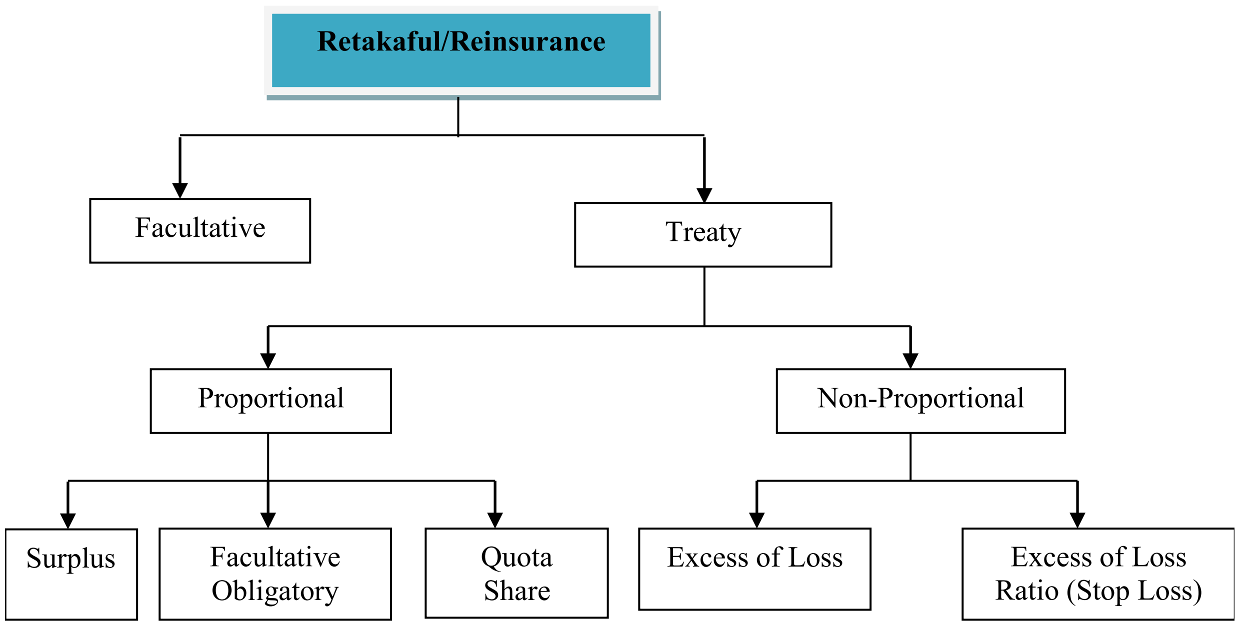
Table 5-2 ***Treaty reinsurance***

Proportional Reinsurance	In proportional reinsurance, the amount retained and the amount ceded will be based on certain proportions of the original sum insured accepted by the insurer. The sum insured, premium and losses will be shared in the same proportion between the insurer and the reinsurer. The two common types of proportional treaties are: a) **Surplus** – The treaty reinsurers are entitled to the share of any surplus risk over the retention of the ceding office up to the limit of the treaty. The limit of treaty capacity is defined in lines; a line is equal to a ceding company's retention on any one risk. Therefore, a ten-line treaty would provide in total a ceding company with a gross capacity of eleven times including its own retention. b) **Quota Share treaty** – The ceding company must cede to the reinsurer a fixed share on every risk undertaken by the ceding company. This treaty is arranged on a percentage basis (for example: Insurer – 60%, Reinsurer – 40%). The ceding company cannot retain all of any risk, no matter how small the sum insured.

Table 5-2 ***Treaty reinsurance***

Non-Proportional Reinsurance	Under this arrangement, the ceding company and the reinsurer do not share each loss in a fixed proportion and may not share some losses at all. The ceding company will be responsible for all losses below the loss retention amount and reinsurance will deal with the balance of any loss above the figure with usually an upper limit. The two common types of non-proportional treaties are: a) **Excess of Loss** – The reinsurer will only share the losses when a claim exceeds the amount of loss retained by the ceding company. For example, if the Excess of Loss Treaty is set at RM50,000 maximum in excess of RM10,000, then the insurer will have to bear the first RM10,000 after which the reinsurer will compensate up to a maximum limit of RM50,000. b) **Excess of Loss Ratio (Stop Loss)** – This cover is designed to prevent wide fluctuation in the claims ratio. If the insurer wishes to prevent the loss ratio from exceeding say, 90%, then it will buy an excess of loss ratio cover above 90% to 120%. The insurer will have to take a co-share of at least 10% on the range of between 90% and 120%. This is because reinsurers want to make sure the insurer will exercise prudent underwriting when accepting a risk.

Figure 5-1 ***Types of retakaful/reinsurance***



5.2 RISK MANAGEMENT UNDER RETAKAFUL/REINSURANCE

REGULATORY FRAMEWORK FOR RETAKAFUL OPERATORS

In order to ensure an orderly growth of retakaful business in Malaysia, in tandem with the growth of takaful business, Bank Negara Malaysia (BNM) has formulated a regulatory framework i.e. the *Guidelines on Establishment of Retakaful Operators in Malaysia (BNM/RH/GL/004–12)* as follows:

Table 5-3 ***Regulatory Framework for Retakaful Operators***

FEATURE	DESCRIPTION/REMARKS
Financial strength and financial flexibility	• The applicant must be financially sound with strong capital support and good track record of operating profits to ensure that the proposed new retakaful operator provides good security and continued commitment to its retakaful operations in Malaysia; and • The applicant should have a combined paid-up capital and surplus of at least USD100 million and good international ranking or rating from well-recognised rating agencies.
Related experience in insurance/reinsurance and/or takaful/retakaful	The applicant should have the experience of conducting diversified types of retakaful business. Favourable consideration will be accorded to the applicant with special technical expertise that benefits the Malaysian takaful market and the region.
Ability to contribute towards national agendas	• The applicant must be able to demonstrate that the proposed retakaful operator could contribute effectively to the development of the takaful industry and hence complement the efforts taken by the Government and the Bank in establishing Malaysia as an international Islamic financial centre. Favourable consideration will be given to applicant intending to establish its retakaful set-up in Malaysia as the centre for its regional or international retakaful business; and • The applicant will also be required to provide plans towards transferring technical knowledge to local takaful market and optimising local talents in the management of the company.
Viability of the Malaysian operations	The business plan of the proposed retakaful operator should demonstrate the viability of its Malaysian office within a 5-year period based on realistic assumptions.

6

CHAPTER 6 GENERAL INSURANCE AND TAKAFUL PRODUCTS

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CHAPTER OBJECTIVE

To understand the types of general insurance policies and takaful certificates and the scope of cover.

LEARNING OBJECTIVES

After you complete this chapter, you will be able to:

- *Describe the basic features and outlines of typical coverage for the various classes of General Insurance/ Takaful.*
- *Comprehend the types of Motor Insurance/ Takaful policies.*
- *Appreciate the coverage offered under Fire Insurance.*
- *Explain the types of Industrial Insurance/ Takaful and their extensions.*
- *Recognise the salient features of the Workmen's Compensation Act.*
- *Interpret the liabilities that come under Employers' Liability Insurance/ Takaful.*

6.1 GENERAL INSURANCE/ TAKAFUL PRODUCTS

General insurance or general takaful (sometimes known as *property and casualty insurance* or *takaful*), is a type of insurance or takaful business which provides cover against financial loss to properties and other casualty classes due to fortuitous circumstances. It does not include the other type of takaful business, namely family takaful, which is essentially related to the life of individuals.

The coverage of general takaful products is similar to that of conventional insurance products except for the existence of takaful elements of *tabarru'* and *mudharabah* or *wakalah*. General insurance and takaful, like other forms of insurance and takaful protect people against unexpected loss or damage of properties or goods due to fire, accident, flood and other calamities.

However, unlike general insurance there are some restrictions on the assets that can be covered by general takaful. Assets such as wine, swine, carrion and stolen properties do not comply with Shari'ah principles. No value can be attached to these items. Therefore, they cannot be covered in takaful.

All other assets with intrinsic value that can be acquired, possessed and owned by a person or a body or a body corporate and more importantly, recognised by the law as well as the Shari'ah, are defined as *mal* in Arabic and can be covered in takaful.

6.2 MAIN CLASSES OF GENERAL INSURANCE/ TAKAFUL PRODUCTS

The broad categories of general insurance classes are listed as:

a) Motor – "Act" and Others.
b) Fire – including Business Interruption/ Consequential Loss resultant from Fire.
c) Marine, Aviation and Transit.
d) Medical Expenses and Personal Accident.
e) Liability.

f) Engineering and Contractors All Risks.
g) Workmen's Compensation and Employers' Liability.
h) Miscellaneous – Burglary, Money, Golfers, All Risks and others not listed above.

Generally, all these policies [risks] are underwritten by general insurance companies.

Medical insurance and personal accident insurance are also underwritten by life companies. Both these classes are commonly referred to as Insurance of Persons.

6.2.1 MOTOR INSURANCE/TAKAFUL – ROAD TRANSPORT ACT 1987 (RTA)

Motor vehicles are constantly exposed to various risks while on the road. Apart from the various types of vehicles, public transportation systems and public properties, pedestrians also use the roads daily. These objects and people are exposed to the risk of an accident, an injury, death, loss of or damage either directly or to a third party.

The motor insurance policy protects and compensates persons against any financial losses resulting from an accident or theft. It is also designed to compensate third parties against injuries sustained during an accident where the policyholder and/or their authorised driver are found to be negligent.

Under Section 90 of the *Road Transport Act 1987*, it is not lawful to permit a person to use a motor vehicle on the road unless there is in force a policy of insurance in respect of third party risks (third party bodily injury and property damage).

Drivers who breach this regulation are subject to:

- A fine of RM1, 000 or 3 months imprisonment or both.
- In addition, if the court deems so, they also may be disqualified from holding a licence for a period of 12 months from the date of conviction.
- The *Road Transport Act 1987* also includes other sections such as:
  - Section 41 – Causing death by reckless or dangerous driving.
  - Section 42 – Reckless and dangerous driving.
  - Section 43 – Careless and inconsiderate driving.

THE PURPOSE AND SCOPE OF COMPULSORY MOTOR INSURANCE

One important aspect of the government's involvement in insurance is where it has made certain classes of insurance compulsory. This is the case for certain types of injury and damage following road accidents and certain injuries at the workplace.

The Need for Compulsory Motor Insurance

The following are the reasons for making motor insurance compulsory:

a) Provision of funds

If a third party makes a claim against any negligent driver, the court declares an award. There would be no point in awarding damages to someone if there were no funds to meet the award. The enactment of compulsory insurance ensures, as far as possible, that funds are available when damages are awarded. This is because insurance companies are guaranteed and have the funds to make out these payments which can sometimes be in millions.

b) Easing the Government's burden

It is unlikely that the government would allow people injured at work or in other accidents to go without compensation entirely. If the responsible party does not have funds, the government may have to come forward with some form of compensation. The existence of insurance eliminates this possibility as insurers have the funds to compensate victims.

c) National Concern

Governments often bring in legislation in response to public concern about risks. It is likely that this played a part in the introduction of compulsory insurance for motor vehicles.

THE MALAYSIAN MOTOR INSURANCE POOL (MMIP)

The Malaysian Motor Insurance Pool (MMIP) is a high-risk insurance pool that is run collectively by the insurance and takaful industry under orders from the regulators. It provides motor insurance to vehicles having difficulty obtaining motor insurance from the commercial insurance market. These high risks in the pool are shared among all general insurance and takaful companies.

MOTOR TARIFF

Motor and takaful insurance in Malaysia have been gradually detariffed since July 2016. However, insurers are still closely guided by the various sections in the policy despite being more innovative in the products and extensions provided by each insurer. Some benefits have been amended accordingly. Bank Negara still has some control on the maximum discounts allowed for motor.

Reference to the Motor Tariff is made with regards to the following:

a) Different Types of Motor Vehicles
b) Coverage Type
c) Minimum Premium
d) Descriptions of Section A and Section B
e) Rating Tables
f) Short Period Rates
g) Additional Benefits

h) No–Claim–Discount
i) Cancellation Procedures

The Motor Tariff comprises 11 Sections:

1) Section 1 – Revised Knock-for-Knock Agreement
2) Section 2 – General Regulations
3) Section 3 – Guide to Completion of the Policy Schedule
4) Section 4 – Guide to Completion of the Certificate of Insurance
5) Section 5 – Private Car Tariff
6) Section 6 – Commercial Vehicle Tariff
7) Section 7 – Motor Cycle Tariff
8) Section 8 – Endorsements
9) Section 9 – Warranties
10) Section 10 – Specimen Policies
11) Section 11 – East Malaysia Motor Tariff

The Motor Tariff also caters for Fleet policies for a single company that has more than 10 cars and prefers a single master policy to manage these vehicles.

TYPES AND USES OF VEHICLES

Table 6-1 ***Types and uses of vehicles***

Private Car	"Private car" includes vehicles being used solely for social, domestic and private pleasure purposes including the insured's own business but excludes use for hire and reward, racing, speed testing, tuition, etc. The normal private car policy excludes use for the carriage of goods. If this coverage is required, an additional 70% premium/contribution will be charged.
Commercial Vehicle	This category of vehicles includes vehicles used for businesses, transportation and hire and drive. Any vehicle other than three-wheeled carriers which are not provided for under the private car or motorcycle tariff falls under this category. Examples of commercial vehicles include: • Motor Trade • Goods-Carrying Vehicles • Hire Cars • Omnibuses, private and public • Special Types
Motorcycle	The term "Motorcycle" shall include motor scooters and auto cycles or mechanically assisted pedal cycles with an engine capacity not exceeding 100cc with a constant gear ratio and manufacturer's speed not exceeding 25 mph. Private motorcycles are those that are used for social, domestic and private pleasure purposes and are used to carry out the insured's own business. Commercial motorcycles are those that are used by the insured for business or profession including carriage of goods but excluding use for carriage of passengers.

6.3 TYPES OF MOTOR INSURANCE/ TAKAFUL POLICIES/ CERTIFICATES

The Motor Tariff caters for the following policy types/coverage types:

a) **Comprehensive**;
b) **Third Party**;
c) **Third Party, Fire and Theft** – only in respect of vehicles laid up in a public or private garage;
d) **Act** – minimum cover reserved for vehicles with very high risk.

Table 6-2 ***Motor tariff policies***

Comprehensive	The coverage provided under the comprehensive motor policy includes the following sections: **a) Section A – Loss or Damage to your Vehicle** This will cover you if your vehicle is damaged or lost under the following circumstances: • Accidental collision or overturning • Collision or overturning caused by mechanical breakdown or wear and tear • The impact caused by falling objects provided there is no flood or typhoon • Fire, explosion or lightning • Burglary, housebreaking or theft • Malicious act • Whilst in transit including its loading or unloading by road or inland waterway and direct sea route across the straits between the island of Penang and the mainland • The basis of Settlement will include the following options: • Pay the cost of repairs • Pay in cash the amount of loss • Reinstate or replace your vehicle Transportation of Vehicles Damaged in an accident (Towing): • Up to RM200 for the private and commercial vehicle (or RM50 for motorcycle) as towing charges Exclusions to Section A include: • consequential losses of any nature • loss of use of a vehicle • depreciation, wear and tear, rust and corrosion, damage to tyres unless the vehicle is damaged at the same time • the act of cheating, criminal breach of trust • excess Policy Excess is the first amount under the policy that must be borne by the insured. The reason for having an excess is to avoid small claims which eventually can be an administrative nightmare to the insurer. Compulsory Excess is additional RM400 excess that will be applicable when • the driver is not named in the policy • the driver's age is below 21 years • the driver is a holder of a provisional licence

Table 6-2 *Motor tariff policies*

	b) Section B – Liability to Third Party Will pay the amount you or your authorized driver who are legally liable to pay (including claimant cost and expenses) for • Death or bodily injury to the third party • Damage to third party property Cover for Legal Representatives: • The legal cost incurred for the defence of any charges including causing death up to RM2,000. Exclusions under Section B: • Death or bodily injury to any passengers being carried for hire or reward • Death or bodily injury to any person in the course of employment with the insured • Damage to property belonging to the insured or driver • All legal costs and expenses which are not incurred in or recoverable in Malaysia, Singapore and Brunei • A person who is a member of the insured's household unless bound to travel under his contract of employment • Any claims brought outside the geographical and jurisdiction limit of Malaysia, Singapore and Brunei Other General Exclusions under the motor policy are as follows: • Driving without a valid driving licence • The driver is drunk and/or under the influence of drugs • The vehicle being used for an unlawful purpose • Caused by war, terrorism, strike, riot • Caused by earthquake, storm, flood, typhoon or other convulsions of nature • Motorsports or competition • Loss, damage or liability outside the geographical area • Nuclear risk • The vehicle was left unattended
Third Party Policy Only	The Third Party Policy will pay the amount you or your authorized drivers are legally liable to pay (including claimant's cost and expenses) for • Death or bodily injury to the third party • Damage to third party property Cover for Legal Representatives: • The legal cost incurred for the defence of any charges including causing death up to RM2,000 Exclusions: • Death or bodily injury to any passengers being carried for hire or reward • Death or bodily injury to any person in the course of employment with the insured • Damage to property belonging to the insured or driver • All legal costs and expenses which are not incurred in or recoverable in Malaysia, Singapore and Brunei • A person who is a member of the insured's household unless bound to travel under his contract of employment • Any claims made outside the geographical and jurisdiction limit of Malaysia, Singapore and Brunei.

Table 6-2 *Motor tariff policies*

Third Party, Fire and Theft	In addition to the cover granted by the third party only policy, this policy also provides cover for the loss of or damage to the insured vehicle as a result of fire or theft. The theft and fire risk elements contribute to the rate sufficiently and the premium is close to that charged for a comprehensive policy, which is 75% of the total comprehensive premium. The cost of this insurance makes it unpopular among consumers as they consider it not a worthwhile option and would rather take up the comprehensive cover, which provides wider cover.
Act Cover	Act Cover is the minimum coverage provided by motor insurers to meet the requirement of the *Road Transport Act 1987*. The cover required is in respect of legal liability for death or bodily injury to a third party (excluding passengers) caused by or arising out of the use of the insured motor vehicle on a road. This cover is rare and is only reserved for situations where the risk is exceptionally poor or high.

6.3.1 EXTRA BENEFITS AND ADDITIONAL COVER

The Motor Tariff allows for policyholders to extend coverage to include extra benefits and additional cover, apart from the standard coverage. Given below are some of the benefits, and the requirements that are applicable to them, according to the requirement of the insured.

a) Flood, windstorm, rainstorm, typhoon, hurricane, volcanic eruption, earthquake, landslide/landslip, subsidence or sinking of the soil/earth or other convulsions of nature:
   - Additional premium of 0.5% on the value for each year or part of the year
   - Minimum Premium: RM15

b) Breakage of glass in windscreen or windows
   - The amount must not exceed the sum insured selected
   - A claim in respect of this benefit will not affect the NCD
   - Additional Premium of 15% on the Sum Insured selected
   - Minimum Premium: RM 30

c) Strike, riot and civil commotion
   - Private cars – 0.3% of the sum insured of the vehicle per annum
   - Minimum Premium: RM5

d) Tuition and testing purposes
   - Privately owned cars, not owned and operated by a driving institute
   - Additional Premium of 50% of the scheduled premium and this will not be subject to NCD

e) Additional Named Driver
   - In addition to the insured and one other named driver, additional named drivers will be granted free of compulsory excess, if they are named in the policy and the additional premium of RM10 per additional name is paid.
   - All drivers' extension is no longer permitted for private cars used by individuals.

f) All drivers' extension is granted for private car policies issued to a company, or business organisations only.
   - Additional Premium of RM 50 per vehicle

g) Passenger Liability
- Additional premium of 25% of the third-party premium according to the cubic capacity of the vehicle.
- If seating capacity is above 5 (including the driver), an additional premium of RM10 per additional seat will be charged in addition to the 25% additional premium based on the third party premium rate.

h) Liability of passengers for acts of negligence
- Additional premium of RM 7.50 per vehicle

i) Additional Business Use
- For named persons other than the insured or fellow employees
- Additional premium of 25% per named person

6.3.2 NO-CLAIM-DISCOUNT (NCD)

The Motor Tariff has a provision which allows the insurer to award the insured with a discount if there are no claims made on his motor insurance policy on an annual basis. The No-Claim-Discount is allocated to the insured on each and every vehicle separately. The insured may use his NCD entitlement by transferring it from one car to another depending on the entitlement so that he may enjoy a higher discount on the premium for the car which has a higher Sum Insured.

The No-Claim-Discount given to a policyholder increases by the year, and is based on the NCD table (see Table 6-3). If an insured changes his insurer or transfers his NCD, he must produce certain documents as proof that there were no claims with his previous insurer.

Following are the documents that can be used as proof to enjoy the NCD entitlement:

- Policy Schedule
- Renewal Notice
- Endorsement with NCD stated on it

The new Insurer will reconfirm the NCD level by logging into the ISM NCD System

Table 6-3 ***NCD entitlement as per the Motor Tariff***

Number of Renewals	Private Car	Motor Cycle	Commercial
1 year	0%	0%	0%
2 years	25%	15%	15%
3 years	30%	20%	20%
4 years	38 1/3%	25%	25%
5 years	45%	25%	25%
6 years	55%	25%	25%

Source: Malaysia Insurance Online, 2010

Whenever a vehicle is not insured or renewed for a period of time, the NCD level comes down one level every year.

6.4 FIRE INSURANCE/TAKAFUL

Fire insurance is categorised as property insurance, and covers tangible property such as buildings, machinery and plant, and so on, against loss or damage caused by fire, flood and other extraneous perils. Although the word 'property' includes motor vehicles, ships and aircraft, insurance for such property are dealt separately by specialised types of insurance such as motor, marine and aviation.

Fire insurance forms a separate class. A fire insurance policy involves an insurance company agreeing to pay to the insured a certain amount equivalent to the estimated loss caused by fire, within the time specified in the contract. The indemnity is subject to change depending upon the policy.

Fire insurance has now been detarriffed and insurers are allowed to give a discount of up to 30 % on the tariff rate for commercial risks also known as commercial rate. However the commissions, and policy and endorsement wordings used are still as per the Fire Tariff which is regulated by Persatuan Insurans Am Malaysia (PIAM).

Fire insurance is a specialised form of insurance designed to cover the cost of replacement, reconstruction or repair to the property damaged by fire or other extended perils such as a flood. The policy covers damage to the building itself, and may also be extended to cover damage to nearby structures, personal property, and the expenses associated with not being able to live in or use the property if it is damaged.

The standard fire policy provides cover to the insured in the event of loss or damage to the property insured by:

- Fire.
- Lightning.
- Explosion of gas used for domestic purposes only.

ADDITIONAL COVER

Subject to the insured's agreement and payment of additional premium, the basic policy can be extended to cover the following named perils:

- Aircraft Damage;
- Earthquake and Volcanic Eruption;
- Storm/ Tempest;
- Flood Damage;
- Explosion;
- Impact Damage;
- Bursting or Overflowing of Water Tanks, Apparatus or Pipes;
- Riot Strike and Malicious Damage;
- Electrical Installation Clause B;
- Bush or Lallang Fire;
- Subsidence and Landslip;
- Spontaneous Combustion;
- Damage by Falling Trees or Branches and Objects therefrom;
- Sprinkler Leakage;
- Smoke Damage.

BASIS OF SUM INSURED

The measure of an insured's loss is the cost of restoring the damaged property or replacing it with property similar in condition to that at the time of the loss.

Buildings	The current cost of reconstruction of the building to the original form means less deduction justified for the betterment
Plant & Machinery	The cost of replacement with a new item less deduction for depreciation due to wear and tear
Stocks	**Raw materials** – the cost of materials including freight and duty **Finished goods** – the cost of raw materials plus production cost

Important Note

It is necessary that:

- Vacant risk premises are subject to the Vacant Risk Warranty, whereby no storage of goods of any kind is permitted and all doors, windows and other openings shall be tightly secured.
- Cover ceases once the property becomes unoccupied for more than 30 days.

PREMIUM RATING

Table 6-4 ***Types of premium rating***

Tariff Rating	• Applicable to risks where the sum insured (fire and fire consequential loss combined) is less than RM10 million. • Premium rates are as per Revised Fire Tariff (latest revised version with effect from 01 July 2000).
Self-Rating	• Applicable to risks where the sum insured (fire and fire consequential loss combined) is between RM10 million to RM50 million. • Premium rates are computed by insurers using the self-rating structure provided by PIAM, which is found in the Revised Fire Tariff.
Special Rating	• Special rating can be applied for risks where the total sum insured exceeds RM50 million (fire and fire consequential loss combined). • PIAM's Technical Rating Committee will determine the special rate. • Insurers are required to submit an application for review of the special rate to the Rating Committee in the event of any material change of the risk.

6.5 FIRE BUSINESS INTERRUPTION INSURANCE/TAKAFUL

Fire business interruption insurance, also known as consequential loss insurance, provides indemnity to the insured in respect of loss of profits. Any loss under the material damage policy is likely to affect the business interruption insurance as this leads to an interruption in the business in terms of loss of production, sales and consequent earnings.

This policy will pay for net profit and fixed charges resulting from interruption of business following loss or damage by fire and the insured perils. This insurance can only be taken together with fire (material damage) insurance.

COVERAGE

The policy will compensate the insured in respect of:

- Loss of gross profit following reduction in turnover, and
- Increase in cost of working

resulting from fire, including damage by any additional perils specified in the material damage policy.

The Gross Profit, which will be the sum insured under this policy, can be calculated on a:

- Difference basis, or
- Addition basis.

The figures are derived from the previous year's accounts.

a) **Difference Basis:** This method of calculating gross profit will take into account:
    - The sum of turnover and the amount of closing stock and work in progress less the sum of the opening stock, uninsured working expenses, and work in progress.

b) **Additional Basis:** This method of calculating gross profit will be as follows:
    - Net Profit plus insured standing charges (fixed charges) such as salaries, wages, EPF contribution and bonuses.

INCREASED COST OF WORKING

Increase in cost of working means the expenses that will be necessarily and reasonably incurred for the sole purpose of avoiding and diminishing the reduction in turnover subject to the economic limit as stated in the policy. This could be in the form of rental of alternative premises, express freight, overtime expenses, and so on.

ADDITIONAL COVER

Depending on the insured's needs and subject to the insurer's agreement and the payment of additional premiums, the basic policy can be extended to cover the following special perils:

- Specified supplier's extension,
- Unspecified supplier's extension,
- Prevention of access extension,
- Public utility extension (water, electricity and gas),
- Unspecified customer's extension,
- Infections or contagious diseases, murder, suicide, pest, food or drink poisoning or defective sanitary arrangements.

EXCLUSIONS

Since the business interruption policy comes together with material damage insurance, the exclusions will be similar to the material damage policy.

COMMON CLAUSES

Some common clauses used in this policy would be:

- Accountants' Clause.
- Payment on Account Clause.
- Departmental Clause.
- Alternative Basis Clause.
- Upward Adjustment Clause.
- Material Damage Proviso Waiver Clause.
- Salvage Sales Clause.

SUM INSURED

The sum insured will be tied up with the Indemnity Period/Maximum Indemnity Period selected by the insured. Indemnity Period refers to the period which starts when the loss occurs and ends no later than the maximum indemnity period, which is the maximum period for which an insurer will pay, after which the insured becomes his own insurer. The indemnity period will depend on the nature of the business, the ability to obtain other premises and facilities with which the existing premises or contents can be repaired or replaced. The sum insured must therefore be suitably adjusted for trends in the business. It should be borne in mind that this policy is subject to average in the event of underinsurance.

6.6 HOUSEOWNERS AND HOUSEHOLDERS INSURANCE/TAKAFUL

Houseowners' insurance, also called homeowners insurance (often abbreviated in the real estate industry as HOI), is the type of property insurance that covers residential property, i.e. private dwellings, apartments or flats.

The householders' insurance (HHI), on the other hand, provides coverage for household contents only.

Another type, house owners and householders insurance, combines various personal insurance protections, which can include losses occurring to one's home, its permanent fixtures and fittings, loss of its use (additional living expenses), as well as liability insurance for accidents that may happen at the home or at the hands of the homeowner within the policy territory.

Houseowners and householders insurance is a multiple-line insurance, meaning that it includes both property and liability coverage, with an indivisible premium, meaning that a single premium is paid for all risks. Standard forms divide coverage into several categories, and the coverage provided is typically a percentage of Coverage A, which is coverage for the main dwelling.

Typically, cover afforded by the house owners and householders policy is as follows:

- Fire, lightning, thunderbolt, subterranean fire.
- Explosion.
- Aircraft and other aerial devices and/or articles dropped therefrom.
- Impact by any road vehicles or animals not belonging to or under the control of the insured or any member of his family.
- Bursting or overflowing of domestic water tanks, apparatus or pipes.
- Theft but only if accompanied by actual forcible and violent breaking into or out of a building or any attempt thereat.
- Hurricane, cyclone, typhoon, windstorm.
- Earthquake, volcanic eruption.
- Flood but excluding loss or damage caused by subsidence or landslip.

INTEREST/ PROPERTY INSURED

Table 6-5 ***Interest/ property insured in the Houseowners and Householders Insurance/Takaful Policy***

Section I	• Buildings • Loss or damage to the building
Section II	• Household contents • Loss or Damage to Contents • Property Temporarily Removed • Damage to Mirrors by breakage (excluding hand mirrors) • Compensation for Death of the Insured provided death occurs within 3 calendar months of injury • Servants' Property
Section III (A)	• Loss of Rent if the dwelling is rendered uninhabitable, due to an insured peril.
Section III (B)	• Liability to the public up to RM50,000

PREMIUM/CONTRIBUTION AND EXTENSIONS

The basic premium is calculated based on a standard fire tariff rate prescribed by Persatuan Insurans Am Malaysia (PIAM) and is affected by the type of building (dwellings detached, and non-detached, flats or apartment), and construction classification of the building.

At an additional premium, the basic policy can be extended to cover the following:

Table 6-6 ***Extensions to the basic Houseowners and Householders Insurance/Takaful Policy***

Applicable to Section I – Buildings	• Plate glass • Alterations, repairs and additions
Applicable to Section II – Contents	• Unoccupancy in excess of 90 days • Full theft
Applicable to both Sections	• Riot, Strike and Malicious Damage • Subsidence and Landslip • Increase in the limit of liability to the Public

SUM INSURED

The following is a simple guide on how to arrive at the rebuilding cost and subsequently the sum insured on a building for insurance purpose.

Example

Rebuilding cost and the sum insured on a building for insurance purpose

- Length of property: 66 feet
- Width of property: 22 feet
- No. of floors: 2
- Total built-up area of property: 66 x 22 x 2 = 2,904sq. feet

Current BASIC rebuilding cost,* say @ RM80 per sq. foot = 2,904 x 80 = RM232,320

*(*Note: The rebuilding cost would depend on the finishing as well as the location of the property. A building contractor can easily provide a quotation. As a rule of a thumb, a figure between RM60 to RM150 per square foot can be used.)*

Based on the above rebuilding cost, you can roughly work out the sum insured for insurance purposes on the following basis:

Indemnity Basis	
Rebuilding cost	232,320
less depreciation for wear and tear, say 20%	(46,464)
	185,856
add inflation for insurance year, say 5%	9,293
	195,150
Rounded-up	**205,000**
Reinstatement Value Basis	
Rebuilding cost	232,320
add inflation for insurance year, say 5%	11,616
	243,936
add inflation for max. reinstatement, say 12 months @7%	17,076
	261,012
Rounded-up	**262,000**

The policyholder may increase the above figures sufficiently to include:

- Removal of Debris and/or
- Professional Fees.

The above figures are used to show the workings of the calculation only.

AVERAGE CLAUSE

If at the time of loss, the property insured is of greater value than the sum insured, the insured will have to bear a rateable proportion of the loss.

Example

Average clause

- Value at Risk: RM250,000
- Sum Insured: RM200,000
- Loss or Damage: RM 80,000
- Insurer pays: $\frac{200{,}000}{250{,}000} \times 80{,}000 = RM64{,}000.$
- The balance of RM16,000 will be borne by the insured due to underinsurance.

6.6.1 INDUSTRIAL ALL RISKS INSURANCE/TAKAFUL

This insurance/takaful provides cover against loss of or damage to property and/or interests caused by any unforeseen sudden and accidental physical loss, destruction or damage such as fire, lightning, explosion, falling of aircraft, smoke, flood, self-combustion, short circuit, burglary and risks other than those specifically excluded in the insurance policy/takaful certificate as well as loss of profit as a consequence of material damage to the property covered.

This class of business is normally offered to commercial and industrial risks which require a more careful technical underwriting approach and support from reinsurance/retakaful. Industrial mega risks are normally written under the property all risks class.

6.7 MARINE INSURANCE/TAKAFUL

Marine insurance is one of the earliest forms of insurance and had its humble beginnings in Edward Lloyd's coffee house which became the meeting place for parties in the shipping industry wishing to insure cargoes and ships, and those willing to underwrite such ventures. These informal undertakings eventually led to the establishment of the insurance market called Lloyd's of London and several related shipping and insurance businesses. Marine insurers provide cover for known quantifiable risks, mainly hull and machinery insurance for ship-owners, and cargo insurance for cargo owners.

The subject matter of marine insurance and their potential exposure to risks are summarised as follows:

Figure 6-1 ***Subject matter of marine insurance***

6.7.1 MARINE HULL INSURANCE/TAKAFUL

Marine hull insurance covers loss or damage to the vessel and machinery arising from maritime perils as well as salvage costs and limited property damage liability. The terms and conditions of the coverage are spelt out in the Institute Time Clauses – Hulls. Builder's risk policies, on the other hand, protect these vessels during construction until they are ready for operation.

3/4TH COLLISION LIABILITY

The marine hull insurance covers damage caused by collisions with other ships for only ¾ of the liability for such damage (a quarter of such damage is paid by Protection & Indemnity clubs). The maximum recovery under hull policies, including damage to the insured ship and liability for the damage it had caused is the insured value of the ship.

PROTECTION & INDEMNITY (P&I)

P&I clubs provide insurance cover for broader, indeterminate risks, such as third-party liabilities that marine insurers usually do not cover. Third party risks include a carrier's liability to a cargo-owner for damage to cargo, a shipowner's liability after a collision, environmental pollution and P&I war risk insurance that is to say legal liability arising out of acts of war affecting the ship.

Example

Protection & Indemnity (P&I) Insurance

Assume that both vessels in a collision are insured for ¾ collision liability with their hull underwriters and for ¼ with their P&I Clubs. Vessel A is 75% to blame for the collision and vessel B is 25% to blame. Vessel A suffers damage costing $100,000 and vessel B damage costing $200,000. The payments by each underwriter are illustrated below.

	Vessel A	**Vessel B**
Percent to blame	75%	25%
Own damage	$100,000	$200,000
Liability to other vessel	$150,000 (75% x $200,000)	$25,000 (25% x $100,000)
Net settlement	$125,000 paid to B	
Underwriters pay	$112,500 (3/4 x $150,000)	$18,750 (3/4 x $25,000)
P&I pays	$ 37,500 (1/4 x $150.000)	$ 6,250 (1/4 x $25,000)

Each collision liability underwriter reimburses its share of each vessel's gross liability to the other vessel. In most maritime jurisdictions, the question of responsibility for collisions is determined with reference to the International Regulations for the Prevention of Collisions at Sea, which codify how vessels should conduct themselves in order to avoid collisions. The apportionment of liability between the vessels is normally based on the causative importance of any breaches of these regulations.

6.7.2 MARINE CARGO INSURANCE/TAKAFUL

Marine cargo may take the following forms of insurance, when using sea or inland waterway transportation:

a) **Free on Board (FOB)** – risk passed on to the buyer including payment of all transportation and insurance cost once delivered on board the ship by the seller.
b) **Cost and Freight (CFR)** – title, risk and insurance cost passed on to the buyer when delivered on board the ship by the seller who pays the transportation cost to the destination port.
c) **Cost, Insurance and Freight (CIF)** – title and risk passed on to the buyer when delivered on board the ship by the seller who pays the cost of transportation and insurance to the destination port.

There are three main types of marine cargo policies which would incorporate any one of the following clauses:

1) **Institute Cargo Clause A – All Risks**
2) **Institute Cargo Clause B – Specific Risks**
3) **Institute Cargo Clause C – Specific Risks**

The perils insured by the respective Institute Cargo Clauses are described below:

Table 6-7 ***Perils insured by the respective Institute Cargo Clauses***

NAMED PERILS	INSTITUTE CARGO CLAUSES		
	A	B	C
Sinking, stranding, grounding, capsizing	√	√	√
Fire, explosion	√	√	√
Collision	√	√	√
Overturning, derailment of land conveyance	√	√	√
Earthquake, volcanic eruption, lightning	√	√	X
General Average Sacrifice	√	√	√
Jettison	√	√	√
Discharge of cargo at port of distress	√	√	√
General average and salvage charge	√	√	√
Washing overboard	√	√	X
Entry of sea, lake, river water into vessel	√	√	X
Total loss of package during loading or discharge	√	√	X
Pirates and thieves	√	X	X
Deliberate damage or destruction	√	X	X
Wilful misconduct of the insured	X	X	X
Ordinary leakage, loss in weight or volume, wear and tear	X	X	X
Insufficiency or unsuitability of packing	X	X	X
Inherent vice or nature of the subject matter	X	X	X
Unseaworthiness and unfitness of vessel (when the insured is privy to it)	X	X	X
Insolvency or financial default of carrier	X	X	X
War, strikes, riots and civil commotions	X	X	X
Atomic and nuclear weapons	X	X	X

MARINE CARGO EXTENSIONS

The following extensions are provided on payment of additional premiums as prescribed by the Institute of London Underwriters (ILU):

- Institute War Clause
- Institute Strike Clause

MARINE CARGO EXCLUSIONS

Marine Cargo exclusions include:

- Wilful misconduct of the Assured.
- Ordinary leakage, loss of weight or volume, wear and tear.
- Improper packing.
- Inherent vice.
- Delay.
- Insolvency or financial default of carrier.

6.8 AVIATION INSURANCE/TAKAFUL

Most aviation insurance policies are issued on an "All Risks" basis covering damage to the hull, legal liability to passengers and to third parties. Wars and allied perils risks are excluded from the policy cover. However, insurers may write back parts of the exclusion, usually for

a) Strikes, riots, civil commotion or labour disturbances
b) Malicious act or act of sabotage
c) Hijacking or unlawful seizure of aircraft.

There are many types of policies and coverages available in the market for Both small and major airlines. The basic coverage for all airlines is similar, allowing for extension of coverage to meet the needs of major airlines.

Generally, these are two independent policies covering:

1) Aircraft Hull and Liabilities
2) Aviation Hull, 'War and Allied Perils'

Aviation insurance buyers mainly comprise large commercial airliners who may arrange "Fleet Policies" to cover all aircrafts owned or operated by them.

Other buyers for more basic cover would include:

- Corporate/business aircraft owners;
- Private owners; and
- Flying clubs.

6.9 GOODS IN TRANSIT INSURANCE/TAKAFUL

Goods in transit insurance cover conveyances of goods as a direct result of domestic sales or purchases. The insurance is normally taken out by the owner of the goods or by a professional carrier or logistics company; who are equally responsible for the goods in their custody. The goods in transit policy usually offer 'All Risks' type of coverage on an annual basis or on each and every transit basis.

SCOPE OF COVER

The scope of cover includes the following:

- Indemnity for physical loss of or damage to goods by fire, accident, theft or pilferage while being conveyed on land by road, rail and inland waterway (e.g. by ferry from the mainland to Penang island); and
- Whilst loading and unloading from the vehicle or trailers and during temporary storage in the ordinary course of transit within the geographical boundaries (e.g. Malaysia and Singapore).

MAIN EXCLUSIONS UNDER GOODS IN TRANSIT INSURANCE

The main exclusions include:

- wear and tear and depreciation;
- delay, loss of market, consequential loss of any kind;
- theft or pilferage by the insured's employees;
- earthquake and subterranean fire;
- moth, vermin, insects, damp, mildew or rust;
- deterioration and changes by natural causes;
- goods accompanying commercial travellers; and
- cargo such as explosives, hazardous chemicals and acids, cash, bank and currency notes, securities, jewellery, and business books.

6.10 ALL RISKS INSURANCE/TAKAFUL

The all risks policy provides cover which is as wide as the market would allow. It is an insurance that covers each and every loss except for those specifically excluded. If the insurance company does not specifically exclude a particular loss, it is automatically deemed to be covered. This is the broadest type of property policy that can be purchased. For example, if an insurance policy does not specifically exclude losses from wind damage or from malicious damage, the insured is covered for such losses.

The advantage of all risks coverage is that the protection is so sweeping in nature that unusual events are covered. There is no need for a great deal of checking and consultation to determine if an odd occurrence is covered or not. Unless the event is specifically addressed as not being covered, a claim can be filed and paid with no delay. It is therefore priced proportionately and is higher than other types of policies. The cost of this type of insurance should be measured against the probability of a claim.

The policy is underwritten on either of the following two forms:

1) **Named Peril Form** – Basic property insurance policy forms specify coverage only for losses caused by named perils. Any loss not caused by the specified named peril is excluded from the coverage.
2) **All Risks Form** – An all risks policy form functions differently than a named peril form in that it covers losses arising from all but excluded perils. The coverage provided is much broader and all risks forms of insurance are often more desirable.

The all risks covers are designed generally to cover:

- office equipment;
- computers;
- electronic equipment;
- personal effects and jewellery inside and outside the premises;
- plant and machinery.

The happening of a loss is often vouched for by the insured's own words; so moral hazard is of paramount importance in the area of underwriting.

- Valuation certificates by accepted valuers must be furnished in the case of jewellery, expensive watches, works of art and antiques.
- Photographs and other means of identification must be taken for jewellery to assist in future claims settlement.

EXTENSIONS

Basically, the policy coverage is already very wide and extensions would be superfluous.

Some examples of common clauses that can be included in the policy are:

- Strike, Riot and Civil Commotion;
- Automatic additions/deletions;
- Reinstatement of loss;
- Temporary removal;
- Reinstatement value;
- Agreed Value Clause;
- Pairs and Sets Clause.

6.10.1 EQUIPMENT ALL RISKS INSURANCE/TAKAFUL

This policy is designed to cover heavy and moveable equipment such as tractors, forklifts, cranes and the like which are not licensed for use on public roads, against physical loss or damage.

6.10.2 BUSINESS ALL RISKS INSURANCE/TAKAFUL

The use of all risks policies in the commercial sector has become more popular with increasingly expensive and sophisticated pieces of machinery being introduced in factories and offices. This policy is designed for the commercial sector.

The advent of chip technology means that comparatively small machines are replacing larger and bulkier equipment. It is quite probable that a laptop, desktop PC or server be accidentally dropped or otherwise damaged. Such equipment is also easily portable and may regularly leave the main business premises (e.g. laptops). The small bulk conceals a high value and the owner may consider an all risks policy to be worthwhile if it assists in removing some of the uncertainty.

6.11 BURGLARY/THEFT INSURANCE/TAKAFUL

The burglary/theft insurance policy covers the insured against loss or damage to the insured property consequent upon actual, forcible and/or violent entry into or exit from the premises, OR damage to insured property or to the premises as a result of theft or any attempt thereat including armed robbery/hold-up.

The types of insured properties are:

- Any person or business organisation with property to be insured whilst kept in the premises, that requires coverage for stock-in-trade belonging to the insured;
- Goods held in trust or on commission for which the insured is responsible;
- Furniture, fixture, fittings and utensils;
- Household goods and personal effects.

If more than one location is involved, a separate sum insured needs to be declared for each location.

TYPES OF COVER AVAILABLE

There are two types of cover available under the policy:

a) **Full Value Basis** – The total value of the property/goods will be declared as the sum insured. This basis is adopted when there is a possibility of the entire property being stolen at any one time.
b) **First Loss Basis** – This basis is adopted when the insured decides that it is not possible for the entire property to be stolen at any one time. Therefore, a percentage of the total value of the risk would be taken as the sum insured. Usually, at least 20% of the total value declared is taken.

EXCLUSIONS

The main exclusions under the theft/burglary policy are, among others:

- Damage occasioned by fire or explosion;
- Theft by the insured, members of his family and employees;
- War, strike, riot, civil commotion and kindred risks;
- Radioactive contamination.

6.12 MONEY INSURANCE/TAKAFUL

The money policy covers loss of money whilst in transit and whilst kept in locked drawers, safe or strong rooms, or due to any hold-up whilst on the business premises. This policy will be required by organisations that are handling money during their course of business and need to insure the loss of money due to theft, robbery or hold-up or any attempt thereat. Money comprises cash, bank notes, currency notes, cheques, postal orders or money orders and can be insured on the basis of the following:

- Money in the premises whilst kept in locked drawers, safe or strong room;
- Money in transit means from insured premises to bank and vice versa, or from the time of receipt of money anywhere until delivered to bank or premises;
- Money in the private residence of any principal or director of the insured; and
- Other specified locations.

The policy also provides cover for:

- The cost of repair or replacement of the safe or strong room, as a result of theft or attempted theft, if these items are not specifically insured.
- Compensation in the form of a personal accident benefit to employees who may be injured during a robbery whilst accompanying or carrying money.

EXTENSIONS

The extensions under the money policy may include:

- Personal accident to the messenger or custodian;
- Armed robbery and hold-up at the insured's premises;
- Riot and Strike;
- Messenger absconding with money;
- Damage to safe and/or locked drawers.

EXCLUSIONS

The main exclusions under the policy are:

- Losses arising from fraud or dishonesty of the insured's employees;
- Shortage due to errors and omissions;
- Losses from an unattended vehicle.

6.13 FIDELITY GUARANTEE INSURANCE/TAKAFUL

Fidelity guarantee insurance provides indemnity to the employer against loss of money or property as a result of acts of fraud or dishonesty of any employee of the insured:

- during the period of insurance,
- during the uninterrupted continuance of employment of the said employee, and
- in connection with the occupation and duties of the said employee.

Cover can be arranged on all or selected employees based on the following:

- named basis with a specific guarantee amount for each employee,
- named basis with guarantee amount floating for all employees, and
- unnamed basis with guarantee amount floating for all employees in the employment of the insured.

DISCOVERY PERIOD

The policy requires the act of fraud or dishonesty to be discovered:

- during the period of insurance, or
- within six months from the expiry of the policy, or
- within six months after the death, dismissal or retirement of the employee, whichever event happens first.

STANDARD CLAUSES/EXTENSIONS

The standard clauses and extensions available are:

- Auditors and Accountants' Fees up to an agreed sum;
- Automatic Reinstatement of Guarantee Amount;
- Automatic Additions and Deletions of employees;
- Extension of discovery period (12 months) – to be granted on a selective basis;
- Payment on Account;
- Premium Adjustment;
- Loss Notification (30 days);
- Mis-description clause;
- Losses caused by unidentified employees – to be granted on a selective basis.

EXCLUSIONS

The standard exclusions found under this class of insurance are:

- If the nature of the employer's business has changed,
- If the duties and conditions of employment have changed,
- If remuneration of the employee is reduced without sanction by the company, and
- If the precautions and checks for securing accuracy of account are not observed.

Before liability can be admitted by an insurer, the insured must lodge a police report against the employee and criminal proceedings must be initiated so that the insurer will have subrogation rights against the employee concerned. All money and payments due to the employee must be held back and given to the insurer so that their losses can be reduced.

6.14 PERSONAL ACCIDENT INSURANCE/TAKAFUL

This class of insurance caters to the needs of individuals/groups and is essential to protect them from any bodily injury or death due to an accident happening anywhere in the world. The cover is for 24 hours; and is usually effected by an individual person or company. This is a benefits policy, and therefore, is not subject to the principle of indemnity. Personal accident insurance covers the insured person suffering a bodily injury that may result in death or permanent disablement caused solely and directly by violent, accidental, external and visible means, unless otherwise specifically excluded.

The intention of the policy is to provide compensation to the insured or next of kin in the event of an accident causing death or bodily injury, or temporary disablement, daily hospital income, medical expenses and funeral expenses depending on the policy coverage and benefits. The policy is usually extended to include weekly benefits up to a maximum of 104 weeks, if the insured is temporarily totally disabled due to an accident; and reduced weekly benefits if he is temporarily partially disabled from carrying out his usual duties.

Normally, the amount payable for compensation is up to the capital sum insured for cases involving death, permanent total disablement and permanent partial disablement. The definitions of disablement are as follows:

Table 6-8 ***Definitions of disablement***

Death	Bodily injury, which within 12 calendar months from the occurrence thereof, shall solely and directly cause the death of the insured person.
Permanent Total Disablement	The loss of a function of the body whereby total restoration is not possible, e.g. paralysis, loss of vision, hearing or speech.
Permanent Partial Disablement	This is a disablement which is not so severe, such as loss of a finger or toe and the compensation will be based on a percentage of the capital sum insured.
Temporary Total Disablement*	The insured is incapable to fully attend to his work and is compensated based on the number of weeks of his disability.
Temporary Partial Disablement	The insured is incapable to attend to a specific area of his normal duties and compensation will be based on the period of partial disability.
Medical Expenses	This benefit is used to defray medical expenses incurred following an accident.

**For Temporary Total Disablement and Temporary Partial Disablement, the amount payable is based on weekly compensations.*

A group personal accident insurance policy can be affected when there are more than 10 persons in any organisation. Apart from saving administration costs for the insurer, there is normally a further group discount allowed for the insured.

Personal accident insurance can be further extended to include:

- Strike and riot
- Motorcycling
- Sports

However, most personal accident insurance will exclude:

- Dangerous sports or recreation activities
- Tree felling or transportation of logs or sawn timber
- War and kindred risks
- Travelling in an aircraft as a member of the crew
- Self-injury, suicide and wilful exposure to injury, provoked assault
- Insanity or under the influence of drugs or intoxicating drinks
- Pregnancy, childbirth, miscarriage, abortion or pre-existing physical defect
- Disease or illness
- Armed or military duty
- Professional sports

6.15 LIABILITY INSURANCE/TAKAFUL

Liability insurance provides indemnity against claims made by third parties for bodily injury or property damage, and in the case of professional indemnity and directors' and officers' liability for economic or pure financial loss for which the insured may be held legally liable.

6.16 PUBLIC LIABILITY INSURANCE/TAKAFUL

Public liability insurance is designed to indemnify those who are legally liable to pay damages and legal costs for bodily injury or damage to third party properties arising out of their business operations. The public may be in contact with the firm in its offices, or the firm's employees who may be on the premises of others.

The policy has two sections.

Section I

All sums which the insured shall become legally liable to pay compensation in respect of:

- Accidental bodily injury or illness to any person;
- Accidental loss or damage to property belonging to the third party within the geographical limits.

Section II

All costs and expenses of litigation incurred with the written consent of the company in respect of a claim against the insured.

6.17 PRODUCT LIABILITY INSURANCE/TAKAFUL

This insurance indemnifies the insured against all sums which the insured becomes legally liable to pay in respect of accidental bodily injury or illness to third parties, and accidental loss of or damage to third party property, arising out of the use, misuse, consumption, or handling of insured products or goods. The insurance company will also pay on behalf of the insured, all costs and expenses incurred in defending such a claim for compensation. The insurance, however, will not cover the cost of removing, replacing or repairing defective products or loss of use.

Generally, the proposers may be classified as:

a) Manufacturers
b) Wholesalers
c) Retailers
d) Distributors

The company will indemnify the insured against all sums up to the limits specified for which the insured shall become legally liable to pay compensation for:

- Accidental bodily injury or illness to any person not being a member of the insured's family or engaged in or upon the service of the insured.
- Accidental loss or damage to property not being property belonging to or in the custody or in the control of the insured or any member of the insured's family or any person who at the time of the accident is engaged in and upon the service of the insured.
- Companies, organisations or individuals are exposed to and can be held legally liable for bodily injury, loss or damage caused by their acts or omissions to members of the public and their property.

6.18 PROFESSIONAL INDEMNITY INSURANCE/TAKAFUL

This insurance is essential to protect professionals like solicitors, accountants, registered medical practitioners, architects, engineers and others as their sale of knowledge, skills or advice, even on a casual basis, is open to judgement according to the standards of their professions.

The policy provides protection for these professionals on the conduct of their practice or their profession. The policy covers and protects them against breaches of professional duty. So these professionals must always exercise due care and skill in the execution of their practice and advice to their clients.

Clients who depend on advice from such professionals expect a reasonable degree of skill, care and knowledge. Any error, omission or alleged act of negligence could lead to expensive lawsuits and the payment of damages.

If a third party suffers loss after relying on a professional's advice, it is entitled to recover the loss from the professional who provided the advice.

TYPICAL EXCLUSIONS

- Prior known claims and/or circumstances
- Fraud and Dishonesty
- Claims by related or associated entities
- Fines and Penalties
- Goods Manufactured (not professional service)
- Duties assumed beyond reasonable/accepted professional standards
- Services performed in areas outside of expertise
- Services not performed for the firm

Table 6-9 ***Examples of claims under Professional Indemnity Insurance/Takaful***

PROFESSIONALS	CLAIMS TYPE
Engineer	Inferior design of the building, building collapses
Accountant	The client relies on accountant's incorrect tax advice and gets fined by the tax office.
Real Estate Agent	Real estate agent does not inspect client's rented property and tenants damage it.
Property Manager	Miscounts votes at property owners meeting
Marketing Consultant	Fails to advise on the best marketing/promotional method
Land or Quantity Surveyor	Mis-pegging of land, underestimating the amount of concrete required
Architect	Signs off building prematurely, the building does not meet functionality requirements
Solicitor	Error in the conveyance, fails to secure patents/protect the invention

6.19 DIRECTORS AND OFFICERS LIABILITY INSURANCE/TAKAFUL (D&O)

Over the past decade, there has been an increasing tendency for courts to hold company directors and their senior officers personally responsible for their negligence in the running of their company. Legislation has made directors liable for the behaviour of a company, and in this way, shareholders, creditors, customers, employees and others can now take action against directors as individuals.

The Directors and Officers Liability policy provide cover for:

- an indemnity to the company with respect to the costs it incurs in indemnifying a director against the successful defence of a claim; and
- an indemnity to the director in circumstances where this cannot be obtained from the company because the defence has not been successful.

Liability may arise due to lack of care or skill in the performance of duties, for example, negligent advice or misstatement, particularly in the context of a merger or takeover when failure to understand economic trends results in a poor forecast of the company's performance.

As with other liability policies, this policy pays only for damages and for defence costs in relation to claims.

The Directors and Officers Liability policy provide cover for defence costs as well as the amount of compensation for which a director may be liable to pay.

6.20 WORKMEN'S COMPENSATION INSURANCE/TAKAFUL

In accordance with the *Workmen's Compensation Act 1952*, employers are legally obligated to insure their employees, who are defined as "Workman" under a Workmen's Compensation insurance policy. However, this stipulation is no longer applicable to employees who are SOCSO members as provided under the *Employees' Social Security Act 1969*.

"Workman" is defined under the Act as any person who has entered into or works under a contract of service or of apprenticeship with an employer, whether:

a) By way of manual labour or otherwise;
b) The contract is expressed or implied or oral or in writing;
c) The remuneration is calculated by time or by work done;
d) By the day, week, month or any other longer period.

The following persons, among others, are exempted from the definition of "workman":

- Any person employed otherwise than by way of manual labour whose earnings exceed RM500 a month.
- A person whose employment is of casual nature and who is employed otherwise, other than for the purposes of the employer's trade or business, not being a person employed for the purposes of any game or recreation and engaged or paid through a club.
- A domestic servant.
- Armed and police officers.
- Any member of the family of the employer residing with him/her.

The policy indemnifies the insured with respect to his legal liability:

a) To pay compensation under the *Workmen's Compensation Act 1952* to all employees who are "workmen" in respect of death or injury due to accidents or occupational disease arising out of and in the course of employment, or
b) At Common Law.

Social Security Organisation (SOCSO)

Workmen's Compensation insurance in Malaysia used to be an important component under accident insurance. However, Workmen's Compensation insurance is fast being replaced by the Social Security Organisation (SOCSO or PERKESO), which operates an employment injury and occupational diseases insurance scheme and an invalidity pension scheme for workers earning less than RM3000 a month. The growth and expansion of SOCSO over the years have somehow diminished the importance of the Workmen's Compensation insurance provided by Malaysian non-life insurers.

6.21 FOREIGN WORKERS' COMPENSATION SCHEME

Under Section 26(2) of the *Amended Workmen's Compensation Act 1952*, it is mandatory for every employer to insure all foreign workers employed by him under an approved insurance scheme with respect to any liability that he may incur under the said Act.

Any employer who fails to insure foreign workers under the said scheme shall be held guilty of an offence and shall be liable, on conviction, to a fine not exceeding RM20,000, or to imprisonment for a term not exceeding 2 years, or both.

FOREIGN WORKERS' COMPENSATION SCHEME

Section 1

Table 6-10 ***Scope and benefits of the Foreign Workers' Compensation Scheme***

SCOPE OF COVER	BENEFITS
Accidental death due to employment injury	60 months earnings or RM18,000 whichever is lower Additional payment of RM7,000 in event of death arising out of and in the course of employment
Permanent Total Disablement	60 months earnings or RM23,000 whichever is lower
Permanent Partial Disablement	A sum of money based on the capital sum of RM23,000 calculated in accordance with the First Schedule of the *Workmen's Compensation Act*
Temporary Total/Partial Disablement	A sum of money calculated in accordance with Section 8(e) of the *Workmen's Compensation Act*
Hospitalisation and Medical Expenses	Pays in accordance with the provisions of the *Workmen's Compensation Act* (max. RM750)
Occupational Disease	According to the Second Schedule of the Act

Section 2: Repatriation Expenses

This section indemnifies the insured for the actual repatriation expenses incurred or RM4,800, whichever is the lower, in the event the insured worker dies or suffers permanent total disablement.

Section 3: Personal Accident Insurance/Takaful

(Accidental Personal Injury sustained during Off-Work Hours)

This section pays to the insured worker or his legal representative for personal injury sustained in an accident which occurs outside the working hours of the insured worker, within Malaysia.

Table 6-11 ***Scope and benefits of Personal Accident Insurance under the Foreign Workers' Compensation Scheme***

SCOPE OF COVER	BENEFITS
Accidental Death (occurring within 12 months of the accident)	Compensation sum of RM23,000
Permanent Total Disablement (occurring within 12 months of the accident)	Maximum compensation sum of RM23,000
Permanent Partial Disablement	Based on RM23,000 calculated in accordance with the First Schedule of the *Workmen's Compensation Act*
Temporary Disablement	A sum of money calculated in accordance with Section 8 (e) of the *Workmen's Compensation Act*
Medical Expenses	Pays in accordance with the provisions of the *Workmen's Compensation Act* subject to maximum RM750.

6.22 EMPLOYERS' LIABILITY INSURANCE/TAKAFUL

Legal Liability gets attached to the employer when injury or disease is caused by an accident to an employee arising out of or in the course of his employment. For those categories of employees not protected by the *Workmen's Compensation Act* or SOCSO, a liability at law still exists and the employer can obtain indemnity under the Employers' Liability policy.

The policy indemnifies the insured against liability at law for damages with respect to:

a) Accidental bodily injury or disease arising out of and in the course of employment;
b) All costs and expenses incurred with the written consent of the company.

6.23 ENGINEERING INSURANCE/TAKAFUL

Contractors' all risks insurance, erection all risks insurance, and insurances covering machinery breakdown, boilers, computers and other equipment, and loss of profits, are all included under engineering insurance. With the rapid growth of the Malaysian economy, especially in the construction, housing, manufacturing and services sectors, the demand for engineering insurance has increased manifold. However, this class of insurance still has to deal with some serious problems such as:

- Lack of local technical expertise to handle the sophistication and complexity of engineering risks;
- Limited experience of domestic insurers;
- Inadequate capacity of domestic insurers;
- Existence of very 'low' premium prices as local insurers 'under-price' their premiums due to competition.

MACHINERY BREAKDOWN INSURANCE/TAKAFUL

This policy covers sudden and unforeseen damage to the insured machinery, plant or equipment whilst at work or at rest and during cleaning, maintenance, overhauling, inspection or removal to another position within the premises. It excludes gradual damage and loss from any foreseeable cause.

The sudden and unforeseen damage elements include:

- Faulty material, design, construction and erection;
- Vibration, maladjustment and misalignment;
- Loosening of parts and ineffective lubrication;
- Excessive electrical pressure and insulation failure;
- Short circuits or arcing;
- Carelessness or lack of skill.

MACHINERY BREAKDOWN LOSS OF PROFITS INSURANCE/TAKAFUL

This policy complements the machinery breakdown (material damage) policy by providing cover for the resultant loss arising from material damage claim. While the machinery breakdown policy provides cover for material damage, the machinery breakdown loss of profits policy provides cover for the loss of profits arising from the damage covered under the machinery breakdown policy.

The policy operates in a similar manner as the fire business interruption policy. The policy provides cover against loss of gross profit, reduction in turnover and/or increase in the cost of working. It can also be arranged to cover the auditor's fees incurred to determine the amount of loss in the event of a claim.

The interest insured falls into three main categories:

1) Gross Profit;
2) Increase in Cost of Working;
3) Auditor's Fees.

BOILER AND PRESSURE VESSEL INSURANCE/TAKAFUL

This policy covers explosion or collapse of the insured plant including damage (other than fire) to the property belonging to the insured. It also includes liability at law for damages with respect to bodily injury to any person not arising out of/or in the course of employment of such person in the service of the insured and damage to third party property caused by explosion or collapse.

The policy incorporates an inspection service and provides cover against:

- damage to the insured plants;
- damage to the insured's surrounding property; and
- property damage and bodily injury to third parties caused by explosion and collapse of boilers and pressure plants.

Basically, there are only two categories of boilers:

a) steam boilers, and
b) hot water boilers.

Examples include steam receivers, steam engines, economisers, superheaters and the like, and other pressure vessels. All plants operate under some degree of pressure and are therefore subject to the risk of explosion or collapse.

Exclusions

The standard exclusions found under this class of insurance are:

- Wear and Tear;
- Failure of individual tubes in boilers of the water tube, locomotive or other multi-tubular types in superheaters or in economisers;
- Damage to property of the insured or that held by him in trust, caused by fire arising from explosion or collapse of vessels;
- Loss sustained by the stoppage of work;
- Testing of vessel exceeding the maximum permitted pressure.

6.24 ELECTRONIC EQUIPMENT/ COMPUTER INSURANCE/TAKAFUL

Electronic equipment insurance covers loss or damage to electronic equipment/computer and its data carrying media, the costs of rebuilding of the data following damage to the computer and with the option to cover business interruption arising from damage to the computer. On business interruption, the coverage could be in line with the increased cost of working, loss of revenue or loss of gross profit.

The term "electronic equipment" in the context of insurance comprises all-electric systems which generally have only a moderate power requirement. Equipment within low and medium power range includes but is not limited to:

- electronic data processing systems and equipment;
- electrical and radiation (electro-medical) equipment such as body scanners;
- communication facilities – media equipment, telephone exchanges and the like.

There are three (3) sections of cover afforded under this policy:

Section I: Material Damage/Physical Damage

This section provides cover on an all risks basis to any physical loss or damage to the items insured unless specifically excluded.

Section II: Data Media Cover

This section provides cover on a first loss basis for both the material value of the data media and the costs of reprocessing and restoring lost information due to physical loss or damage.

Section III: Increased Cost of Working/Extra Expense Cover

The section covers for expenses such as hire charges, transport charges for data media and personnel, expenses for accommodation away from the base, `out of business hours' charges or works on holidays and the like.

6.25 CONTRACTORS ALL RISK INSURANCE/TAKAFUL

Contractors all risks insurance and erection all risks insurance cater mainly to the needs of the construction industry. These policies are non-renewable and coverage is offered only for the duration of projects; and will lapse once the projects are completed.

Contractors all risks insurance is an all risks policy covering any unforeseen and sudden physical loss or damage to contract works, construction plant and equipment and/or construction machinery from any cause whilst at the site during the period of insurance unless excluded under the policy.

The policy also indemnifies the insured against third party claims with respect to bodily injury and/or property damage arising out of and in connection with the execution of the contract works insured against and occurring during the period of insurance.

There are two sections to this policy:

Section I: Material Damage

1) Item 1 – Contract Works.
2) Item 2 – Construction Plant and Machinery.
3) Item 3 – Principal's Existing Property.
4) Item 4 – Professional Fees.
5) Item 5 – Removal of Debris.

Section II: Liability to Third Parties

Provides cover for third party bodily injury and third party property damage occurring in connection with the contract works.

Duration of Cover

The duration of the cover is as follows:

- During the contract period, the cover is for all risks.
- During the maintenance period, the cover is limited to loss or damage caused by the insured in the course of remedial or maintenance works after the practical completion of the project.
- Cover for construction plant and machinery starts from the time the equipment is unloaded at the contract site until loading for dispatch from the contract site.

Maintenance Visits Cover

There are two types of maintenance visits cover:

a) Maintenance visits

The insurer's liability during the maintenance period is limited to loss or damage caused by the insured while rectifying defects for the purpose of complying with the obligations under the maintenance provision of the contract.

b) Extended maintenance

In addition to the above, this coverage includes loss or damage during the construction work.

6.26 ERECTION ALL RISKS INSURANCE/TAKAFUL (EAR)

The erection all risks policy covers loss or damage to the contract works, predominantly erection of machinery coupled with testing, including legal liability to third parties, arising out of the performance of the contract. Again, certain exclusions can be extended subject to the payment of additional premium.

The contract works usually comprise the construction, installation, testing and commissioning of plant, machinery or equipment. Briefly, the EAR insurance policy provides cover for:

a) Site erection and testing of all kinds of:
   i) individual machines, apparatus and assemblies;
   ii) complete power facilities and production plants where the above-said items are used.
b) Civil engineering work necessary for the project to be erected may be included in the cover, provided the nature of the project is predominantly that of erection work.
c) In addition, the cover may include:
   i) Machinery, plant and equipment required for erection;
   ii) Property located on the site, belonging to or held in the care, custody or control of the insured;
   iii) Expenses incurred for the clearance of debris following a loss;
   iv) Additional expenses incurred for overtime, as well as for express freight;
   v) Legal liability arising out of property damage or bodily injury suffered by third parties and occurring in connection with the erection work or near the erection site.

6.27 BONDS

Insurance companies frequently issue Bonds in addition to insurance policies. Insurers are not the only organisations that can issue bonds; any person or organisation (such as a bank) that is prepared to offer surety for someone else can issue bonds.

It is important to distinguish between a bond and an insurance policy.

- Bonds are speciality contracts issued under seal and usually involve a three-party relationship.
- Insurance policies, on the other hand, are legally called simple contracts and involve a relationship between two parties, the insured and the insurer.

In Malaysia, the majority of the bonds issued by insurance companies consist of Performance Bonds, while the other types of bonds issued include Tender Bonds, Advanced Payment Bonds, Maintenance Bonds and Supply Bonds.

The bond business is generally not written on its own without the other project insurances like Contractors All Risks and Erection All Risks insurances.

Performance Bonds are used predominantly in relation to building or engineering projects where the contractor is often required by the principal to furnish a Performance Bond to guarantee itself against the failure of the contractor to perform satisfactorily according to the terms and conditions of the contract.

Performance Bonds are bonds issued to one party of a contract as a guarantee against the failure of the other party to meet obligations specified in the contract. For example, a contractor may issue a bond to a client for whom a building is being constructed. If the contractor fails to construct the building according to the specifications laid out by the contract, the client is guaranteed compensation for any monetary loss.

As the demand for Performance Bonds has expanded following the rapid economic development in Malaysia, new business opportunities have arisen for Malaysian non-life insurers. However, the business for Performance Bonds requires considerable care by insurers and, as a result, lax underwriting may endanger the solvency of insurers. Throughout the years, several insurers have suffered substantial losses on account of their laxity and the indiscriminate issue of their Performance Bonds.

A Performance Bond, therefore, involves three parties:

a) **The Principal** – The party that awards the contract work and is likely to be indemnified under the policy if the contractor defaults or fails to perform a specific duty or to perform the duty properly;
b) **The Contractor** – A person who has accepted the contract award and is obligated to perform the works under the contract;
c) **The Surety (insurer)** – The provider, i.e. the insurer, who agrees to pay a sum of money if the contractor fails to perform his obligation under the contract with the Principal.

7

CHAPTER 7 LIFE INSURANCE PRODUCTS

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CHAPTER OBJECTIVE

To understand the different types of life insurance policies and their scope of cover.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Describe the basic features and outline the typical life insurance policy cover for various classes of insurance.*

7.1 LIFE INSURANCE PRODUCTS

Life insurance is a contract between a policy owner and the insurer, whereby the insurer agrees to pay a specific amount of money (sum assured) to the policy owner or directly to the beneficiaries on death, disability or diagnosis of a critical illness. The policy owner, in return, will pay a fixed amount of money, at regular intervals or in a lump sum (premium) into a fund managed by the insurance company.

The term 'assurance' means coverage of an event that is certain to happen. Assurance is similar to 'insurance' (and sometimes the terms are interchangeable) except that insurance protects policyholders from events that are uncertain or might happen.

In addition to securing financial protection for dependents and covering the family's daily expenses, life insurance helps beneficiaries in the following ways:

- Maintain their standard of living;
- Pay off any household debt;
- Secure children's education;
- Supplement retirement savings.

7.2 TYPES OF LIFE INSURANCE POLICIES

a) Term
b) Whole Life
c) Endowment
d) Investment-Linked
e) Life-Annuity Plan

7.2.1 TERM ASSURANCE

This is the earliest and simplest form of life insurance. As the word 'term' suggests, it is for a fixed term or period and is not permanent (unlike 'whole life'). The sum assured will be paid only on death but some term assurance policies also include critical illness and disability.

Term assurance provides the purest form of life insurance protection for the lowest premium as no benefits are payable if the life assured survives the term. There is no cash or surrender value if the policy owner decides to terminate or cancel the insurance mid-term.

There are many variations to term assurance, each with its own unique feature to cover the specific needs of the consumer.

Example

Variations to term assurance

- Guaranteed insurability option guarantees renewal without a new application or health declaration to be submitted.
- Guaranteed convertibility option guarantees conversion from term to permanent life insurance without a health declaration but subject to premium rate review on conversion.
- Decreasing term assurance is when the level of protection is reduced but the premium remains unchanged throughout the term of the policy. Such policies are appropriate for mortgage protection where the sum assured reduces as the loan is being repaid.

The advantages and drawbacks of term assurance are summarised below:

Table 7-1 ***Advantages and drawbacks of term assurance***

Advantages	Disadvantages
Lower Premiums: Term life insurance has the lowest premiums compared to other forms of life insurance. Such policies are suitable for persons with low incomes starting a job or career and require high protection for their dependents. They are also suitable for those just starting a new business and have invested substantial resources or capital in the business or a business enterprise may need to insure a 'key man' shareholder or partner whose premature death could adversely affect the sustainability of the business	**Increase in premiums** may pose particular hardship upon conversion from term to permanent as premiums depend on the age and medical condition of the policy owner.
Flexibility of application: Insurance companies are more flexible in accepting applications because of the non-permanent nature of cover, particularly younger applicants below the age of 50 years and who are in good health are not required to go through a medical examination. Policies also provide '*guaranteed insurability*' option upon renewal.	**Age restrictions** may apply for applicants above the age of 50-55 years.

7.2.2 WHOLE LIFE ASSURANCE

Whole life insurance is the purest form of permanent life insurance protection for the 'whole of life'. It is also the cheapest form of permanent protection for dependents as the policy remains in force as long as the premiums are paid. The disadvantage, however, is that the premiums have to be paid even in old age or until a claim such as critical illness or disability arises. The sum assured is payable only on death or upon the attainment of a certain age such as 85, 90 or 100 years.

In some cases, *Limited Payment Whole Life Assurance* policies are available where the sum assured is payable only on death, but premiums are payable for a limited number of years or cease upon attainment of a specified age, e.g. 60 or more. The advantage is that although premiums are higher, the 'saving element' provides for greater cash value which may come in handy in the event of an emergency when the policyholder may take a policy loan to pay off future premiums or the policy becomes fully paid up under the non-forfeiture provision (without having to pay future premiums) based on the cash value which accumulates after three (3) consecutive years of premium payment.

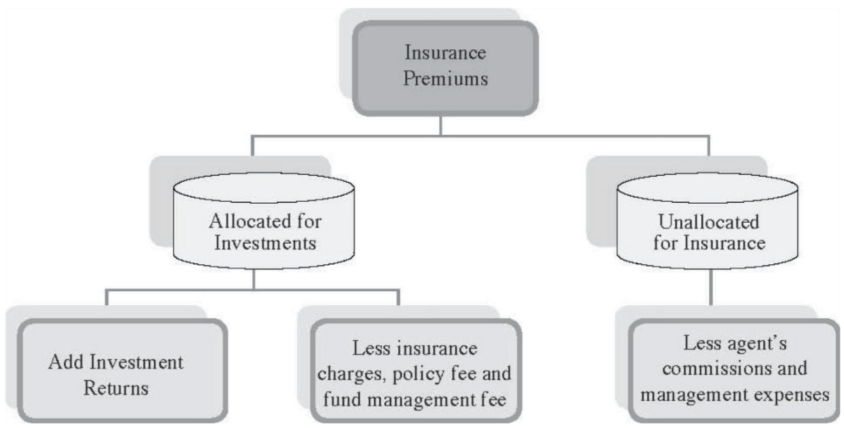
7.2.3 ENDOWMENT INSURANCE

An endowment is an insurance contract which guarantees the payment of the sum assured if the policyholder survives until the end of the policy term or on 'maturity date'. The sum assured is paid to the beneficiaries in the event of premature death. Endowment insurance, therefore, provides both protection and savings which enable the policyholder to fund children's education or save for retirement. With the acquired cash value the policy provides special privileges like non-forfeiture and paid-up policy provisions.

7.2.4 INVESTMENT-LINKED LIFE INSURANCE

Investment-Linked life insurance combines investment and protection in a single policy. The insurance company sets aside a specific fund from the premium for investment purposes. The policyholder is given the option of investing in equities (higher risk), bonds or fixed income securities (lower risk) or a combination of both. Some insurers disclose the percentage that is invested but the policyholder may not know exactly the amount of returns earned on the investments because the investment portfolio is under the management of the insurance company. Insurers deduct charges which include policy fee and fund management fee from the investment portion, and other charges such as commissions and expenses from the insurance portion.

Figure 7-1 ***How investment-linked life insurance works***



7.2.5 LIFE-ANNUITY PLAN

An annuity is a retirement fund which can be purchased for the right to a series of periodic payments at intervals of one year or less under a contract with a life insurer. Therefore, life-annuity plans differ from life insurance contracts in that an annuity does not provide for the payment of the sum assured on death, disability or critical illness. It provides a 'pension' for the lifetime of the annuitant. If death occurs during the annuity period, the premium (or the balance of it) will be paid to the beneficiary or spouse of the annuitant depending on the type of annuity purchased.

There are two types of Annuities:

a) **Immediate Annuity** – Payments begin immediately after the purchase of the annuity and continues until the remainder of the lifetime of the annuitant.
b) **Deferred Annuity** – Payment begins any time after twelve months or on the attainment of a specified age when the insurer will begin the periodic payment until the death of the annuitant. The premium for the purchase of the annuity is paid in one lump sum at entry, or periodic payments are made for a defined period (say 10 years). If death occurs during the period of 'deferment', the premiums paid are returned with or without interest

It is important to note that effective 2013, the government of Malaysia granted an 8% tax exemption on investment income in a deferred annuity fund to life insurers. This complements the existing 10-year personal tax relief of RM 3,000 on voluntary contributions to insurance annuities. Collectively, these tax incentives are expected to translate into lower insurance premiums for the benefit of policyholders.

7.3 CRITICAL ILLNESS INSURANCE

In Malaysia, critical illness insurance is sold as an optional extra or as a stand-alone life or health insurance policy. The policy makes a lump sum cash payment if the policyholder is diagnosed with one of the critical illnesses listed in the policy. The standardisation of critical illnesses provides clarity of cover at the time of claim. The policy is automatically terminated on payment of the sum assured and no further cover or sums will be payable if death occurs subsequently.

Given below is the list of the 36 Critical Illnesses applicable to policies issued in Malaysia:

Table 7-2 ***Critical Illnesses applicable to policies issued in Malaysia***
1. Stroke
2. Heart Attack
3. End Stage Kidney Failure
4. Cancer
5. Coronary Artery By-Pass Surgery
6. Other Serious Coronary Artery Disease
7. Angioplasty and Other Invasive Treatments for Major Coronary Artery Disease
8. End Stage Liver Failure
9. Fulminant Viral Hepatitis
10. Coma
11. Benign Brain Tumour
12. Occupationally Acquired Human Immunodeficiency Virus (HIV) Infection

Table 7-2 ***Critical Illnesses applicable to policies issued in Malaysia***
13. Blindness (Total Loss of Sight)
14. Deafness (Total Loss of Hearing)
15. Major Burns
16. HIV due to Blood Transfusion
17. End Stage Lung Disease
18. Encephalitis
19. Major Organ/Bone Marrow Transplant
20. Loss of Speech
21. Brain Surgery
22. Heart Valve Surgery
23. Terminal Illness
24. Bacterial Meningitis
25. Major Head Trauma
26. Chronic Aplastic Anaemia
27. Motor Neuron Disease
28. Parkinson's Disease
29. Alzheimer's Disease/ Irreversible Organic Degenerative Brain Disorders
30. Muscular Dystrophy
31. Surgery to Aorta
32. Multiple Sclerosis
33. Primary Pulmonary Arterial Hypertension
34. Medullary Cystic Disease
35. Severe Cardiomyopathy
36. Systemic Lupus Erythematosus with Lupus Nephritis

7.4 GROUP LIFE INSURANCE

Group life insurance is arranged mainly by employers (who have an insurable interest in the lives of their employees) to provide employee benefits under a master policy. The insurance may be either on a contributory (premium paid by the employee) and voluntary basis or non-contributory (premiums paid by the employer) basis.

Group insurance is also arranged for members of trade unions, associations and other entities who do not have an insurable interest in the lives of their members. In this regard, the *Financial Services Act 2013* (FSA) provides that no person shall arrange a group policy for persons in relation to whom he has no insurable interest without disclosing to each person:

- the name of the insurer;
- his relationship with the insurer;
- the conditions of the group policy, including the remuneration payable to him; and
- the premium charged by the insurer.

The FSA also provides that an insurer is liable to the person insured under a group policy if the group policy owner has no insurable interest in the life of that person and where the person has paid the premium to the group policy owner, the insurer will be liable regardless of whether the insurer has received the premium from the group policy owner. The insurer will pay the monies due to the person insured under the group policy or any person entitled to him.

7.4.1 GROUP LIFE UNDERWRITING GUIDELINES

Designed to prevent anti-selection, minimum standards for the acceptance of risks for group insurance such as the following are established:

a) The minimum number of employees in a group is usually ten (10) although special consideration may be given for non-contributory schemes, where the employer pays the premium and 100% of eligible employees are insured. In all other cases, at least 75% of eligible employees must join the plan.
b) Eligibility is confined to only permanent employees between the ages of 16 and 60 although the age limit may be extended on demand. New employees will be automatically added; while existing employees who resign, retire, or are terminated will be deleted, from the date of their recruitment or termination as the case may be.

7.5 SUPPLEMENTARY CONTRACTS

A rider is a supplementary contract offering additional benefits to a life insurance policy (which basically covers death) to include specific contingencies like accident, disability and hospitalisation.

Riders therefore supplement the basic life insurance policy with additional benefits on payment of additional premium.

a) A **Personal Accident (PA) Rider** provides payment of an additional benefit or sum insured in the event of death or disability caused by an accident. ‘Accident’ is defined as ‘bodily injury solely and directly caused by external, violent and visible means’.
b) A **Waiver of Premium Provision** waives future premium payments in the event of a disability that is deemed total and permanent for the rest of the insured’s life. The disability may result from sickness or accident; but a medical practitioner will have to certify the improbability of the insured being able to pursue his usual occupation. Nowadays, insurers grant this benefit without any extra charge if the basic cover is designed to include an appropriate risk premium for such exposure.

7.6 PARTICIPATING AND NON-PARTICIPATING CONTRACTS

A participating life policy means a life policy conferring the right to the policy owner to participate in allocations, from the assets of an insurance fund, the amount or timing of which is at the discretion of the insurer. A life insurance company is required to establish and maintain a separate insurance fund for its life insurance business relating to participating life policies.

When the assets of the insurance fund exceed the liabilities, there is a surplus. The surplus of a life insurance fund will be distributed (on the recommendation of an appointed actuary) either as a transfer out of the life insurance fund to the shareholders’ fund to pay dividends to shareholders and/or relating to participating policies as a bonus to policyholders.

Non-participating policyholders have no right to share in the divisible surplus of the insurer’s life insurance fund.

7.7 METHODS OF DISTRIBUTING SURPLUS

a) **Simple Reversionary Bonus** – The bonus is declared as a percentage of the sum assured and it is paid in the same circumstances as the original sum assured (i.e. on death or on maturity).
b) **Compound Reversionary Bonus** –The bonus allotted is in proportion to the sum assured and the bonus accumulated under the policy and the bonus is paid in the same circumstances as the original sum assured (i.e. on death or on maturity).
c) **Cash Bonus:** The bonus usually takes the form of cash distribution and is usually contingent upon the payment of the next premium. When a participating policy is surrendered (terminated), the cash value includes the cash bonus.
d) **Maturity or Terminal Bonus** –This is a method of passing on to the policyholders some of the benefits of the unrealised capital appreciation of ordinary shares and property holdings of the company. The rate of bonus declared on each valuation is valid for the period up to the next valuation only and does not create any right to bonus beyond the next valuation date.

Terminal bonus is only paid on policies resulting in claims either by maturity or death, provided the policies concerned are kept fully in force by payment of premiums until such date of claim. Where premiums are discontinued, this bonus is not payable.

Also, it is normal to prescribe a minimum period for which the policy should have been in force at the time payment becomes due, say 15 or 20 years. Any policy which has not been in force for this stipulated period may not be entitled to this bonus.

The bonus is usually expressed as a percentage of the attaching reversionary bonuses; say 25% of all existing bonuses. It can be expressed as a percentage of the basic sum assured for each year the policy has been in force.

a) **Interim Bonus** – It is normally declared at the valuation date for the policy year preceding that date i.e. in arrears. A question, therefore, arises as to what happens to policies which result in claims in between valuation dates. In these cases, bonuses are paid at an interim rate and are called interim bonuses.
   The rate of such bonuses is decided in advance and though in principle, it should be at the rate expected to be declared at the next valuation date. It usually is equal to the bonus last declared.
b) **Guaranteed Bonus** – Some life insurance policies provide a guaranteed bonus each year. Since the bonus is guaranteed, such policies are strictly non-participating policies with the sum assured increasing automatically each year at a predetermined rate.

8

CHAPTER 8 FAMILY TAKAFUL PRODUCTS

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CHAPTER OBJECTIVE

To understand the types of family takaful certificates and their scope of cover.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Describe the basic features and outline of typical family takaful certificate cover for various class of takaful.*

8.1 FAMILY TAKAFUL PRODUCTS

Family takaful provides the participant with protection and long-term savings. Participants of the scheme are provided financial benefits in case of tragedy, and also get a return on the investment. Moreover, participants have the option to choose the period of coverage and there is no penalty in case of cancellation.

8.1.1 TYPES OF COVER

Different types of family takaful protection are designed by takaful operators to meet the requirements of individuals as well as corporate participants. Generally, family takaful protection can be grouped as follows:

INDIVIDUAL FAMILY TAKAFUL (FOR INDIVIDUALS)

This group includes education, investment-linked, annuity, mortgage, and health plans. Under this type of cover, participants receive financial benefits arising from death or permanent disability, as well as long-term savings (investment), and investment profits that are distributed upon claim, maturity or early surrender.

GROUP FAMILY TAKAFUL (FOR EMPLOYERS, CLUBS, ASSOCIATIONS AND SOCIETIES)

Group education, group medical, and retirement plans fall under this category. A minimum number of participants are required to qualify as a 'group' under these plans. Participants receive protection in the form of financial benefits arising from death or permanent disability.

Examples of products falling into this category are as follows:

- Mortgage Reducing Term Takaful;
- Group Credit Takaful;
- Employee Benefits Takaful.

FAMILY TAKAFUL RIDERS

As extensions of the basic family takaful, these riders provide personal accident and disability, medical and health coverage. The various riders available are:

a) Critical Illness Takaful Rider;
b) Accidental Death and Disability Takaful Rider;
c) Waiver of Contribution Takaful Rider;
d) Payor Savings Takaful Rider;
e) Term Takaful Rider;
f) Hospital and Benefit Takaful Rider;
g) Family Income Takaful Rider.

8.1.2 INDIVIDUAL TAKAFUL PLANS

SAVINGS TAKAFUL

The savings takaful plan comprises the elements of savings and returns on investment with individual protection. This investment-type plan participates in profit, which is distributed back to participants. This plan is designed to optimise the returns on investment to participants.

Savings Takaful Cover

This plan utilises two key elements that meet or satisfy the obligation under the savings takaful:

a) Level Term Cover; and
b) Investment Account.

Salient Terms and Conditions

Table 8-1 ***Terms and conditions of savings takaful***

Benefits	• Financial compensation is paid in the event of death or total permanent disability of the participant before the certificate matures. The sum covered plus the accumulated amount in the Participants' Account (PA) are payable to the participant, participant's beneficiary or next of kin. • Upon maturity of the certificate, the participant will receive the accumulated amount in the Participants' Account (PA) and also be entitled to share the net surplus from the Participants' Special Account (PSA fund) (if any).
Contribution Amount	The contribution amount will depend on the entry age and terms of the certificate.
Partial Withdrawal	Partial withdrawals from the PA are allowed after the certificate has been in force for a minimum number of years as stipulated in the certificate. Under normal practice, withdrawals are allowed during the lifetime of the certificate subject to the takaful operator's terms and conditions. Each withdrawal must satisfy a minimum gap period between withdrawals. A nominal transaction fee is charged to the PA for each withdrawal.

Table 8-1 ***Terms and conditions of savings takaful***

Top-up Option	Top-up contribution is allowed from the commencement of the certificate. The amount of top-up shall be subject to a minimum amount set by the takaful operator. This top-up amount shall be solely allocated to the PA which will earn a profit.
Rider Attachment Option	A participant can opt for any rider contract to be attached to the basic certificate.
Better Investment Return	This plan allows the takaful operator to optimise investment returns to participants.
Exclusions	The certificate excludes pre-existing conditions.

CHILD EDUCATION TAKAFUL PLAN (CETP)

The Child Education Takaful Plan (CETP) provides protection and long-term savings to finance a child's higher education expenses. The child is provided with financial benefits if the payor suffers a setback covered under the plan. At the same time, the child can avail himself of funds required for his higher education upon maturity of the certificate. Parents also enjoy tax relief not exceeding RM 3,000 a year for child education plans and medical benefit plans.

CETP can be grouped as follows:

a) **Ordinary Child Education Takaful** – The participant and his/her child receives financial benefits arising from death or permanent disability, as well as long-term savings (education fund), and investment profits that are distributed upon claim, maturity or early surrender.

b) **Investment-Linked Child Education Takaful** – A portion of the contribution is used to buy investment units, such as units in equity or fixed income securities. In addition to the ordinary takaful protection which covers death and permanent disability, the investment units are sold upon claim, maturity or early surrender.

c) **Family Takaful Rider** –It is an extension of the basic coverage for both the participant and his/her child. The rider provides coverage against personal accident and disability, hospitalisation benefits, funeral expenses and critical illnesses.

Salient Terms and Conditions of CETP

Table 8-2 ***Terms and conditions of Child Education Takaful Plan***

Benefits	• Upon maturity and if the child survives, the benefit payable would be the agreed sum covered under the plan (given under the Shari'ah concept of *hibah*) plus the accumulated surplus sharing. However, if the CETP comes with an investment-linked feature, the child will receive the value of the investment units in addition to the agreed sum covered under the plan. Upon maturity of the certificate, the child will receive the accumulated amount in the Participants' Account (PA) and is also entitled to share the net surplus from the PSA fund, if any.

Table 8-2 *Terms and conditions of Child Education Takaful Plan*

	• Should the payor die before the CETP matures, the periodic contribution of the plan will be paid by the takaful operator on behalf of the participant until the maturity date of the plan. On the maturity date, the child will be entitled to receive the amount accumulated in the PA, surplus from the PSA and share of profits from investment (if applicable). • However, if all the contribution goes into the PSA, depending on the takaful scheme participated, the above treatment applies or the sum covered will be payable directly into an account under the child's name and managed by an appointed trustee. The sum payable is the benefit (on the basis of *hibah*) together with the accumulated surplus sharing (if any) upon maturity. A lump sum amount of the sum covered plus the accumulated amount in the PA and the PSA will be paid to participant's next of kin. • Should the child (as the participant of the plan) die, depending on the takaful scheme participated the certificate holder will receive the sum covered under the plan (given under the Shari'ah concept of *hibah*) plus the accumulated surplus sharing. Alternatively, the certificate holder may terminate the certificate for a surrender value or may nominate another child as participant.
Contribution Amount	The contribution amount depends on the entry age and term of the certificate. Waiver of Contribution: In the event of the payor's death or the payor suffering from total permanent disability (TPD) within the takaful period, all future contributions will be paid through the fund until the maturity date.
Partial Withdrawal	Partial withdrawals from the PA are allowed after the certificate has been in force for a minimum number of years as stipulated in the certificate. Under normal practice, withdrawals are allowed during the lifetime of the certificate subject to the takaful operator's terms and conditions. Each withdrawal must satisfy a minimum gap period between withdrawals. A nominal transaction fee is charged to the PA for each withdrawal.
Top-up Option	Top-up contributions are allowed from the commencement of the certificate. The amount of top-up is subject to a minimum amount set by the takaful operator. This top-up amount shall be solely allocated to the PA, which will earn profit.
Rider Attachment Option	A participant can opt for any rider contract to be attached to the basic certificate. A family takaful rider or an extension of basic coverage for both participant and child is also available. The various riders provide coverage against personal accident and disability, hospitalisation benefits, funeral expenses and critical illnesses.
Better Investment Return	This plan allows the takaful operator to optimise investment return to participants.
Exclusions	Usually, a CETP will not cover the following: • Attempted suicide or self-inflicted injury, while sane or otherwise. • Death or injury sustained due to breaching of the law. • Provoked assault. • Under the influence of drugs or alcohol. • AIDS or HIV. • Any other causes prohibited by the Shari'ah.

MORTGAGE REDUCING TERM TAKAFUL

Buying and owning a house is one of life's achievements, which essentially satisfies the basic human need for shelter. However, unexpected events may lead to loss of income or a decreased ability to fulfil financial obligations. In the event of death or Total Permanent Disability (TPD) of the participant, the participant's surviving family members may have to continue servicing the outstanding financing of the house. With a Mortgage Reducing Term Takaful (MRTT) plan, the financial burden arising from this death or TPD is covered on a long-term basis.

MRTT is a Shari'ah-compliant single contribution plan. In the event of death or TPD, the plan provides a reducing takaful benefit payable from the Risk Fund. The paid amount is expected to match the outstanding mortgage/home financing. This plan also has a special feature where the participant or his nominee is paid the excess from the accumulated Participants' Fund. The objective of the cover may not be restricted to only owning or financing a home but this is the usual understanding.

Type of Cover

It offers guaranteed benefit to settle the mortgage balance, based on the table of reducing sum covered plus a consolation benefit, payable upon death or permanent disablement (within accepted terms).

Salient Terms and Conditions

Table 8-3 ***Terms and conditions of Mortgage Reducing Term Takaful***

Benefits	• This plan provides protection to the participant on the amount financed by a financial institution. It provides a reducing sum covered, payable on the death or Total Permanent Disability (TPD) of the participant prior to the settlement of the financing. • Upon the death/TPD of the participant, the Reduced Sum Covered is payable to the mortgagee. In addition, the accumulated amount in the PA is also payable to the beneficiary. • The total permanent disability can be based on "any occupation". • Surplus sharing: Sharing of net surplus from the takaful operation (if any) as long as no claim was made during the period of takaful.
Contribution Amount	MRTT is a single contribution plan. The contribution amount correlates to the financing amount granted by financial institutions, subject to underwriting approval. The duration and amount of the home financing facility have to be equal to the amount and duration of the approved housing financing facility amount.

Table 8-3 ***Terms and conditions of Mortgage Reducing Term Takaful***

Guaranteed benefit to settle the mortgage balance	• MRTT simply ensures that the mortgage will be settled, thus securing the payment of the debt in a home financing facility. A guaranteed benefit payment (based on the table of reducing sum assured) becomes payable upon death or TPD (subject to standard exclusions on death or TPD). • **Liberal TPD Definition:** If a participant cannot perform his own or a similar occupation by training, education or experience for a period of six consecutive months, the TPD benefit becomes payable. In other MRTT plans offered, the TPD benefit only becomes payable if the participant cannot perform any work to earn a living for the rest of his lifetime. • This is equally applicable for completed properties and properties under construction (i.e. full level term coverage during the period of construction).
Riders	Various accident riders can be attached to the MRTT annual contribution.
Termination	Participating in this takaful plan is a long-term commitment. An early termination of the takaful certificate usually involves high costs and the surrender value payable may be less than the total contributions paid. This is only allowed if the said property is fully paid (early settlement of loan) or the said property has been sold and the loan settled in the process.
Exclusions	• The death or TPD benefit shall not be payable if the participant's death is due to or arising from suicide or attempted suicide and/or other causes prohibited by civil and criminal laws and the Shari'ah. • Under such circumstances, only the value of the Participants' Fund at the time of death will be payable. • No benefit shall be paid if the TPD is due to AIDS, war, an aerial activity other than as a fare-paying passenger of a scheduled air flight, or the influence of intoxicants.

8.1.3 GROUP TAKAFUL PLANS

GROUP CREDIT TAKAFUL PLAN

This type of group takaful plan is designed to provide coverage to pay off the outstanding financing facility/debt amount owing to any institution in the event of the participant's death (who is the applicant/borrower) or if the participant becomes totally and permanently disabled.

Types of Cover

There are four types of coverage under this plan depending on the method used to calculate the outstanding sum covered:

a) Level Cover
b) Flat Rate Reducing Cover
c) Compounded Rate Reducing Cover
d) Rule of 78 or Sum of Digits

Salient Terms and Conditions

Table 8-4 ***Terms and conditions of Group Credit Takaful Plan***

Benefits	• **Death Benefit:** In the event of the death of the participant within the term of the certificate, the sum covered plus the balance in the PA will be payable, in one lump sum, to the grantee. • **TPD Benefit:** In the event of TPD of the participant within the terms of the certificate, the sum covered plus the balance in the PA will be payable in one lump sum, to the grantee. • Upon death/TPD of the participant, the sum covered is payable to the grantee. In addition, the accumulated amount in the PA account is also payable. • **Maturity Benefit:** Upon maturity of the certificate, the participant will receive the accumulated amount in the PA.
Contribution Amount	There are different types of contribution payment methods. Typical plan designs may include the following : • Single Contribution • Annual Contribution

8.1.4 EMPLOYEE BENEFITS TAKAFUL

This plan is a yearly renewable plan offered to groups of people under one master certificate:

- Employer Group
- Association Group
- Other groups formed for a purpose other than participating in takaful.

Participating in employee benefits takaful helps employers or associations:

- To portray a caring image of the employer/association;
- To boost employees'/members' morale and productivity;
- To attract and retain employees/members;
- To enjoy tax deduction;
- To fulfil demand in labour negotiations.

Types of Cover

The plan offers the following types of coverage:

a) **Death Benefit** – In the event of the death of the participant within the term of the certificate, the sum covered plus the balance in the PA is payable, in one lump sum, to the certificate holder (employer, association or grouping, as the case may be).
b) **TPD Benefit –** In the event of TPD of the participant within the term of the certificate, the sum covered plus the balance in the PA is payable in one lump sum, to the grantee.
c) **Funeral Expenses –** This is payable to the next of kin upon satisfactory proof of death.

Salient Terms and Conditions

Table 8-5 ***Terms and conditions of Employee Benefits Takaful***

Eligibility	• The minimum limit for participation is subject to the takaful operator's terms and conditions but normally the limit is 10 people per group. Amounts above the non–medical limit (free cover limit) require evidence of insurability eligibility before coverage is effective. Takaful operators reserve the right to vary these requirements and to extend this limit, subject to the maximum age stated in the takaful operator's terms and conditions, as and when applicable. • **Expiry Age:** This is subject to the takaful operator's terms and conditions. • Takaful operators will allow flexibility on a case–to–case basis subject to underwriting and retakaful limits.
Information Required	1. Company Name 2. Nature of Business 3. Staff Name and IC number 4. Date of Birth 5. Gender 6. Salary (if sum covered is based on multiples of salary) 7. Sum Covered (Fixed or Multiples of Salary) 8. Claims experience for the past 3 years 9. Existing coverage, if any.

8.1.5 GROUP IMMEDIATE DEATH EXPENSES TAKAFUL

This group plan is designed to minimise risk selection and provide a common base of takaful for the covered group of participants.

Scope of Coverage

a) An employer or an organisation is the Master Contract Holder.
b) **Level Sum Cover:** One-year term coverage for a group of participants with different types of plan designs.
   i) Typical plan designs may include the following:
      - Flat Sum Cover plans, such as RM1,000 for all participants.
   ii) Sum Cover based on employment category, such as:
      - Senior Manager RM2,500
      - Manager RM2,000
      - Executive RM1,000
   iii) Sum Cover based on membership category, such as:
      - Principal Member RM2,500
      - Spouse Member RM2,000
      - Child Member RM1,000
c) **Death due to accidental or natural causes:** In the event of the death of the participant within the term of the certificate, the sum covered plus the balance in the PA is payable, in one lump sum, to the Master Participant or the participant's beneficiary or next of kin.

8.1.6 COMPREHENSIVE GROUP TAKAFUL

This plan is designed to minimise selection of risk and provide a common base of takaful for the covered group of employees (participants) with saving elements for retirement purposes. This plan is marketed or promoted on a per-unit basis, and is based on the value set by the takaful operator.

Type of Cover

Death and Total Permanent Disability (TPD) Benefit: In the event of death or TPD of the participant within the term of the certificate, the sum covered plus the accumulated amount in the PA are payable to the participant's nominees or next of kin.

Salient Terms and Conditions

Table 8-6 ***Terms and conditions of Comprehensive Group Takaful***

Benefits	• **Death Benefit:** In the event of the natural death of the participant, the sum covered plus the balance in the PSA will be payable to his beneficiary or next of kin. • In the event of accidental death, the takaful operator shall pay twice the value of the sum covered, payable to participant's beneficiary or next of kin. • **TPD Benefit:** In the event of TPD (all causes), the sum covered is payable in instalments or one lump sum, starting from the confirmation date of TPD.
Contribution Amount	Contributions are payable until maturity of the certificate.
Top-Up Contribution	Participants are allowed to top up their contribution when the certificate has been in force for one year. The amount of top-up shall be subject to a minimum of one time the monthly contribution. This top-up amount shall be solely allocated to the PA.
Riders	Other Supplementary Benefits available: • Group Hospital Benefit Takaful Rider • Group Critical Illness Takaful Rider • Group Accidental Death and Disability Takaful Rider • Group Permanent Partial Disablement Takaful Rider • Group Immediate Death Takaful Rider • Taking up the supplementary benefit will not increase the sum covered but will reduce the amount in the PA.

8.2 FAMILY TAKAFUL RIDERS

A rider is an addition to the basic certificate to confer additional benefits – sometimes requiring an additional payment. One can also combine a set of riders and append them to the main certificate. The contributions undergo an upward revision, depending on the rider or combination chosen.

One additional benefit available is the permanent accidental total/partial disability benefit. The nature of the disability determines the extent of the pay-out, over and above the basic sum assured. The pay-out is either in the form of an annuity or a lump sum payment. Even after a claim has been settled against this rider, the other certificate benefits remain.

Another connected benefit is the waiver of contribution rider. Should a permanent disability affect the participant's capacity to earn, this rider waives all future contribution payments. The term benefit rider endeavours to provide an additional sum, equivalent to a maximum of the basic sum covered should the participant die during the tenure of the certificate.

Takaful operators also offer a critical illness benefit. Should the participant be afflicted by any of the critical illnesses as listed by the takaful operator offering this rider, the participant stands to receive compensation. However, once a claim on this ground has been paid, additional claims on the same ground cannot be made at a subsequent date.

The other riders offered are the major surgical and hospitalisation benefits. The former entails a pay-out, depending on the surgical procedure. The latter covers the expenses involved in hospitalisation by paying room charges subject to a certain ceiling on both the amount and the number of days in a year that the participant can avail of the benefit.

The rider overrides any conflict with the certificate. In other words, if there is a provision in the rider that is different from the same provision that was originally mentioned in the certificate, then the rider prevails. Riders may exclude or remove coverage, which can lower the contribution; however, in most cases riders add more coverage to the existing certificate.

8.2.1 CRITICAL ILLNESS TERM RIDER

The critical illness takaful rider is an individual level takaful cover offered for protection purposes. This plan provides protection against any of the specified critical illnesses within the term of the plan.

Types of Cover

The rider provides full payment of the critical illness sum covered upon the participant being diagnosed as suffering from any critical illnesses as defined in the plan.

This plan is available in two forms:

a) **Accelerated Plan:** This rider provides a lump sum payment of the critical illness sum covered, which is advanced from the basic sum covered, upon diagnosis. A claim made under this rider reduces the sum covered in the basic plan.
b) **Additional Plan:** This rider provides a lump sum payment of the critical illness sum covered upon diagnosis. The payment made under this rider does not reduce the basic sum covered, therefore making this option more expensive compared to the accelerated plan.

Salient Terms and Conditions

Table 8-7 ***Terms and conditions of Critical Illness Takaful Rider***

Sum Covered	The participant can choose the amount of coverage up to the basic plan coverage.

Table 8-7 ***Terms and conditions of Critical Illness Takaful Rider***

Benefits	• Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA. • Upon diagnosis, the critical illness sum covered is payable subject to the following conditions: ○ The total and permanent disablement is based on "any occupation" definition. ○ The disability benefit is payable after satisfying a qualifying period (waiting period) that such disability must last for a continuous period of not less than six (6) months in duration. ○ Additional mortality and/or occupational loadings are added as appropriate to the participant's profile and TPD definition. Extra loadings shall be computed as a multiple factor to the minimum net rate. No discount whatsoever will be given as these are the minimum net rates.
Contribution Amount	The contribution will depend on the rider or the combination of plans chosen.
Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	Pre-existing conditions are excluded from this benefit. *Note: Disease diagnosed within three (3) months from the issue date of the plan or date of reinstatement is not covered by this plan.*

8.2.2 ACCIDENTAL DEATH TAKAFUL RIDER

This plan is an individual level takaful cover for protection, which can only be attached to a basic plan. This plan provides financial compensation to the participant in the event of death, Total and Permanent Disability (TPD) or Partial and Permanent Disability (PPD) due to accidental causes within the term of the certificate.

Salient Terms and Conditions

Table 8-8 ***Terms and conditions of Accidental Death Takaful Rider***

Sum Covered	The participant can choose the amount of coverage up to a certain amount above the basic plan coverage, subject to the takaful operator's terms and conditions (e.g. 5 times the basic coverage).
Benefits	• **Accidental Death Benefit** – In the event of accidental death of the participant within the term of the certificate, the sum cover plus the balance in the PSA will be payable. • **Accidental TPD Benefit** – In the event of accidental total and permanent disablement of the participant within the term of the certificate, the sum covered plus the balance in the PSA will be payable to the participant. • **Accidental PPD Benefit** – In the event of accidental partial and permanent disablement of the participant within the term of the certificate, the sum covered plus the balance in the PSA will be payable to the participant's beneficiary or next of kin. Payment of the sum covered is as per the Schedule of Indemnity.

Table 8-8 ***Terms and conditions of Accidental Death Takaful Rider***

	• **Maturity Benefits** ○ Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA. ○ Upon expiry, the outstanding contributions inclusive of returns will be distributed accordingly to participants.
Contribution Amount	The contribution depends on the rider or the combination of plans chosen.
Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	Pre-existing conditions are excluded from this benefit.

8.2.3 WAIVER OF CONTRIBUTION RIDER

The waiver of contribution takaful rider is a plan which allows for all future contribution (including attaching riders, except critical illness rider) to be waived, upon the participant being diagnosed as suffering from any of the 39 critical illnesses defined in the contract[10].

Upon diagnosis, the benefit is payable subject to the following conditions:

a) The total and permanent disablement is based on "own occupation" definition.
b) The disability benefit is payable after satisfying a qualifying period (waiting period) that such disability must last for a continuous period of not less than six (6) months in duration.
c) Pre-existing conditions are excluded from the benefit.

Salient Terms and Conditions

Table 8-9 ***Terms and conditions of Waiver Of Contribution Takaful Rider***

Sum Covered	The participant can choose the amount of coverage up to a certain amount above the basic plan coverage, subject to the takaful operator's terms and conditions (e.g. 5 times the basic coverage).
Benefits	Upon diagnosis, the benefit is payable subject to the following conditions: • The total and permanent disablement is based on "own occupation" definition. • The disability benefit is payable after satisfying a qualifying period (waiting period) that such disability must last for a continuous period of not less than six (6) months in duration. • Maturity Benefit: Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA.
Contribution Amount	The contribution will depend on the rider or the combination of plans chosen.

[10] Source: Bank Negara Malaysia 2001.

Table 8-9 ***Terms and conditions of Waiver Of Contribution Takaful Rider***

Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	Pre-existing conditions are excluded from the benefit.

8.2.4 PAYOR SAVINGS RIDER

The payor savings plan is a takaful rider plan which can only be attached to a basic plan. This plan waives all future non-outstanding contributions due under the certificate (including attaching riders) in the event of the payor's death, Total and Permanent Disability (TPD) and/or being diagnosed as suffering from any critical illnesses (as specified in the contract), prior to the certificate's maturity. This plan is uniquely designed to provide protection to the payor as well as to encourage savings/investment.

Types of Cover

a) **Death Benefit:** In the event of the death of the payor, arising from any causes, all future non-outstanding contributions due under the certificate (including attaching riders, where applicable) are waived.

b) **Total and Permanent Disability (TPD):** In the event of a total and permanent disablement of the payor, arising from any causes subject to the terms and conditions of the rider, all future non-outstanding contributions due under the certificate (including attaching riders, where applicable) are waived.

c) **Critical Illness Benefit:** In the event the payor is diagnosed as suffering from any one of the critical illnesses (as specified in the contract), all future non-outstanding contributions due under the certificate (including attaching riders, where applicable) are waived.

Salient Terms and Conditions

Table 8-10 ***Terms and conditions of Payor Savings Rider***

Sum Covered	The participant can choose the amount of coverage up to the basic sum covered.
Conditions	Upon TPD or diagnosis of critical illness of the payor, the payor benefits sum covered (PBSC) is payable subject to the following conditions: • The total and permanent disablement is based on "any occupation" definition. • The disability benefit is payable after satisfying a qualifying period (waiting period) that such disability must last for a continuous period of not less than six (6) months in duration.

Table 8-10 ***Terms and conditions of Payor Savings Rider***

Benefits	• **Death Benefit:** In the event of the death of the payor, arising from any causes, all future non-outstanding contributions due under the certificate (including attaching riders, where applicable) are waived. • **Total and Permanent Disability (TPD):** In the event of total and permanent disablement of the payor arising from all causes subject to the terms and conditions of the rider, all future non-outstanding contributions due under the certificate (including attaching riders, where applicable) are waived. • **Critical Illness Benefit:** In the event the payor is diagnosed as suffering from any one of the critical illnesses (as specified in the contract), all future non-outstanding contributions due under the certificate (including attaching riders, where applicable) are waived. • **Maturity Benefit:** Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA.
Contribution Amount	The contribution will depend on the rider or the combination of riders chosen.
Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	Pre-existing conditions are excluded from this benefit.

8.2.5 TERM TAKAFUL RIDER

The term takaful rider is a takaful rider plan which can only be attached to a basic plan. This is an individual level takaful cover with greater coverage and wider benefit scope.

Type of Cover

The plan provides financial protection in the event of death and total disablement of the participant within the term of the certificate.

Salient Terms and Conditions

Table 8-11 ***Terms and conditions of Term Takaful Rider***

Sum Covered	The participant can choose the amount of coverage up to a certain amount above the basic plan coverage subject to the takaful operator’s terms and conditions (e.g. 5 times the basic coverage).

Table 8-11 *Terms and conditions of Term Takaful Rider*

Benefits	• **Death Benefit:** In the event of the death of the participant within the term of the certificate, the term rider sum covered (TRSC) plus the balance in the PSA will be payable, in one lump sum to the participant's beneficiary. • **Total and Permanent Disability:** In the event of total and permanent disablement of the participant within the term of the certificate, the TRSC plus the balance in the PSA will be payable, in one lump sum, to the participant. • **Maturity Benefit:** Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA.
Contribution Amount	The contribution will depend on the rider or the combination of plans chosen.
Exclusions	Pre-existing conditions are excluded from this benefit.

8.2.6 HOSPITAL BENEFIT TAKAFUL RIDER

The hospital benefit takaful rider is an individual takaful rider plan which can only be attached to a basic plan. This plan provides the participant with daily cash benefit, should the participant be hospitalised due to any cause, subject to the terms and conditions of the rider.

Type of Cover

The plan provides hospitalisation benefit.

Salient Terms and Conditions

Table 8-12 *Terms and conditions of Hospital Benefit Takaful Rider*

Sum Covered	The participant can choose the amount of coverage from as low as RM10 a day to the maximum limit set by the takaful operator
Benefits	• **Hospitalisation Benefit** In the event the participant is hospitalised due to illness or injury for a minimum duration as set by the takaful operator, the hospital benefit is payable from the first day of the hospitalisation. The maximum number of days entitled is subject to the plan participated (this differs according to the plan and takaful operator).
Contribution Amount	The contribution will depend on the rider or the combination of plans chosen.
Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	• No hospitalisation benefit shall be payable unless hospitalisation takes place after the period stated in the rider certificate (this differs according to the plan and takaful operator). • This benefit excludes pre-existing conditions.

8.2.7 IMMEDIATE DEATH EXPENSES TAKAFUL RIDER

The immediate death expenses rider provides immediate financial assistance to the participant's beneficiary (ies) in the event of the death of the participant.

Type of Cover

Upon satisfactory proof of death, the participant's beneficiary (ies) or next of kin will receive the immediate death expenses benefit promptly without any other required supporting documents.

Salient Terms and Conditions

Table 8-13 ***Terms and conditions of Immediate Death Expenses Rider***

Benefits	• **Death Benefit:** In the event of the death of the participant within the term of the certificate, the immediate death expenses benefit plus the balance in the PSA will be payable to the participant's beneficiary (ies) or next of kin. • **Maturity Benefit:** Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA.
Contribution Amount	The contribution will depend on the rider or the combination of riders chosen.
Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	This benefit excludes pre-existing conditions.

8.2.8 FAMILY INCOME RIDER

The family income rider gives the participant and his family a safety net in the event he is totally and permanently disabled, or diagnosed with a critical illness within the plan period. The scheme allows a bigger portion of the PA to be utilised for investment purposes, which gives a more optimised rate of return. It also provides for more frequent allocation of investment income and a surplus to the Participants' Investment Account. Immediate reinvestment of such income and surplus will in turn provide a better total return.

Types of Cover

In the event of death, where Total Permanent Disability (TPD) or critical illness is covered under the plan, the income benefit amount will be paid to participant's nominated beneficiary or next of kin for the remainder of the certificate term.

Salient Terms and Conditions

Table 8-14 ***Terms and conditions of Family Income Rider***

Sum Covered	The participant can choose the amount of coverage from as low as RM10 per day up to a maximum limit set by the takaful operator.
Benefits	• **Death Benefit:** In the event of death arising from any of the causes covered under the plan, the income benefit amount covered will be paid to the participant's nominated beneficiary or next of kin for the remainder of the certificate term. • **Total Permanent Disability (TPD) Benefit:** In the event of TPD arising from any of the causes covered under the plan, the income benefit amount covered will be paid to the participant for the remainder of the certificate term. • **Critical Illness Benefit:** In the event that the participant is diagnosed as suffering from any of the critical illnesses covered under the plan, the income benefit amount covered will be paid for the remainder of the certificate term. • **Maturity Benefit:** Upon maturity of the certificate, the participant will receive the accumulated amount in the PSA.
Terms and Conditions	Upon TPD or diagnosis of any of the critical illnesses, the amount covered will be paid according to the following conditions: • The total and permanent disablement is based on "any occupation" definition. • The disability benefit is payable after satisfying a qualifying period (waiting period) that such disability must last for a continuous period of not less than six (6) months in duration.
Contribution Amount	The contribution will depend on the rider or the combination of riders chosen.
Better Investment Return	This takaful model allows the takaful operator to optimise investment returns to participants.
Exclusions	This benefit excludes pre-existing conditions.

9

CHAPTER 9 INSURANCE AND TAKAFUL DOCUMENTATION

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CHAPTER OBJECTIVE

To understand the documentation involved in Insurance and Takaful and the endorsement and renewal procedures followed.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Appreciate Insurance and Takaful Documentation.*
- *Recognise the salient features of the Insurance Policy/Takaful Certificate.*
- *Understand the renewal procedures, and Premium/Contribution Warranty.*

9.1 INSURANCE AND TAKAFUL DOCUMENTATION

In terms of documentation, takaful and conventional insurance may operate in a similar way except for the inclusion of *aqad* in the proposal form. The documentation is the basis of transparency and mutual consent between the takaful operator/insurer and the participant/proposer. Mutual consent is declared to be the main criterion for a lawful transaction. There could be no real consent where coercion, fraud, or injustice of any sort is used whether directly or indirectly. The contracting parties must be fully aware of their respective obligations in fulfilling their promises made on the subject matter and consideration as per the duties and rights of each party.

9.2 (a) THE INSURANCE CONTRACT

An insurance contract is an agreement or promise that is legally enforceable between two parties, i.e. the insurer and the insured whereby the insurer in return for a consideration (Premium) agrees to undertake for a stated length of time (Period of Insurance) to indemnify the insured up to an agreed amount (Sum Insured) for the value of such defined property (Property Insured) if damaged by an insured peril.

A contract of insurance (except life and personal accident insurance – on the life of a person) is a contract of indemnity and this principle is to put the insured in the same financial position as the insured was before the misfortune occurred.

The sum insured must be fixed at a level which will provide an adequate compensation at the time of loss. For insurance in real property, depreciation must always be taken into account.
The cost of insurance depends on the scope of cover, and any additional cover requires additional premium. Generally speaking, only unforeseen and fortuitous losses are insurable. Therefore, foreseeable misfortune is not insurable.

9.2 (b) THE TAKAFUL CONTRACT

As defined in section 2.5.2, a takaful contract involves the concept of tabarru' (to donate for the benefit of others as opposed to paying a premium as in conventional insurance) and mutual sharing of losses. Under this contract, participants hand over a donation of a certain portion of the takaful contribution that they agree to pay, enabling them to fulfill their obligation of mutual help and joint guarantee, should any of their fellow participants suffer a defined loss. The concept of tabarru' eliminates the uncertainty in the takaful contract.

Bank Negara Malaysia requires all takaful operators to observe application of Shariah contracts in a takaful product. The following are terms and conditions that should clearly be stipulated in all its legal documentation:

Tabarru`

a) a statement that the tabarru` takes into effect when a takaful participant contributes to the PRF;
b) a statement that the PRF is collectively owned by the pool of takaful participants;
c) a statement that a takaful operator may revise tabarru` charges subject to notification being made to takaful participants, for products with non-fixed tabarru` charges; and
d) types and amount of benefits payable from PRF;

Wakalah

a) A description of the subject matter or task to be delegated by takaful participants to a takaful operator.
b) Details of the agreed Wakalah fees as follows:
    i) types of fees and the corresponding tasks or services to be undertaken by the takaful operator;
    ii) basis in determining fees, for example as a percentage of the takaful contributions; and
    iii) terms in which fees shall be paid, for example fees are taken upfront upon payment of takaful contributions;
c) circumstances that would be deemed as mismanagement or negligence by the takaful operator and remedial action that will be undertaken accordingly;
d) a statement that the principal amount of takaful contributions placed under PIF Investment is not guaranteed by the takaful operator; and
e) conditions for dissolution of the Wakalah, which include: circumstances in which the contract will be dissolved; and treatment of the Wakalah fees in the event of a dissolution.

Mudarabah

a) profit or surplus sharing ratio; and
b) a statement that principal amount of takaful contributions placed under PIF Investment is not guaranteed by the takaful operator.

Qard for PIF Savings

a) specified amount of takaful contributions placed as Qard;
b) a statement that the principal amount of Qard is guaranteed by a takaful operator;
c) specified events for Qard payment, for example payable upon maturity of takaful certificate; and
d) a statement that any benefits from the Qard PIF Savings is based on the licensed takaful operator's discretion and not made conditional to the Qard

Hibah

a) a) amount and specified events for hibah to be given; and
b) b) a statement that any hibah from shareholders fund is at the discretion of the licensed takaful operator.

Sources: Bank Negara Malaysia Takaful Operational Framework. Applicable to: Licensed takaful operators including professional retakaful operators. Issued on: 26 June 2019 BNM/RH/PD 033-7

9.3 THE PROPOSAL FORM

To obtain an insurance coverage, the proposer needs to complete a proposal form. The proposal form is a legal binding document between the proposer and the insured. There must be an element of insurable interest and the proposer must declare all material facts when completing the proposal form. The sum insured required for the coverage must be adequate to protect the proposer against underinsurance and the application of the average clause as the policy operates on an indemnity basis (for most general insurance coverage except for personal accident and life insurance).

The proposal form can be submitted to the insurer either directly by the proposer, through an agent (who must be an authorised and licensed intermediary), or a licensed insurance broker.

Schedule 9 of the *Financial Services Act 2013* (FSA) and *Islamic Financial Services Act 2013* (IFSA) respectively states that the proposer must fully and faithfully, disclose all the facts which the proposer knows or ought to know; otherwise, the policy issued hereunder may be void. If there are any unfair practices by the insurer, the proposer may write either to the Ombudsman for Financial Services (OFS) [formerly known as Financial Mediation Bureau] or BNM's Customer Service Bureau.

Every class of insurance has its own proposal form. The purpose of a proposal form is to seek information from the person who wishes to insure, to enable the underwriter to assess the nature of the risk proposed. The proposal form also forms the basis of the insurance contract and is used together with the insurance policy and claim form in the assessment of a claim.

Insurance proposal forms vary with the type of insurance requested, with additional questions for certain types of risks. A simple proposal form contains the following information:

Table 9-1 ***Information contained in a proposal form***

Proposer's name	This information must be fully completed and clearly identify the person(s) to be insured. The name must be the same as in the National Registration Identification Card (IC) or Business Registration for business.
Address	This information is needed to enable the insurer to communicate with the insured. It may also have a bearing on the evaluation of the risk if the address also happens to be the situation of risk. The address also gives the underwriter an opportunity to understand the financial background of the insured based on the popularity of the location. This applies to high-end status type locations, also known as "rich men's locations". This information would be useful for cross-selling purposes.
Location of risk	This is important, as it will tell the underwriter where the risk is situated as this may have a bearing on the rate. Sometimes, the location of risk is not the same as the postal address. Equally important in risk assessment is ascertaining to understand the accessibility to the location, especially by the firefighting team in the event of an emergency.

Table 9-1 ***Information contained in a proposal form***

Occupation of proposer/ Occupation of risk	This is the key element in the risk assessment process and often has a direct bearing on the rating of the risk. The occupational activities of the individual or company (including subsidiaries) must be clearly stated. **Example:** In a personal accident policy, an insured listed his occupation as a Vice-President. He was rated as a Class 1 risk based on his being the Vice-President of his company. However, if the company happened to be a three-man construction company and his actual duties were those of a crane operator, then the more suitable risk classification would be either Class 3 or Class 4.
Claims history	The proposer should provide details of all previous losses relevant to the risk proposed, whether they were insured or not. Obviously, this has a bearing on the risk assessment process including the decision to accept or decline a risk.
Subject matter to be insured	The proposer must clearly state the person or property to be insured, particularly if a different person is applying for the insurance.
Sum Insured	The sum insured must be clearly stated for each type of benefit being insured (taking depreciation into account if it is a property insurance). The sum insured on the property should be based on market value to avoid underinsurance or overinsurance.
Declaration	This information is usually a statement printed on the form which expresses the proposer's desire to insure and accept a policy subject to the usual conditions of that class that warrants the truth of the answers to the questions contained in the proposal form. This is especially important for life/accident and health insurance on health questions and pre-existing condition exclusions as well as occupational considerations.
Signature	This form should be signed by the person that who proposes for insurance coverage since he or she is the only person who can fully attest to the truthfulness of the information contained in the proposal form.
Date	The date of the signature must also appear to attest to the conditions of the declarations.

Note:

- All questions in the proposal form must be fully answered by the proposer. The proposer must also disclose further information which is material to the proposed risk even though it is not asked in the proposal form. This is the disclosure of material facts, which is a requirement under all insurance policies.
- It also attempts to put on record that the proposer warrants that the statement given is true and therefore, if there is any misrepresentation or non-disclosure this will render the insurance contract void.
- The proposal form also contains a declaration that it is the basis of a contract between the proposer and the insurer.
- A completed proposal form received by the insurer does not mean that the insurer has accepted the risk.
- The insurance contract will only be enforced when the insurer has indicated in writing the acceptance of the risk proposed or by the issuance of a cover note/acceptance letter.

9.4 COVER NOTE/ E-COVER NOTE

Once the proposal form has been accepted by the insurer or his authorised agent, a cover note is issued as proof of coverage. The cover note is a temporary protection provided by the insurer as proof of the insurance contract. The cover note normally expires within 30 days from the date of issuance, during which the insurer will issue the actual policy and, in the case of motor insurance, a certificate of insurance as well. Nowadays, these cover notes are electronically issued (e-cover note). Insurers assign this authority to their agents.

With the advancement of technology, many insurers are skipping the process of issuing a cover note and instead are immediately issuing the insurance policy (for motor and simple risks). The relevant data of the subject matter and the insured's particulars are entered into their system by their agents.

9.5 INSURANCE POLICY/ TAKAFUL CERTIFICATE

An insurance policy is evidence of the contract made between the proposer and the insurer. Each policy or class of insurance has its own heading, preamble, operative clause, exceptions, conditions and warranties according to its specified requirements.

The constituent parts of the policy are as follows:

Table 9-2 ***Constituent parts of the insurance policy***

Recital clause or preamble	This refers, among other things, to: • the parties to the contract, • the proposal form and declaration as the basis of the contract, • consideration of premium payment *WHEREAS the insured by a proposal and declaration which shall be the basis of this contract and is deemed to be incorporated herein has applied to ABC Insurance Sdn. Bhd. (hereinafter called the Company) for the insurance hereinafter contained and has paid or agreed to pay the Premium as consideration for such insurance.*
Operative clause	This clause sets out the circumstances in which the insurers are liable to the insured, and it must be read in conjunction with the schedule. *NOW THIS POLICY WITNESSES that if during the period of insurance the Insured Person shall suffer Bodily Injury resulting solely and directly from accident caused by outward violent and visible means which shall directly and independently of any other cause result in Death or Disablement or Medical Expenses then the Company shall subject to the Terms Exceptions and Conditions contained herein or endorsed hereon pay compensation to the Insured or to his legal personal representatives.*
Schedule	The contents of the schedule depend upon the cover selected. The schedule gives details of the insured, period of cover and the subject matter insured.

Table 9-2 ***Constituent parts of the insurance policy***

Conditions	These are the rules which govern the application and interpretation of the contract as a whole. Breach of a condition could allow the insurer to repudiate the claim but the situation of the breach must be analysed before such action is taken.
Exceptions	This stipulates the risks that are excluded from coverage under the policy. An insurance policy cannot provide cover for everything and therefore it will carry a list of exclusions.
Attestation clause	This is worded according to the insurer's method of execution of documents and gives the policy document its legal effect by being properly attested and signed.

Normally, an insurance policy contains the following information:

- Insured's name and address which is based on the proposal form;
- The premium that is calculated by the underwriter for the risk to be insured;
- Policy number that is assigned by the insurance company;
- Date of issuance of the policy;
- The agency that brought in the business to the insurance company;
- Details regarding the subject matter;
- **Clauses:** conditions set by the insurer for the insurance coverage;
- **Warranty:** certain requirements that the insurer imposes on the insured and which must be continuously abided by;
- **Exclusions:** risk exposures that are not covered under the policy;
- Period of insurance for the insurance coverage;
- **Sum Insured:** the amount required by the insured for the insurance coverage.

9.6 CERTIFICATE OF INSURANCE/TAKAFUL

In the case of motor insurance, a certificate of insurance is issued. The *Road Transport Act 1987* has made it compulsory that every vehicle on the road should be issued a certificate of insurance as proof of insurance coverage.

- The certificate of insurance cannot be cancelled nor transferred.
- In the event of cancellation, the insured must return the original certificate of insurance.
- If lost, the insured must write officially to the insurer and get a Commissioner for Oaths to sign the declaration of the loss.

9.7 ENDORSEMENT

During the period of insurance, the policyholder may require certain changes to be made on the policy. This can be done through the issuance of an endorsement. Among the normally issued endorsements are the ones relating to:

- changes to the subject matter;
- increase or decrease in the sum insured;
- transfer of interest;
- change in the insured's details e.g. address;
- cancellation of the policy.

9.8 RENEWAL

9.8.1 RENEWAL PROCEDURES

Generally, an insurance policy is an annual policy that expires at 12 midnight. If there were no claims made under the policy, or even if there were claims made during the policy period but within an acceptable level, the insurer may invite the policyholder to renew the insurance for another year. The renewal can be done in any of the following ways:

- On the same terms as previously issued, and/or
- The sum insured can be revised depending on the market value, and/or
- Certain amendments can be made depending on the risk exposure, and/or
- Extra benefits can be included on renewal, and/or
- Certain amendments can be made depending on the claims experience.

If the risk is unacceptable, the insurer can decide not to send out a renewal notice or decline the renewal altogether. When a renewal notice is sent out and the insured accepts the terms, the insurer will issue a renewal policy or renewal certificate.

9.8.2 RENEWAL NOTICE

Insurers normally send reminders to the insured by issuing a renewal notice 60 days in advance of the policy expiry date. The purpose of the renewal notice is to notify the insured that the policy is about to expire, including reminding the insured of any changes the insured needs to make on the renewal policy. The renewal notice will contain the following information:

- Insured's details;
- Subject matter;
- Sum insured, coverage type and any additional coverage;
- Excess, if any;
- Premium details.

The insured has to review the sum insured to ensure its adequacy in line with the market value. Most insurers issue renewal notices with the old sum insured and the insured needs to reduce or increase the sum insured after taking into consideration the latest market value.

Sometimes, insurance companies may use a renewal certificate to renew the insurance instead of issuing a new insurance policy. The particulars stated on a renewal certificate are brief and they usually refer to the previous policy unless stated otherwise.

9.9 ASSUMPTION OF RISK AND PAYMENT OF PREMIUM/CONTRIBUTION

The *Financial Services Act 2013*, para 84 states:

> *(1) No licensed insurer shall assume any risk in respect of such description of policy as may be prescribed by the Bank unless and until the premium payable is received by the licensed insurer in such manner and within such time as may be prescribed by the Bank.*
>
> *(2) Where the premium payable under subsection (1) is received by a person on behalf of a licensed insurer, the receipt shall be deemed to be receipt by the licensed insurer for the purpose of that subsection and the onus of proving that the premium was received by a person who was not authorised to receive the premium shall lie on the licensed insurer.*

The *Islamic Financial Services Act*, para 96 carries similar description for Takaful.

The present practice is: all life insurance products are on *"cash before cover"* as per (1) and is applicable to general motor insurance also.

The Regulations relating to CBC requirements prohibit a licensed general insurer from assuming any risks in respect of motor policies until the premium payable under the policy is received by the insurer.

9.10 MOTOR CASH BEFORE COVER REGULATION

> *No cover can be granted until the premium has been paid in accordance with the Regulations issued under the Section. Any person who fails to comply with this Section shall be guilty of an offence and shall on conviction be liable to a fine not exceeding RM500,000.*

This simply means no motor cover note shall be issued without the payment of the premium.

The insurance industry, through PIAM, has also initiated self-regulating (industry regulations).

The Cash before Cover regulation also applies to individual personal accident insurance and travel insurance.

9.11 PREMIUM/CONTRIBUTION WARRANTY

General insurance companies are required to enforce a 60-day Premium Warranty clause on most types of insurance covers except for motor insurance policies, travel insurance, marine hull insurance and insurance bonds.

Under the Premium Warranty clause, the insured is required to pay the premiums charged for the insurance within 60 days from the effective date of insurance cover (the insurance policy, cover note and/or renewal certificates shows the effective date of cover). If the premium is not paid by the 60th day, the insurance cover will be automatically cancelled from the 61st day.

This clause is an expressed condition of the policy, and in the event of a claim after the 61st day, shall render the policy invalid.

> *PREMIUM WARRANTY: It is a fundamental and absolute special condition of this contract of insurance that the premium due must be paid and received of by the Company within sixty (60) days from the inception date of this policy/endorsement/renewal certificate. If this condition is not complied with then this contract is automatically cancelled and the Company shall be entitled to the pro rata premium on the period they have been at risk, Where the premium payable pursuant to this warranty is received by an authorised agent of the Company, the payment shall be deemed to be received by the Company for the purposes of this warranty and the onus of proving that the premium payable was received by a person, including an insurance agent, who was not authorised to receive such premium shall lie on the Company. Subject otherwise to the terms and conditions of this policy.*

These two regulations have brought about better credit controls of outstanding premiums and it has enhanced the financial position of insurance companies.

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CHAPTER 10 CLAIMS PROCEDURES AND PROCESS

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CHAPTER OBJECTIVE

To understand the general procedures in place when a claim is made and comprehend the notification process and right of action.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Appreciate the general procedure followed for claims.*
- *Recognise the reasons for delay in the claims settlement process.*
- *Understand loss and its particulars in detail.*
- *Explain the different types of claims and the procedures used for each.*

10.1 INTRODUCTION

The objective of takaful/insurance is to assist participants/policy owners who might suffer a loss, damage or a catastrophe. An insurance policy/takaful certificate document comes with a promise to pay or compensate participants/policy owners in the event the insured/participant suffers a misfortune coverable under the policy. The takaful/insurance contract is essential to justify the amount of the compensation payment that is given to the participant/policy owner who suffers a loss. This is also essential for the calculation of the compensation, since it involves utilisation of the takaful/insurance fund, which involves others' money. It is therefore important to ascertain that payment in takaful/insurance is made to compensate for a real loss or burden sustained by the participant/policy owner due to an incident defined in the certificate or cover. However, the details and procedures as stated in this chapter are put in place as guidelines and a control mechanism to protect the fund, and are thus beneficial to the participants/policy owners as well as takaful operators/insurance companies.

Takaful/insurance is all about the payment of claims, and the ultimate test of a responsible and efficient insurer/takaful operator is of the:

- promptness and fairness with which it compensates the economic loss of the insured;
- effectiveness when indemnifying third party claims.

Therefore, it is incumbent upon insurers/takaful operators, as administrators and managers of the scheme, to act promptly and judiciously when handling claims intimated by the insured/participants. Insurers/takaful operators have set certain minimum standards among themselves with respect to claims handling where the objective is to achieve equitable and fast claims processing. Insurers and takaful operators have to ensure that all claims are valid and genuine so that the insured/participants are comfortable and satisfied that their funds are being well-managed.

10.2 GENERAL PROCEDURE FOR CLAIMS

Claims are generally divided into 2 categories i.e. general insurance/takaful claims and life insurance/family takaful claims. General insurance/takaful claims are further categorised as motor claims, property damage claims, liability claims and casualty or personal accident claims. While the procedure for life insurance/family takaful claims is quite straightforward, it is more complex for general insurance/takaful claims.

10.2.1 CONDITIONS FOR A VALID CLAIM

To ascertain the validity of a claim, insurers/takaful operators set a standard procedure. The following questions must be answered before the insurer/takaful operator can go ahead with the claims settlement process:

- Is the policy/certificate in force?
- Has the premium/contribution been paid?
- Is the loss caused by the insured peril?
- Is the subject matter affected by the loss the same as that insured under the policy/certificate?
- Has notice of loss been given without undue delay?
- Did the claim happen within the waiting period?
- Does the loss fall under any exclusion?

10.2.2 COMMON REASONS FOR DELAY IN CLAIMS SETTLEMENT

Delay in the settlement of claims has been a cause for concern. This has resulted in poor customer perception of insurers/takaful operators and problems for beneficiaries.

Table 10-1 ***Common reasons for delay in claims settlement***

Reasons for Delay	Measures to Overcome the Reasons for Delay
Incomplete / insufficient documentation	Understanding the process flow and documents required for every claim is important.
Inability to determine the contract status	Agents/brokers must have a thorough knowledge of the policy/scheme sold by them and its status so as to advise the client accordingly.
Delayed response from the claimant	Upon receiving any request from the claims department, the client is expected to act on the request without waiting for further reminders to be issued.
Claim being outside the scope of cover	The distribution channel must be knowledgeable of all the benefits provided in the insurance/takaful and ensure proper advice is given to the policyholder/participant or claimant.

Table 10-1 ***Common reasons for delay in claims settlement***

Outstanding premium/contribution still due to insurer/takaful operator	The employee, agent, broker and client must be made to understand that life insurance/family takaful plans are Cash Before Cover (CBC). Therefore, no claim is payable if the premium/contribution is not paid in full.
Mindset of Claim Servicing	Claims services have too long been mislabelled as a back–office operation. It is very much a front-office operation, a critical function in the day-to-day activity of the company. It is the most important customer touch point for the insurance/takaful business. What is being sold are effectively claims services. Responsive claims services are one of the many competitive advantages that differentiate one company/operator from another. Quantitative benchmarking must be in place to determine the efficiency and the turnaround time in settling a claim.

10.3 NOTIFICATION OF CLAIMS

The notification of claims is the responsibility of the insured. However, it is also common practice that an agent or an insurance broker issues the notification on behalf of the insured, especially for large commercial businesses. The notification of claims is governed by the policy conditions that may vary for different types of insurance. However, the following general conditions are applicable for all general insurance cases:

a) Immediate notification;
b) Claims notification process;
c) Particulars of the loss;
d) Right of action;
e) Contribution.

10.3.1 IMMEDIATE NOTIFICATION

The insured has a duty to notify the insurer of an incident, or legal proceedings which may lead to a claim immediately or within a specified time limit. The insured must not admit liability, or answer any letters without the written permission of the insurer. In liability claims, the insured must send any writs, summons or other legal documents or letters to the insurer as soon as they are received. This is to make sure the insurer is able to take control of the claim as early as possible.

10.3.2 CLAIMS NOTIFICATION PROCESS

Claims can be notified either by a phone call, email, short messaging service (SMS), fax, and any electronic platform or in person. This is normally done by the claimant or the claimant’s appointed intermediary, or the workshop handling the repairs.

- This notification is then reviewed by the claims personnel to ensure there is a valid cover at the time of loss or accident.
- The claims personnel will also check whether policy premium has been paid by the claimant.
- Once this has been done, the claims personnel will register the claim in their system and set a provisional reserve. It is most important to get critical information regarding the loss at the earliest so that accurate reserving can be done. If there is insufficient information, the claims personnel will set a reserve based on the average reserving practices approved and recommended by Bank Negara Malaysia.
- For cases where the reserve amount exceeds the claims personnel's limit of authority, the file will be sent to a more senior staff having a higher authority limit than the reserve amount. This is also applicable to branches, where cases with higher reserves are sent to the Head Office for the registration process and subsequent review and settlement.

10.3.3 PARTICULARS OF THE LOSS

The insured must provide the insurer with all documentation required in the evaluation and settlement process. The insured must provide the description of the loss, the circumstances surrounding it, and any supporting evidence such as receipts, invoices, stock records, plan and specifications.

10.3.4 RIGHT OF ACTION

The insured must immediately do whatever is deemed necessary to mitigate losses at the site where the loss occurred. The insured must also help the insurer to take legal action against any third party that might be liable for the claims in accordance with the principle of subrogation.

10.3.5 CONTRIBUTION

The insured must provide all the details of any other policies that cover the same subject matter and against the same peril. This is in line with the principle of contribution where all insurers will have to compensate the insured their portion of the claims proportionately.

10.4 LIFE ASSURANCE/ FAMILY TAKAFUL CLAIMS

For life insurance, there are primarily two types of claims which are initiated after:

a) a pre-specified date, e.g. the maturity of a savings or endowment policy, or
b) a significant, unscheduled event involving the policyholder occurs, e.g. death or accident or illness.

With maturities and other pre-specified events, the insurer tends to take the lead, initiating communication with the insured.

In the event of death claims, it is important to have certain mechanisms in force to ensure that the insurer receives proper proof of death of the life insured, such as the death certificate, and that the proper legal recipients of any proceeds of a claim are identified taking into account any will or assignment of the proceeds which may have been made. This procedure may involve the use of the courts, e.g. the obtaining of probate on a will.

10.5 ACCEPTANCE OF LIABILITY

There is a significant difference between notification and acceptance of liability by the insurer. On notification, the first thing the insurer does is to establish whether the loss is valid by asking a range of questions:

- Was the policy in force at the time of loss or damage?
- Is the sum insured adequate?
- Are there any conditions, terms, exclusions which would render the claim not payable?
- Has the insured complied with the conditions of the policy such as mitigating the loss, risk management, prevention strategies and compliance with legal requirements?
- Does the person making the claim have a right to claim under the policy?
- Are there any other policies covering the same subject matter and perils at the time of loss?

Only after the insurer accepts that there is a valid claim would they start on the claims resolution.

10.6 CLAIMS REGISTRATION

The registration process begins immediately after the claim has been registered and a valid claim number has been assigned to the said case. The insurer's automated system assigns a claim number to the claim once the notification process is done. The registration process takes into consideration the following:

- Assignment of a claim number.
- Setting up of a reserve amount for the claim.
- Documentation whereby the claims personnel start to gather relevant documents pertaining to the claim. They liaise with the claimant, workshop, and intermediary to ensure completion of the documentation process.
- For cases involving co-insurance, reinsurance (both facultative and treaty), XOL and/or treaty reinsurers, notification is done through the Preliminary Advice of Loss.
- In the event the claim amount exceeds the Treaty limits, the XOL Treaty is notified by official means.
- Once the claim has been registered, an acknowledgement letter is sent out within 7 days, upon registration, to comply with the BNM JPI /GPI 14 (revised) Guidelines.

10.7 PROCEDURES USED IN SETTLING CLAIMS

A majority of the claims is handled by the Claims Department. The insurer, in its efforts, tries to control claims as early as possible so that it can:

- ensure that appropriate damage mitigation actions are initiated as soon as possible;
- appoint appropriate experts to manage and assess claims as soon as possible; and
- select appropriate and cost-effective solutions to control the severity of claims.

It is important that the insured provides sufficient information to the insurer to estimate the loss. This is normally done using the claim form and attaching supporting documentation to quantify the amount, such as purchase receipts or valuations. For life insurance and personal accident insurance, the compensation value is normally defined under the policy. For liability insurance, the value depends on the judgement of the courts.

Claims management involves various aspects of claims, including the use external expertise for areas in which insurers do not have a specialist to evaluate the loss. Some of the important aspects of claims management include:

- proper and accurate provision of reserves;
- ensuring and handling claims in accordance with and within the set authority limits;
- ensuring each claim that is registered is accounted for and has proper reserves;
- counter-checking and/or random checking to ensure transparency in claims handling;
- setting key result areas and key performance indicators;
- timely correspondence with the claimant (insured), intermediaries and management;
- minimising and lowering claims costs either by review of part prices, workshop estimates, loss adjusters' reports, or using internal adjusters wherever possible, or setting a minimum claim limit for the appointment of an external loss adjuster;
- using the services of special investigation units to understand theft trends and legitimate claims;
- constantly reviewing and implementing salvage recovery within authority limits;
- constant reviewing of active and non-active claim files;
- constant implementation of plans and timely review of claims data in establishing the financial impact of claims;
- continuous training of staff to increase their level of technical competence; and
- continuous review and implementation of management action plans to combat loss ratio and identify areas for improvement.

10.8 CLAIMS DOCUMENTATION

In addition to the claim form or accident report form, other relevant documents must also be submitted by the claimant to substantiate the claim. The documents may vary with the type of insurance coverage and the nature of the claim.

10.8.1 CRUCIAL INFORMATION FOR CLAIMS PROCESSING

For accurate claims settlement, it is crucial that claims personnel have details of the circumstances of the accident or loss, and relevant supporting documents regarding the circumstances of the accident or loss.

All claims should be notified as soon as possible for immediate action. Some examples of documents required for claims processing for the different classes of insurance are as follows:

Fire Insurance/Takaful

- Photographs, if any;
- Technician's Report, where applicable;
- Purchase invoices, repair bills, sales record and other relevant documents;
- Police Report;
- Fire Brigade report.

Burglary Insurance/Takaful

- Police Report;
- Photographs, if any;
- Purchase invoices, repair bills, sales record and other relevant documents.

Public Liability Insurance/Takaful (Third Party Liability Claims)

- Third Party official letter;
- Photographs or sketch plan of the scene of the incident;
- Specialist report, where applicable;
- Medical report and/or death certificate and post-mortem report where bodily injuries are sustained;
- Discharge receipt and indemnity form or court order;
- Repair bills for third party property damage;
- Police report.

Personal Accident Insurance/Takaful (Bodily Injury Claims)

- Medical leave certificate;
- Medical report;
- Salary slips;
- Photographs of injuries, where applicable.

Personal Accident (Death Claims)

- Post-mortem report;
- Death Certificate;
- Burial Certificate;

- Police Report;
- Letter of employment;
- Certified copy of identity card.

Motor Claims (Own Damage)

- Police Report;
- Certified copy of registration card;
- Certified copy of driving licence and identity card of the driver;
- Repairer's estimate, where applicable;
- Adjuster's report on circumstances of accident and recommendation of the cost of repairs;
- Repairer's final bill for payment;
- Discharge Voucher.

Motor Claims (Total Loss or Theft Claims)

- Original registration card;
- Duly signed JPJ K3 Forms (2 copies);
- Keys;
- Statement from the finance company on the outstanding amount due to them, where applicable;
- A release letter from hire purchase company, where applicable;
- Certified copy of Certificate of Business Registration, if company-registered vehicle;
- Valuation letter from franchise dealers or adjuster's confirmation of market value;
- Acceptance and duly signed discharge voucher;
- JPJ TM-AB form (copy) duly signed and authenticated by JPJ/Sessions Court Judge/Magistrate or Consular of Malaysian Embassy.

Windscreen Claims

- Photographs of damage;
- Police report, if applicable;
- Original repair bill and receipt.

Third Party Vehicle Damage Claims

- Third party official letter;
- Police report;
- Police sketch plan and photographs;
- Certified copy of third-party driver's identity card and driving licence;
- Copy of third-party policy;
- Certified copy of vehicle registration card;
- Adjuster's recommendation based on report forwarded by the third party;
- Knock-for-Knock confirmation and approval, where applicable;
- Third party discharge voucher.

Third Party Bodily Injury Claims

- Third-party official letter;
- Police report;
- Police sketch plan and photographs;
- Certified copy of third-party driver's identity card and driving licence, where applicable;
- Adjuster's report;
- Specialist report, where applicable;
- Medical report and/or death certificate and post-mortem report, where applicable;
- Discharge receipt and indemnity form or court order.

10.9 USE OF LOSS ADJUSTERS

The claims personnel handling claims have to decide whether to assign a loss adjuster for the loss. In some companies, internal loss adjusters are employed to work on cases that are small in nature. This is done in line with the objective of reducing the claims cost. Only in cases where the amount exceeds certain set limits would a loss adjuster be assigned to review the legitimacy of the claims and to recommend an estimated loss amount. Normally, loss adjusters are appointed as soon as a file is registered, irrespective of the sum insured. This is done to take advantage of the loss adjuster's experience in investigating the claims.

The loss adjuster plays an important role in gathering relevant documents from the insured, financier, investigating officer and any other party who could help to finalise the loss adjustment and complete the loss adjuster's report for the insurer's consideration. Nowadays, most assignments of adjusters are done using the electronic media or platform.

The role of a loss adjuster is to:

- independently review the extent of the loss;
- check the validity of cover;
- check the adequacy of the sum insured at the time of loss;
- mitigate and minimise the extent of the loss;
- assess the quantum of the loss;
- submit the loss adjuster's report.

A loss adjuster is a:

- trained expert in the class of insurance which involves a survey or investigation;
- person who can highlight any red flag on suspicious claims or claims that are out of pattern;
- person who can highlight any changes in any industry that requires insurers to re-evaluate their position towards the said industry;
- person who acts as a settlement agent for the insurer based on the mandate approved by the insurer;
- person who will assist the policyholder to mitigate the loss;
- person who can advise the insurer on risk improvements that need to be undertaken;
- person who can track down witnesses and get them to attend court.

If neither the loss adjuster nor the claims staff has the expert knowledge to deal with some aspects of a claim, the case is referred to a pool of experts such as:

- Forensic scientists to establish the cause of a fire,
- Medical practitioners to determine the seriousness of a claimed medical condition and whether or not it is genuine,
- Accident reconstruction experts to establish the speed and path of vehicles involved in a road accident,
- Structural engineers to determine whether a building should be demolished rather than repaired.
- Art and jewellery valuers to establish whether the amount claimed is reasonable or not.

Use of the experts stated above may be expensive, and therefore the insurer must be careful and engage such experts only when really required, based on its own discretion. Engaging experts in the right manner helps the insurer benefit by way of a huge reduction in the claims cost.

PART C

11

CHAPTER 11 INTRODUCTION TO SHARI'AH

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CHAPTER OBJECTIVE

To learn the objectives of Shari'ah, and the Islamic judgements on actions.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Appreciate the Concept of Ad-Deen and the underlying contracts with reference to takaful.*

11.1 OBJECTIVES OF SHARI'AH

The Shari'ah, or Islamic law, is the "centrepiece and backbone of the religion of Islam". It is the entire body of Islamic law, and the term literally means "the road to watering place." It is based on the Qur'an, which Muslims believe is the revealed book of Allah (swt) given to Muhammad (saw) over 23 years, ending in 632 CE, and the Sunnah, or example of the Prophet Muhammad (saw) whom Muslims believe was divinely guided. The Hadith, which are sayings and actions of Prophet Muhammad (saw) and provide information about the Sunnah, were recorded in the two centuries after Muhammad's (saw) death in authenticated Hadith collections.

The Shari'ah prescribes Muslim behaviour in every aspect of life from private matters between the individual and Allah to relationships with others from the family or the widest community. The Shari'ah contains categories and subjects of Islamic law called the branches of *fiqh* (literally, "understanding"). They include Islamic worship, family relations, inheritance, commerce, property law, civil (tort) law, criminal law, administration, taxation, the constitution, international relations, war and ethics, and other categories. The Shari'ah, therefore, provides the ultimate criteria for judgment on every aspect of one's individual and social life.

The main objective of the Shari'ah is to ensure that human life is based on *ma'ruf* (good) and to cleanse it of *munkar* (evils). The word *ma'ruf* denotes all the qualities that have always been universally accepted as 'good' by human conscience, and conversely, the word *munkar* denotes all those qualities that have always been condemned by human nature as evil.

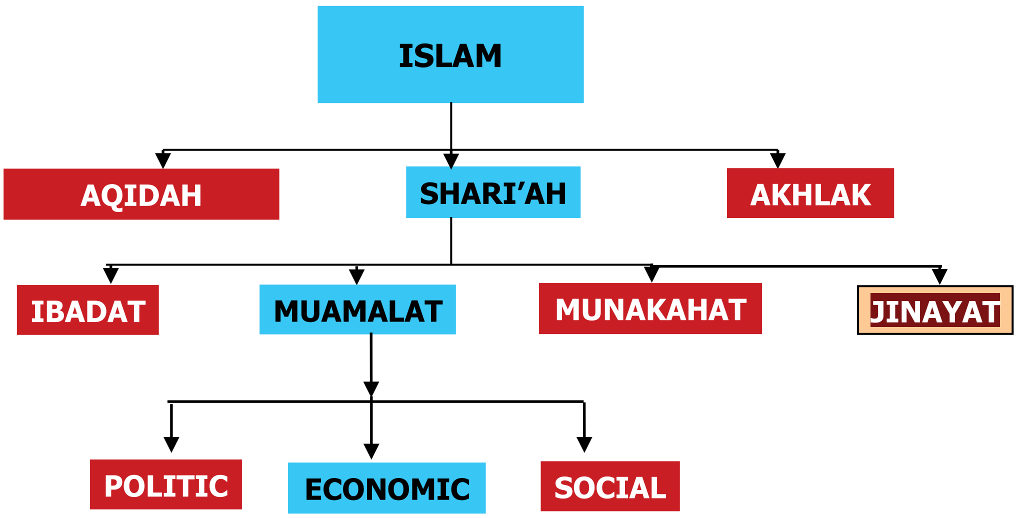
11.2 THE CONCEPT OF *AD-DEEN*

Broken down to its bare elements, Islam comprises *Aqidah* (a set of beliefs), the Shari'ah (a set of laws) and *Akhlak* (a code of moralities).

- ***Aqidah*** means a set of beliefs. From the Islamic point of view, *aqidah* means a strong belief in Allah (swt), His Prophets, the hereafter, the angels, the holy books and predestination.
- ***Shari'ah*** or Islamic law is also known as *fiqh* or Islamic jurisprudence. *Fiqh* deals with the observance of rituals, morals and social legislation in Islam. Branches of *fiqh* include *Ibadat, Muamalat, Munakahat* and *Jinayat*.

  - ***Fiqh Ibadat:*** The rules of ritual purification, prayer, pilgrimage, fasting, zakat (almsgiving of which payment made annually under Islamic law on certain kinds of property and used for charitable and religious purposes, one of the Five Pillars of Islam), jihad and some other forms of worship are dealt with under this heading. Most of these rules deal with the rights owed to Allah (swt) by the individual alone or by the community as a whole.
  - ***Fiqh Muamalat:*** This area deals with property, contracts, business organisation, security of debts and insolvency, pre-emption, gifts, bequests and *waqf* (voluntary, permanent, the irrevocable dedication of a portion of one's wealth – in cash or kind – to Allah).
  - ***Fiqh Munakahat/Usrah:*** This area deals with marriage, divorce, inheritance, guardianship and related matters. This is similar to the conventional version known as the personal law.
  - ***Fiqh Jinayat:*** This area deals with major offences like unlawful sexual intercourse (*zina*), theft (*sariqah*), robbery, piracy and brigandage (*hirabah*), and other matters collectively known as *hudud* laws.
- ***Akhlaq*** is a term referring to the practice of virtue, morality and manners in Islamic theology and philosophy (*falsafah*). It refers to one's disposition, nature, temper, ethics, morals or character (of a person). *Akhlaq* covers all aspects of a Muslim's behaviour, attitude and work ethics which influence his or her acts.

Figure 11-1 ***Elements of Islam***



11.3 ISLAMIC JUDGMENTS ON ACTIONS

In Islam, all actions or acts must be guided by five judgments classified as follows:

Table 11-1 ***Islamic judgments on actions***

Wajib **(Obligatory)**	The term "*wajib*" refers to acts the performance of which is obligatory. Examples are performing *solat* (the obligatory prayers) and fasting in the month of Ramadhan. In its technical sense, these are acts whose commission is demanded by the Lawgiver (Allah swt) in certain and binding terms.
Mandub **(Recommended)**	*Mandub* is defined as a demand by Allah (swt) for the commission of an act without making it binding and without assigning any blame for its omission. The rule for *mandub* is that for doing so there is a reward (*thawab*) for the doer, while omitting it entails no penalty.
Haram **(Prohibited)**	*Haram* is defined as that the omission of which is required by Allah (swt) in binding and certain terms. An example of a prohibited act (*haram*) is the misappropriation of another's wealth.
Makruh **(Reprehensible or Disapproved)**	*Makruh* is defined as that, the omission of which is demanded by Allah (swt) in non–binding terms. An example of the reprehensible act (*makruh*) is a debt which is not documented (unrecorded).
Mubah **(Permissible)**	The *mubah* or permissible act is one in which Allah (swt) has granted a choice of commission or omission, without blame or praise for omission or commission. According to this principle, all contracts and transactions are permissible, unless there is evidence indicating otherwise.

11.3.1 SOURCES OF THE SHARI'AH

Primary Sources

Table 11-2 ***Primary sources of the Shari'ah***

	Primary Sources	**Description**
1)	**The Qur'an**	The Qur'an is the very word of Allah (swt) revealed to the Holy Prophet (saw) for the benefit of all mankind. It is a divine revelation and is the first and main source of Islamic law and to Muslims, the absolute authority in deciding legality and every legal obligation. The Qur'an is a comprehensive and indivisible guide and must be accepted and implemented in its entirety.
2)	**Sunnah**	Sunnah literally means "method". The Sunnah comprises what the Prophet (saw) said (*qaulan*), did/actions (*fi'lan*) and agreed (*taqrir)*. All the actions and words of the Holy Prophet (saw) were inspirations from Allah (swt) and did not originate from the Prophet's (saw) own desires. The Sunnah should be distinguished from the Hadith, which means sayings or speeches. It refers to the sayings of Prophet Muhammad (saw). In addition, the Hadith in this sense is synonymous with the Sunnah which is wider in meaning.

Secondary Sources

Table 11-3 *Secondary sources of the Shari'ah*

	Secondary Sources	Description
1)	***Ijma'* (Consensus)**	*Ijma'* is the juristic consensus of opinion of the *mujtahid* imams (classical Islamic jurists) at a particular time after the death of the Prophet (saw) regarding the legal position of a matter or problem. In its application, *ijma'* is an agreement of the *mujtahidin* (Islamic jurists) in the event the ruling being sought is not found in either of the main sources i.e. the Qur'an and the Sunnah. All the *mujtahidin* must reach a consensus on a juridical opinion at the time an issue arises.
2)	***Qiyas* (Analogy)**	*Qiyas* means to equate the legal position of a matter that has no ruling in the Qur'an and the Sunnah to one that has due to the *illat* (underlying cause or reason) of the ruling. In other words, the *mujtahidin* refer back to the Qur'an and the Sunnah and make analogical reasoning between a new matter that has no ruling with the one that already has a ruling. Literally, it is the extension of a Shari'ah value from the original case to a new case, because the new case has the same effective cause as the original case.
3)	***Maslahah* (Public Interest)**	*Maslahah* (consideration of public interest) is a concept in traditional Islamic law, invoked to prohibit or permit something on the basis of whether or not it serves the public's benefit or welfare. The concept is related to that of *istislah.* While the meaning of *maslahah* is 'consideration of public interest', the meaning of *istislah* is 'to seek the best public interest' which is in line with the aims and objectives of the Shari'ah.
4)	***'Urf* (Custom)**	*'Urf* is a term referring to the custom or 'knowledge' of a given society, leading to change in the *fiqh.* *`Urf* is a source of Shari'ah ruling where there are no explicit primary texts in the Qur'an and the Sunnah specifying the ruling. *`Urf* can also specify something generally established in the Qur'an and the Sunnah.
5)	***Istishab* (Presumption of Continuity)**	*Istishab* means the presumption of existence or non-existence of facts. It can be used in the absence of other proofs (*dalil). Istishab* relates to the sense that the past accompanies the present without any interruption or change.
6)	***Istihsan* (Juristic Preference)**	*Istihsan* means juristic "preference". Muslim scholars may use it to express their preference for particular judgments in Islamic law over other possibilities. It is one of the principles of legal thought underlying personal interpretation or *ijtihad*.

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CHAPTER 12 BASIC *MUAMALAT*

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CHAPTER OBJECTIVE

To learn the basic principles of *Muamalat*, and the concept of contract with respect to the same.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Recognise the basic principles of Muamalat and the prohibitions laid therein.*
- *Understand the contracts that support Takaful.*

12.1 INTRODUCTION TO *MUAMALAT*

The literal meaning of the term *Muamalat* (plural of *Muamalah*) is 'the transactions' while its technical idea is any form of mutual dealings held between people to solve their everyday needs, especially in matters relating to trade and commerce. *Muamalat* is a social relationship which consists of various economic and non-economic activities.

12.1.1 BASIC PRINCIPLES OF *MUAMALAT*

Among the basic principles that play a role in forming Shari'ah rulings in *Muamalat* are:

- **Freedom of Contract**
  - Muslims are free to put conditions in their agreements except those that prohibit something which is permissible or permits something which is prohibited.
- **Permissibility as Original Status of Matters**
  - The status of all matters other than rituals is permissible until evidence is given that a certain matter is prohibited.
- **Custom is of Force**
  - A *fiqh* legal maxim states that "Custom is of Force". In many Shari'ah commercial contracts, many things become permissible following customs.

12.1.2 PROHIBITIONS IN *MUAMALAT*

SHARIAH RESOLUTION ON INSURANCE

The concept of conventional insurance has not achieved full agreement from scholars whether it is permissible (halal) or prohibited (haram). Since conventional insurance as it is being practiced now did not exist during the Prophet's time, 'ijtihad' is used to determine whether it is permissible or otherwise.

FATWAS ON PROHIBITION OF INSURANCE

1. ***The National Fatwa Committee***

Fatwa Committee the National Council for Islamic Religious Affairs Malaysia, at its meeting on 15 June 1972 discussed and deliberated on the issue of Life Insurance, resolved that Life Insurance provided by present-day insurance companies are a business transaction which is voidable because it contradicts the Islamic business principles in viewthat the contract contains the elements of Gharar, Maisir and Riba.

As such from the Shariah point of view, insurance is "haram". A committee known as "Badan Petugas Khas" was set up by the government in 1982 to study the feasibility of setting up Islamic Insurance in Malaysia. The "Badan Petugas Khas" concluded that conventional insurance contract is fasid, however, the objection is not against the concept of insurance per se but against the existence of certain weaknesses in the insurance contract. The Takaful Act 1984 was enacted and subsequently the Malaysia's first takaful company was formed in 1984.

2. *The Islamic Fiqh Academy, OIC*

The Islamic Fiqh Academy, emanating from the Organization of Islamic Conference, meeting in its Second Session in Jeddah, Kingdom of Saudi Arabia, from 10 to 16 Rabiul Thani, 1406 H. (corresponding to 22 - 28 December 1985).

After reviewing the presentations made by the participating scholars during the Session on the subject of `Insurance and re-insurance', and after discussing the same, and after closely examining all types and forms of insurance and deeply examining the basic principles upon which they are founded and their goal and objectives, and having looked into what has been issued by the Fiqh Academies and other edifying institutions in this regard; resolved that:

- the Commercial Insurance Contract, with a fixed periodical premium, which is commonly used by commercial insurance companies, is a contract which contains major element of risks, which voids the contract and therefore, is prohibited (Haram) according to the Shariah.
- The alternative contract which conforms to the principles of Islamic dealings is the contract of co-operative insurance, which is founded on the basis of charity and co-operation. Similarly, is the case of re - insurance based on the principles of co - operative insurance.
- The Academy invites the Muslims countries to work on establishing co -operative insurance institutions and co -operative entities for the re -insurance.

3. *Gharar ("Uncertainty") in insurance practices:*

a) Both parties to the insurance contract do not know exactly what their obligations and responsibilities are to each other, neither the insurer nor the insured knows the outcome of the contract

b) The insured does not know the amount of compensation he is likely to get in case of an accident or a peril as the insured does not know if there will be compensation as the outcome of the contract is not known

c) The insurer does not know when the peril will occur.

d) There is no equity in insurance in that the insured has got to pay the premium but if the peril insured against does not happen, the insured is not paid anything at all.

e) Insurance is a promise to pay compensation which is sometimes fulfilled and sometimes not. Uncertainty in the results of the exchange as at the point the contract is made, the result of the exchange is still uncertain.

4. *Riba ("Usury") in insurance practices*

a) Insurance company invest the premium in interest bearing investment.

b) Insurance company pay interest on their product.

c) Insurance company consider futur e interest when calculating the premium.

d) Insurance contracts contain usury, promise to pay more than the premium paid.

e) Interest charged on late payment of premium. f) Interest charged on policy loan.

5. *Maisir (Gambling) in Insurance Contract:*

a) Insured could receive huge amount of money, without equivalent input.

b) Paying premium without getting any amount in return.

c) Insurer loses if there are too many claimants. d) Premium collected exceeds the claims, Insurers could make huge profits.

Source:

http://takafuleexam.com/e- content/TBEA/content/29175407IBFIM_Part_A/ chapter_A4/page_05.html

12.1.3 THE CONCEPT OF CONTRACT IN MUAMALAT

Islamic scholar, Barbati defined *aqad* or contract in his *kitab* (book) *Inayah 'ala Fath al-Qadri* as follows:

> *"Legal relationship created by the conjunction of two declarations, from which flow legal consequences with regard to the subject matter."*

The literal meaning of *aqad* is "join" or "tie". The English word for *aqad* is "contract". *Contract* can also be defined as being *"an expression of the matching between a positive proposal made by one of the contractors and the acceptance of the other contractor in a way which has an impact on the subject of the contract"*.

A contract must consist of:

Table 12-1 *Elements of Aqad*

Aqidain (The Parties to the Contract)	It is a condition of a valid contract that the parties possess capacity. Capacity is a quality which makes a person qualified for acquiring rights and undertaking duties and responsibilities.
Sighah (Contractual Agreement)	*Sighah* is the form of the contract consisting of *ijab* and *qabul* (offer and acceptance). The offer made by the first party to the contract is called *ijab* because it gives and confirms the freedom of acceptance to the second party.
Ma'aqud alaih (Subject Matter)	This involves the subject matter and price. These are conditions to be taken into consideration according to Islamic jurisprudence for the subject of the contract has to be legal, in existence and identified.

12.2 UNDERLYING CONTRACTS THAT SUPPORT TAKAFUL BUSINESS

Table 12-2 ***Underlying contracts that support takaful business***

	UNDERLYING CONTRACT	EXAMPLE
1)	The nature of the ***Mudarabah*** (profit sharing) practice is that it is a financial contract whereby one party called *rabbu al-mal* provides funds to the other party called *mudharib* who undertakes to manage the fund through investment or trade and generates profits, in which both the *rabbu al-mal* and also the *mudharib* share in the profit in a pre-agreed proportion. *Mudarabah* is the primary doctrine which is adopted by the takaful operator as an alternative to the doctrine of *riba*.	For example, participants in the takaful operation contribute a sum of money to the takaful fund in which the participants are the *rabbu al-mal*, while the takaful operator is the *mudharib* who agrees to manage the fund with the view of making profit which both the participants and the operator share proportionately, no matter a defined risk has run on the subject matter or not.
2)	***Musharakah*** is the idea of *shirkah* (partnership), which has been adopted by contemporary Islamic financial institutions. *Musharakah* is an agreement between two or more parties to operate a particular business in which all parties contribute to the capital with the view of making a legitimate profit. In other words, in *Musharakah* dealing, the parties involved herein share the liability, the profit and also the loss, according to their agreement.	In the takaful contract the participating shareholders mutually agree to contribute a sum of money to initiate the takaful business. This mutual agreement among the participating shareholders with the view of making a profit is called *musharakah*.
3)	***Tabarru'*** means gift or donation which is given by one in favour of someone without seeking any consideration. *Tabarru'* is made based on the general principles of contract, in which the person makes it and binds himself unilaterally by offering something valuable for the noble cause of the welfare of others	• In a takaful operation the element of the contract of *tabarru'* is directly involved. For example, participants' contributions are credited mainly into two accounts: Participants' Account (PA) and Participants' Special Account (PSA). • The amount credited to the PSA is regarded as *tabarru'* which is managed by the takaful operator to provide a security for others who deserve it. In other words, the participants are unilaterally bound to pay the amount into the PSA from which they are not entitled to seek any benefit for themselves.
4)	***Ju'alah*** is a kind of contract of hiring for services, in which one party undertakes to pay a specified amount of money for rendering a defined service in accordance with the terms negotiated between them. An example of a contract of *al-ju'alah* is that a person offers to another to pay some amount of money, if the other can offer a particular service for the former's benefit.	Takaful operation certainly involves the element of the contract of *ju'alah*. As evidence, the participants in the operation make an offer to the operator that they will pay a sum amount of contributions to the takaful fund. Basically the takaful operator will be paid according to their performance in managing the fund, not for providing security against the defined risk.

Table 12-2 ***Underlying contracts that support takaful business***

5)	***Kafalah*** is a contract of surety, bailment, or guarantee. By virtue of Article 612 of the *Mejelle,* a contract of *al-kafalah* is one in which a person adds to himself a responsibility or liability on behalf of another person in respect of demand for something. In this provision, adding the liability or responsibility means a guarantee, which is determined by the principles of contract relating to *kafalah*.	*Kafalah* operation is a kind of doctrine which also involves the element of the contract of takaful. This is because in takaful practice, the participants contribute to the takaful fund by a mutual agreement with the other participants in the scheme. Therefore, all the participants are mutually guaranteeing each other.
6)	***Wakalah*** is a contract of agency, in which a person delegates his business to another and substitutes the other in his place. The person delegated is called *wakil* (agent) whose fundamental obligation is to provide his skill towards the betterment of the assigned job. Thus both the principal and the agent are equally bound to each other under a contract of *wakalah*.	The participants appoint the takaful operator as an agent to manage their account i.e. to invest, reserve, and for underwriting purpose.

PART D

13

CHAPTER 13 INSURANCE AND TAKAFUL BROKING

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CHAPTER OBJECTIVE

To understand the role of a broker and how proper advice and practices matter to the insurer/ takaful operator and the insured/participant.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Recognise the role of a broker as a distribution channel.*
- *Understand the market conduct regulation for Takaful.*
- *Appreciate the basic responsibilities of Takaful Intermediaries.*
- *Learn the proper advice and practices, and the guidelines related to Takaful.*

13.1 INTRODUCTION

Insurance and takaful brokers and insurance and takaful broking businesses are regulated and licensed by Bank Negara Malaysia (BNM) under the *Financial Services Act 2013* (FSA) and the *Islamic Financial Services Act 2013* (IFSA).

The *Islamic Financial Services Act 2013* (IFSA) states that no person shall act or hold himself out as a takaful broker unless he is the holder of a licence as a takaful broker, granted by the Minister and is a member of an association of takaful brokers approved by the Minister.

Insurance & takaful brokers and insurance & takaful broking businesses have to comply with the following:

- All brokers in Malaysia must be licensed. The licence is renewable annually.
- Any misconduct of a broker can lead to the license being revoked or cancelled.
- The business operations of brokers are regulated by the *Financial Services Act 2013* (FSA) and the *Islamic Financial Services Act 2013* (IFSA).
- The minimum capital required is RM500,000.
- Professional indemnity insurance/takaful of not less than RM500,000 is required.
- Quarterly reports are required to be submitted to Bank Negara on premiums transacted according to the class of takaful and brokerage earned for direct takaful and retakaful.
- A separate licence is not required if a broker places retakaful in addition to direct takaful.

The broker represents the insured in the solicitation, negotiation or procurement of contracts of insurance/takaful, and has a duty to the insured to match the insured's insurance/takaful needs with insurance/takaful products that meet these needs. An insurance/takaful broker thus acts as an intermediary between clients and insurance companies and/or takaful operators. Clients may be either individuals or commercial businesses and organisations.

Brokers use their in-depth knowledge of risks and the insurance and takaful markets to find and arrange suitable insurance policies and/or takaful schemes where appropriate. Insurance and/or takaful brokers, unlike tied agents, are independent and offer products from more than one insurer/operator to ensure that their clients get the best deal. The broker represents the insured whereas an insurance/takaful agent represents the insurance company/takaful operator.

Professional insurance and takaful brokers thus deal with many insurers and takaful operators, and have access to different types of policies and certificates of coverage wordings. They act for their clients and help them to decide what risks to insure or participate, what types of cover are best and how much it should cost. They can also consider if there are other ways that the risk can be transferred, such as self-insurance and other non-traditional insurance and takaful products/instruments. In many cases the insurance and/or takaful broker is the most valuable in the event of a claim.

Insurance and/or takaful brokers have a fiduciary duty to act in the best interests of their clients and provide sound practical advice which is independent of any insurance company's/takaful operator's influence, similar to a proficient and qualified accountant or lawyer who provides impartial professional advice, based on years of training, education and experience.

While it is not mandatory to have either a university degree or college diploma to pursue this career, nevertheless, to become a broker you must first be gainfully employed at an insurance and/or takaful broking firm and have successfully completed the Basic Certificate Course in Insurance and Takaful Broking examination jointly conducted by The Malaysian Insurance Institute (MII) and Islamic Banking and Finance Institute Malaysia (IBFIM) and/or the Basic Certificate of Takaful Broking examination or any other certification programme recognised by BNM and the Malaysian Insurance and Takaful Brokers Association (MITBA).

Training and professional development is a never-ending process. Courses to enhance the professionalism and increase the knowledge of insurance and takaful industry staff are offered through MII, IBFIM, and other approved professional insurance and takaful education and training institutions worldwide.

13.2 BROKER AS A DISTRIBUTION CHANNEL

Table 13-1 ***Broker as a distribution channel***

Broker as :	Remarks	
a) Intermediary	• Must be a business licensed by the Insurance and Takaful Regulator i.e. Bank Negara Malaysia. • Minimum required paid-up capital is RM500, 000.	Can be sued for professional negligence if wrong advice is provided.
b) Agent of the Insured/ Participant	Must • obtain insurance and/or takaful qualification, • have practical experience, professional indemnity takaful and/or insurance, • be a registered member of MITBA.	

Table 13-1 ***Broker as a distribution channel***

c) Consultant providing Professional Advice on Insurance and/or Takaful	• Acts on behalf of, and fulfills many other functions/requirements of clients (insured). • Sources for competitive rates, and provides advice, recommends necessary coverage/needs and administers and arranges insured clients' insurance/takaful programme. • Collects premium/contribution on behalf of insurer/takaful operator. • Assists and advises clients in the event of claims. • Earns brokerage and/or professional fees.

13.2.1 ROLE OF A BROKER

Broking is a hands-on role requiring a combination of technical knowledge, and business, communication, people and practical skills.

Typical work activities depend largely on the size and nature of the employer and the scale of the business. In a large company, a broker may specialise in a core area. In a small firm, a broker could be involved in most functions, including new business development, and act as placing broker and claims broker.

The broker's tasks typically involve:

- gathering information from clients, assessing their insurance/takaful needs and risk profile;
- building and maintaining on-going relationships with clients including scheduling and attending meetings and understanding the nature of the clients' businesses or lives;
- foreseeing clients' insurance/takaful needs, such as policy renewals;
- researching insurance companies'/takaful operators' policies and negotiating with underwriters to find the most suitable insurance/takaful for clients at the best price;
- arranging for specialised types of insurance/takaful cover in complex cases (This may involve preparing reports for insurance/takaful underwriters and surveyors and negotiating with insurers/takaful operators);
- advising clients on risk management, and helping to devise new ways to mitigate risks, for example, by adding security measures such as fencing, surveillance cameras or lighting to commercial properties to reduce the likelihood of break-ins;
- renewing or amending existing policies;
- advising clients whether and when they need to make a claim on their policies/certificates;
- marketing and acquiring new clients;
- developing relationships with underwriters, surveyors, photographers, structural engineers and other professionals;
- carrying out administrative tasks such as dealing with paperwork, correspondence, keeping detailed records;
- winning accounts against competitors;

- keeping up with changes in the insurance/takaful market and in the clients' industries;
- collecting insurance premiums/takaful contributions, and processing accounts.

Additionally, the broker should act as an advocate on behalf of their client with respect to issues surrounding the reporting of potential claims to insurers/takaful operators, and in the settlement of claims under the insurance/certificate coverage.

Table 13-2 ***The role of a broker***

Understanding the Client and the Client's Business	Ideally, the broker should have internal resources with direct experience in the client's business. In the case of law firm clients, the broker should have internal resources that have either worked in law firms, or have dealt so exclusively with law firm clients so as to have gained an intimate knowledge of them over a period of years.
Advising on the Insurance/Takaful Required	In-depth knowledge of the client's business naturally leads to a more thoughtful assessment of the client's insurance/takaful needs. The broker should be able to provide useful advice with respect to appropriate levels of coverage, and should identify any particular issues for the firm that may require specific insurance/takaful solutions.

Negotiating Terms and Conditions	The largest portion of the overall service factor in any twelve–month period tends to be the negotiation of terms and conditions with the insurance and takaful market. This process includes, among other things, the following:
	• Development of underwriting submissions
	• Negotiations with insurance and takaful markets
	• Analysis of alternatives obtained to include:
	    ○ Wording comparisons, financial comparisons and discussions with the client firm as to the subjective and objective advantages and disadvantages of each option.
	    ○ In certain circumstances, the broker may assist the client in drafting or customising policy/certificate language for specific insurance/takaful requirements.

Servicing and Administration of Insurance/Takaful Contracts	This function entails streamlining, to the greatest extent possible, the application process and assisting the firm through it, helping the firm gather documentation for the underwriters and, ultimately, packaging materials for appropriate presentation to the underwriters. In addition, the broker assists in the final execution of the transaction and maintains copies of the relevant documentation.
Monitoring Changes in the Marketplace	An experienced broker follows changes in the marketplace and keeps clients informed about changes in insurance/takaful availability and trends, new coverage issues or claim developments that may affect the firm, developments in policy/certificate language, and the activities of comparable firms with respect to insurance and takaful issues. The broker will provide periodic market updates, carrier and product updates, and risk management updates to communicate this information to the firm.
Providing Risk Management Advice	Advice in the area of risk management is provided on both formal and informal bases. The broker should take a proactive approach in offering services to their clients, but should leave the utilisation of such services to the discretion of each client firm.

Table 13-2 ***The role of a broker***

Claims and Coverage Issues Advocacy	Often the broker can act as an intermediary and advocate on behalf of the client with respect to claims situations. Where coverage issues require clarification, the broker can act as an intermediary and attempt to utilise its leverage with the underwriter to effect an interpretation favourable to the client. The broker may also assist in selecting counsel, creating settlement strategies, and collecting fees and loss settlements.

13.3 MARKET CONDUCT REGULATION FOR TAKAFUL INTERMEDIARIES

13.3.1 MARKET CONDUCT SUPERVISION AND ENFORCEMENT

Bank Negara Malaysia supervises the market conduct practices of financial service providers and initiates remedial or enforcement actions for any breach of market conduct requirements.

13.3.2 MINIMUM STANDARDS OF SERVICE

Takaful intermediaries are required to comply with the specified minimum standards of service set by Bank Negara Malaysia, the Malaysian Takaful Association (MTA) and Malaysian Insurance and Takaful Brokers Association (MITBA). The minimum standards of service ensure that takaful intermediaries conduct their business with a high degree of responsibility and professionalism.

Takaful brokers:

- are governed by the Client's Charter on Code of Good Business Practice, and Code of Ethics and Conduct drawn up by MITBA; and
- must adhere to the rules and regulations specified in the *Islamic Financial Services Act 2013* (IFSA).

In addition, a takaful broker's senior management and board of directors must be 'fit and proper' and its employees are required to pass the Basic Certificate Course in Insurance and Takaful Broking.

13.4 RESPONSIBILITIES OF TAKAFUL INTERMEDIARIES IN PROMOTING TAKAFUL

13.4.1 BASIC CONDUCT OF TAKAFUL INTERMEDIARIES

A takaful broker must:

- be a member of MITBA and be licensed by Bank Negara Malaysia. The licence is subject to annual review.
- exhibit good knowledge of the products and services offered by the takaful operator and the market, generally;
- understand customers' needs and assist them in the right choice of takaful products and services;
- explain clearly the nature of information required in the proposal form and also the importance of understanding material facts;

- explain clearly the terms and conditions of the proposed takaful contract to ensure that customers fully understand the takaful products being considered;
- draw attention to any restrictions and exclusions applicable under the proposed takaful contract;
- follow up and provide continuous service, such as renewal and provide updates on relevant new products; and
- provide assistance in making claims against the takaful operator.

13.4.2 PROPER ADVICE AND PRACTICES

ACCOUNTING, AUDITING OF ISLAMIC FINANCIAL INSTITUTIONS (AAOIFI) SHARI'AH STANDARDS

AAOIFI provides guidelines on the following Shari'ah matters for a takaful operation:

- Shari'ah Standard 26 – Takaful;
- Shari'ah Standard 41 – Retakaful.

AAOIFI ACCOUNTING, AUDITING AND GOVERNANCE STANDARDS

AAOIFI guidelines on auditing, accounting and governance for takaful operations are:

- FAS 12 – General Presentation and Disclosure in the Financial Statements of Takaful Operators.
- FAS 13 – Disclosure of Bases for Determining and Allocating Surplus or Deficit for Takaful Operators.
- FAS 14 – Investment of Funds.
- FAS 15 – Provisions and Reserves in Takaful Operators.
- FAS 19 – Contributions in Takaful Operators.

ISLAMIC FINANCIAL SERVICES BOARD (IFSB)

IFSB Standards with respect to takaful operation are:

- IFSB 8 – Guiding Principles on Governance for Takaful Undertakings.

Scope and Coverage

The Guiding Principles shall apply to all takaful operations or undertakings, irrespective of their legal status. They also apply to all operational models adopted by takaful undertakings. Takaful undertakings are encouraged to undertake continuous adoption of best practices, consistent with the objectives set out by these Guiding Principles, and to explain this by making relevant disclosures. Their aim should be to implement governance structures and processes so as to be on a par with, if not better than, their conventional counterparts.

The Guiding Principles have been formulated for direct general and family takaful undertakings. The applicability to retakaful operators is limited because their operating concepts differ in important respects. For example, the participants are direct takaful operators (as cedants) rather than members of the public, so the governance issues that arise are somewhat different. A thorough study of business models of retakaful operators is required before good governance structures and processes can be recommended. Nevertheless, retakaful operators and supervisory authorities are encouraged to consider the Guiding Principles in strengthening their governance framework, and to apply them where appropriate.

Takaful operators must duly observe their fundamental obligations towards the participants, particularly with regard to compliance with Shari`ah rules and principles. Shari`ah governance must remain an inherent feature since the *raison d'être* of takaful is the offering of a protection product that complies with the requirements of the Shari`ah. Therefore, the Guiding Principles shall refer to and adapt the recommendations from the IFSB's Guiding Principles on Shari`ah Governance System with regard to all Shari`ah governance issues arising in takaful operators.

In the case of the disclosure requirements to promote good practice of transparency in takaful, the Guiding Principles recommend the adoption of the "comply or explain" approach. This approach would enable the implementation of these Guiding Principles to accommodate the diversity of legal frameworks in the respective jurisdictions in which takaful operates. Furthermore, it would facilitate the adoption of a governance framework that is commensurate with and proportionate to the size, complexity and nature of each takaful.

IFSB 11 – STANDARD ON SOLVENCY REQUIREMENTS FOR TAKAFUL (ISLAMIC INSURANCE) UNDERTAKINGS

Main Objectives

The overriding objective of this document is to set forth key principles on the solvency requirements for takaful. It is built on the following premises and objectives:

- To increase the likelihood that a takaful would be able to meet all its contractual obligations and commitments;
- To act as an early warning system for regulatory intervention and immediate corrective action, taking into account that the supervisory authority may sometimes have access only to incomplete information, and that even corrective actions may take time to generate the desired impact;
- To provide a buffer so that even if takaful participants were to suffer a loss in the event of failure of a takaful, the impact can be limited or reduced, especially the systemic effects; and
- To foster confidence amongst the general public, in particular the participants, in the financial stability of the takaful industry.

Scope of Application

This Standard is applicable to all takaful and retakaful. However, supervisory authorities may, at their discretion, extend the applicability to takaful "window" operations that fall within their jurisdictions. (In Malaysia "window" operation is not permitted by the regulator.)

This Standard is focused on the takaful as a single entity and the issues of group-wide supervision are not covered in this Standard. The International Association of Insurance Supervisors is actively developing standards and guidance in this area. The IFSB will monitor these developments and may make further proposals in the future.

This Standard places particular emphasis on the solvency requirements for a Takaful Participants' Risk Fund (PRF) or Participants' Special Account (PSA) which is subject to underwriting and the contributions to which are made on the basis of a *tabarru'* commitment. When considering the solvency requirements for those forms of family takaful business which have a savings element in a segregated account, called the Participants' Investment Fund (PIF) or Participant's Account (PA), normally this latter fund is not taken into account in assessing whether the solvency requirements of a takaful are met as there is typically no recourse to certain surplus amounts in individual PIFs or PAs in order to meet a deficiency in a PRF or PSA. In addition, a PIF or PA is typically a pure investment fund, and the related investment risks are fully borne by takaful participants with no need for capital backing from the takaful operator in the form of a *qard* facility.

13.5 RELATED GUIDELINES FOR TAKAFUL

Bank Negara Malaysia (Central Bank of Malaysia), under the power of the Director-General of Takaful, provides additional guidelines for takaful operation covering underwriting, investment, and filing of returns and statistical data (TOSS – Takaful Operators Statistical Submission). BNM also has the monitoring function of undertaking an audit on takaful operators.

As for Accounting Standards, the Malaysian Accounting Standards Board (MASB) has issued accounting standards for the operation of general takaful and family takaful businesses. These standards are in line with the International Financial Reporting Standards which are applicable for entities of public interest.

The *Malaysian Income Tax Act 1967* provides taxing guidelines for takaful operators that manage takaful funds. There are some uncertain treatments of certain items as the taxing provisions refer to conventional operations whereas takaful operates on a different basis.

14

CHAPTER 14 BROKING BUSINESS OPERATIONS

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CHAPTER OBJECTIVE

To learn the responsibilities of a broker towards the client, and the principles and standards that a broker should follow.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Appreciate the broking services and business processes.*
- *Understand the relationship of a broker with his/her clients.*
- *Know the basic principles of Client service and the responsibilities of a broker to his/her clients.*
- *Learn the purpose of Brokers' accounting standards and audits.*

14.1 INTRODUCTION

In their application to any particular broker's office, each unit referred to under the divisions stated below could consist of several persons but this is often impractical except in very large organisations; and in small and medium-sized brokers, one person may have to wear several hats.

The extent and volume of the business dictate whether the departments are divided into Fire, Accident, Motor, Life/Family and Marine or into the more recent divisions of Property, Liability, Transportation and Insurances of the Person. The available staff may be divided into mixed skills sections, each handling a range of clients; or in a large office, a section may be devoted to only one class of client.

14.2 ORGANISATION STRUCTURE

Below is an example of a typical organisation structure in the broker's office:

Table 14-1 ***Typical organisation structure in the broker's office***

DEPARTMENT	JOB FUNCTIONS
Brokering	• Marketing • Servicing • Claims handling • Collection of premium/contribution • Policy/certificate and Documentation checking • Policy/certificate review analysis • Premium/contribution comparison • Policy/certificate design
Retakaful	• Facultative retakaful placement • Treaty retakaful placement • Accounts • Marketing • Service

Table 14-1 ***Typical organisation structure in the broker's office***

Claims	• Registration of claims • Liaison with insurer/takaful operator as regards the appointment of Loss Adjusters • Claim documentation • Monitoring claim settlement
Accounts	• Cash flow management • Investment • Reconciliation of accounts • Monthly operation statement • Statement of accounts • Preparation of payroll/SOCSO/EPF/ income tax
Administration/ Personnel	• Recruitment of new staff • Training of staff • Staff welfare • Employer/Employee relationship • Property management • Secretarial duties (Typing Pool, Mailing, etc.) • Licensing (renewal and CPD)
Research	• Market Intelligence – Competitors • Market Intelligence – Takaful Operators (TOs) • Market Intelligence – Prospective Public Relations Department • Relationship with clients • Relationship with TOs and others in the market • Relationship with the public
Branches	• Act as a company within a company • Functions similar to the Head Office but on a smaller scale

14.3 BROKING SERVICES AND BUSINESS PROCESSES

14.3.1 MARKETING

Marketing refers to the process of creating collateral products or services which are then priced, promoted and distributed to consumers. However, as a marketer of takaful, it is essential that a takaful broker promotes the Shari'ah and possesses ethical attributes in all aspects of its activities. This is called responsible marketing.

Whether it is the marketing of products or services, the following steps can be observed:

Table 14-2 ***The marketing process and activities***

PROCESS	ACTIVITIES
Scope of Marketing	• This process includes identifying, anticipating and supplying customer requirements efficiently and profitably. • It focuses attention towards the needs and requirements of the market. • It is concerned with satisfying those needs or requirements. • It involves analysis, control and planning.

Table 14-2 ***The marketing process and activities***

<table>
<tr><td>Preparation and Planning</td><td>This involves identifying the following:
<table>
<tr><td>Strengths</td><td>Expertise in a certain class or specialisation in a certain area</td></tr>
<tr><td>Weaknesses</td><td>Insufficient staff or lack of specialised skills</td></tr>
<tr><td>Opportunities</td><td>Personal contacts, company affiliated entities, existing client referrals</td></tr>
<tr><td>Threats</td><td>Competition from other brokers, market position</td></tr>
</table></td></tr>
<tr><td>Prospect Generation</td><td>• Information gleaned from newspapers, trade magazines, the Internet
• Strong networking through personal contacts and in-house connections
• Cold Calls
• Targeted Seminars
• Client referrals
• Tenders – These may require pre-qualification</td></tr>
<tr><td>Offerings</td><td>• Opening – Identify client needs.
• Presentation – May be a conceptual report with visual aids. Projecting the company image in the most favourable light.
• Negotiation – Know how to deal with the objection, know what the client really wants, understand the product fully and know the degree of flexibility that is available.
• Closing the meeting – Never make a promise that cannot be fulfilled.</td></tr>
<tr><td>Meeting the Competition</td><td>• Create a speciality niche by obtaining exclusive terms from selected insurers/operators on a particular type of business.
• Identify particular problems faced by a trade and discuss the possible solutions with insurers/operators.
• Provide prompt and efficient after sales services particularly in dealing with claims.</td></tr>
</table>

14.3.2 BROKER RELATIONSHIP WITH CLIENTS

Conceptually, there are six stages in the broker-client relationship metamorphosis.

a) Stage One – Information Gathering
b) Stage Two – New Business or Marketing Stage
c) Stage Three – Formal Trading Relationship (Development Stage)
d) Stage Four – Involvement Stage
e) Stage Five – Pre–Renewal Stage
f) Stage Six – Problem Claims or Complaints

The characteristics that apply and distinguish each stage, along with the relevant management, service and relationship quality issues are discussed as follows:

STAGE ONE – INFORMATION GATHERING

The first phase of the relationship comprises two stages:

a) the pre-relationship stage, and
b) the new business or marketing stage.

The timeline involved can vary from a very short period to several months. Like other professional services, new clients are obtained principally by referrals or recommendations from an existing client or by personal initiation or networking. This stage is also described as the pre-relationship phase, the pre-stage or the initial stage. The broker is generally concerned with ensuring certain issues are addressed.

Amongst these issues, a number of questions might be raised:

- How are details of the broker organisation obtained?
- Has the client been referred to the broker? And by whom?
- What are the reasons for the relationship breakdown with the previous broker?
- If there has been a change of management personnel will there be any conflict of interests?
- What type of service is the client looking for?
- What are the requirements for a new business?
- Does the broker have the expertise (technical advice) available within the organisation?

Once the above criteria and issues have been addressed, the decision is made regarding the continuity of the relationship with the prospective client. A letter is issued to the 'prospect' advising the outcome (i.e. initiating a programme discussion or ending the process). This stage can appear very informal and the prospective client organisation is referred to as a 'prospect'.

STAGE TWO – NEW BUSINESS OR MARKETING STAGE

Businesses may engage brokers in many ways. The initial programme design is discussed with the prospect. Factors include business type, size of the organisation and its risk profile. The prospect's financial and operational information is reviewed. Amongst this information is gross profit, turnover and wage roll projections. Amendments are made, a timescale for tender presentation and service standards are discussed and agreed.

It is made clear at this stage that the broker is acting as the intermediary between the prospective buyer (client) and the insurance/takaful. The appropriate insurers/takaful operators are contacted for quotations. Regular contact may be made to obtain any pertinent information.

Overall activity by the broker is intense. Once the broker has carried out its marketing stage, the tender is presented to the prospective client. The prospect may be obtaining quotations from several other sources; therefore, the broker must await their decision on whether they will go ahead with proposals.

The request for proposal can involve the entire programme or a specific risk issue. For example, the client can request proposals from several agents/brokers that address the entire insurance/takaful programme of the company or one can request a proposal for a specific line of coverage. Some companies believe that by splitting out a specific line of coverage and using multiple agents/brokers to meet the entirety of their needs, they are creating an atmosphere that will *"keep the agents/brokers honest and on their toes"*.

When dealing with governmental organisations looking for coverage, the Open Bidding technique is usually employed. This technique opens the bidding to any and all that can qualify for the process according to the bid specifications. Again, this bidding process will allow the price to take the driver's seat in the process. However, depending on the stringency of the qualifications, only a selected few brokers may qualify. By doing this, they will each have the opportunity to show their differentiation in the process, allowing some of their creativity and intellectual capital to be considered. Brokers would subscribe to third-party tender information providers to know about tender opportunities.[11]

Conceptual Bidding is based completely on the firm's differentiating factors. It is done with no specific insurance policies involved. The end game is to decide who to do business with based on their conceptual presentation. Whoever you select will be the firm that represents you in the eventual pursuit of insurance coverage.

Another method that is often employed is the Limited Broker Assignment. This technique is used to foster an environment of competition. In this technique, the company selects two or three brokers to "go to the markets" to represent them. Each broker is assigned specific markets based on a first come, first served basis. The brokers then pursue the markets they are assigned and come back with their proposal. The company then selects the broker they will use based on those proposals. It is important to note that while this is typically a price-driven approach, there are some differentiating factors that will be evident between the competing brokers. A pitfall of this method is that company may tend to overlook the Effective Cost of Risk as their primary focus would be to reduce insurance premiums.

If the broker is unsuccessful, management must endeavour to establish the reasons for this.

If the tender is accepted, the formal business relationship commences (i.e. stage three), and if rejected, the tentative relationship ends here.

STAGE THREE – FORMAL TRADING RELATIONSHIP (DEVELOPMENT STAGE)

The development stage involves creating a formal relationship between the broker and its respective clients. Here, the broker is given specific instructions to proceed with the tendered proposal and it is at this point that any indicative changes to the programme and premium/contribution financing arrangements are agreed.

[11] For example, www.tenderinfo.com.my.

A professional is assigned. The criteria for this include experience and existing workload. The prospect is advised of contact(s) within the organisation, and the insurers/operators are instructed to go on the cover at the agreed time and cost.

Once the documentation is received from insurers/operators, checks for any errors or omissions against any instructions given take place. Then, costs are presented to the client. Note that the standard of documentation varies dramatically between insurers/operators.

The prospect is now referred to as a client.

STAGE FOUR – THE INVOLVEMENT STAGE

Normally, the involvement stage describes the final six months of the twelve-month cycle of the relationship, and is described as the constant phase or the involvement phase.

The frequency of contact between the broker and the client can vary, depending on the size and type of the client organisation; however, the level of communication is much less than that experienced in stages one and two.

If claims are much higher than anticipated, risk management issues can be assessed.

The broker adopts a proactive approach with the client who is reassured about the quality of service. During this time the client's name soon becomes abbreviated, with everyone in the organisation using the same abbreviation.

STAGE FIVE – PRE-RENEWAL STAGE

This known as the pre-renewal stage and it commences approximately two months prior to the expiry of the insurance/takaful contracts.

The broking organisation makes contact with the client to obtain updated financial and operational projections for the forthcoming twelve months.

Then, the updated and pertinent information is given to insurers/operators to allow the renewal tender to be presented on the correct basis. The results of the terms/tender presented by the insurer/operator will determine whether a further marketing exercise is carried out.

The tender submission is made to the client. This usually takes place through a face-to-face meeting, which also provides the opportunity to review premium financing options.

If at this stage the client rejects the tender, the relationship will be terminated.

However, if accepted, the relationship returns to the development stage and the subsequent stages thereafter.

Stages three, four and five combined last for 12 months. This represents the duration of the insurance/takaful contract. At any time during these three stages, the broker might contemplate the opportunity to cross-sell to their client. Before the pre-renewal contract takes place, the broker might use his last chance to cross-sell other services.

STAGE SIX – PROBLEM CLAIMS OR COMPLAINTS

Once the formal trading has begun at stage three, there is now the ongoing potential for a further stage, the problem or troubled stage. This stage may last for a very short period (one day) or could last for several years, but it does not necessarily mean this leads to the termination of the relationship. Indeed, if handled correctly, this could enhance and strengthen the business-to-business relationship.

During this stage, the frequency of communication between the two organisations increases dramatically. One-to-one relationships can be enhanced or indeed damaged, depending on how effectively the claim or complaint is handled.

This stage can be used by the broker as an opportunity to cross-sell or put in place policy covers that the client was reluctant to put into effect previously.

14.3.3 CLIENT SERVICE

A client who has engaged a firm as their appointed broker may issue a Broker a Record Letter or a Letter of Engagement designating the firm as its dedicated agent. This will notify the insurer/takaful operator that the broker has been appointed to handle the company's insurance/takaful affairs. The letter usually takes effect from a certain date and for a fixed period of time. The appointment may be for a specific policy only. This authorisation may allow a broker to obtain the company's insurance/takaful history even from prior carriers.

In order to provide efficient and effective service to the client, the broker must be knowledgeable, prompt and accurate in his related job–functions:

a) **Knowledgeable** – The broker must know the client's needs and how to satisfy them. The client must also be informed of pertinent market information and developments relevant to the client's operations.
b) **Prompt** – The broker must respond promptly to the client's needs.
c) **Accurate** – Instructions and advice must be delivered accurately, especially policy wordings and interpretations.

14.3.4 AFTER SALES SERVICES

Administrative and Operational

The operational procedures that must be adhered to by all brokers in servicing their client are as follows:

Table 14-3 ***Operational procedures for brokers***

OPERATIONAL MATTERS	BROKER'S RESPONSE
General	• **Phone calls:** For urgent matters, return the call within 30 minutes. For others, return the call within the same day. • **Faxes and E-Mails:** Respond within 24 hours of receipt.

Table 14-3 ***Operational procedures for brokers***

	• **Letters:** Respond as soon as possible (within 5 days of receipt at the most). • **Others:** All other matters should be attended to within 48 hours.
Meetings	Notes should be taken at every meeting with the client or with insurers/operators and copied to file. Depending on the type of meeting, all participants should receive a copy of the minutes, which should be sent out within two to three days after the meeting.
Invoicing	• Invoices should be prepared and submitted to the client as the Cover Note or Binder. • Invoices relating to declarations should be sent within 3 weeks of receipt from the takaful operator/insurer. • The contribution should be collected either before cover as for motor or within 45 days to ensure compliance with premium payment warranty. To ensure this is monitored, an ageing analysis must be made available every 2 weeks for collection purposes.

Important Reminders:

Brokers should:

a) keep abreast of market developments in all classes of takaful/insurance. This will enable them to meet competition from others.
b) maintain all documentation in order to protect their Errors and Omissions Policy.
c) work with a sense of urgency but not set unrealistic deadlines that cannot be adhered to.

In the event they are not able to give a solution to their clients within a given time frame, they should revert to the client advising him of the situation and reason for the delay.

Reviews and Reports

The brokering service is a continuous process. Even after a placement has been made, there is a need to review its effectiveness. Reviews could be conducted on a quarterly or half-yearly basis. In some cases, reviews are done on a monthly basis as clients need to keep in touch on outstanding matters. Thus it may be necessary for the broker to prepare minutes of meetings to show the development of outstanding matters. Periodic reviews should report to the client new developments in the market and what is pertinent to the client's operation.

Brokers also need to prepare their client takaful/insurance manuals.

Table 14-4 ***Client takaful/insurance manuals***

SUBJECT MATTER	TYPE /CONTENT
Types of Client Takaful/Insurance Coverage Manuals	• New Business Reports • Renewal Reports • Specific Project Reports

Table 14-4 ***Client takaful/insurance manuals***

Client Takaful/Insurance Coverage Manuals	• Provide an outline summary of coverage. • Inform the client of takaful operators/insurers involved. • Describe the procedures for alterations / amendments. • Provide contact numbers and addresses of designated employees. • May include a claims procedure. • Should be provided to the client within one month from inception of the programme. • Used as a base for preparing the Renewal Programme.

Claims Services

The purpose of takaful/insurance is to indemnify the client in the event of a loss resulting from the peril covered and it is the duty of the broker to ensure that this promise is kept. The first action that the broker has to take is to confirm from his records that the loss falls within the policy coverage and to give immediate notification to the insurers/operators.

14.4 RESPONSIBILITY TO INSURERS/ TAKAFUL OPERATORS

Table 14-5 ***Responsibility of brokers to insurers/ takaful operators***

Immediate Action	• Give immediate notification by phone and follow up by fax or letter. • Discuss appointment of loss adjuster. • Arrange for Claim Form to be delivered. • Disclose all facts giving rise to the claim and submit all other documentation requested by takaful operator/insurer. • Conduct negotiation in a fair and reasonable manner. • Follow up the status of a claim periodically with the respective personnel in charge by using the diary system. • Obtain latest claim status for renewal purposes. • Assist client in the implementation of loss control measures in order to prevent future similar claims.

Important Reminders:
In handling the claim, brokers should observe some intimacy with the insurers/takaful operators. This may help to expedite the claim process on behalf of the client.
Brokers are reminded to:

- maintain a cordial relationship with insurers/takaful operators;
- never alienate insurers/takaful operators;
- maintain a professional and independent position;
- develop the objective of a long-term relationship with insurers/operators, which normally proves to be profitable.

14.5 RESPONSIBILITY TO CLIENTS

Table 14-6 *Responsibility of brokers to clients*

Immediate Action	• Advise in writing on policy claim conditions and relevant claim procedures. • Advise the client to safeguard all salvage items for review by a loss adjuster. • Advise on Third Party claims: Not to admit liability and to forward all correspondence. Advise on holding third parties responsible for the loss. • Advise on policy wording interpretation. • Recommend suitable loss adjuster. • Be prepared to go to the site of loss. • Advise the client of his rights and obligations under the policy. • Assist in completion of claim form, brief client on the role of the loss adjuster. • Assist in compiling supporting documentation. • Attend all site meetings. • Provide specialist advice i.e. independent claims advisors, surveyors, risk management experts to investigate the loss, if the amount of the loss so warrants.
Follow-up Action	• Arrange meetings with adjuster/insurer/takaful operator. • Follow up with minutes of meeting and action to be taken by the respective parties. • Keep a diary for follow-up, provide updates on the progress of the claim. • Keep a record of all claims relating to a project or class of insurance. • Prepare claims statistics on each class periodically and for renewal. • Negotiate on client's behalf for difficult or disputed cases.
Long-Term Action	• Provide clear procedures for claims notification. • Provide contact persons and numbers for 24 hours stand-by. • Provide advice on third-party claims. • Provide Accident Claim Forms. • Establish a pre-agreed panel of loss adjusters.

14.6 BROKERS' ACCOUNTING STANDARDS

PURPOSE

The purpose of these standards is to provide a uniform basis for all insurance and takaful brokers to maintain their accounts and to prepare their returns to Bank Negara Malaysia. These standards are approved under Section 72 of the *Islamic Financial Services Act 2013* (IFSA).

BANK ACCOUNTS

Every broker shall maintain one or more Premium/Contribution and Claims Accounts with a single bank or as many banks as he thinks fit.

The broker shall pay into the Premium/Contribution and Claims Account:

- such money belonging to him as may be necessary for the purpose of opening or maintaining the account;

- all money received from a client in respect of a contract of insurance/takaful;
- all money received from or on behalf of an insurer, reinsurer, takaful operator or retakaful operator for or on account of a client; and
- money to replace any sums which may by mistake or accident have been drawn from the account.

Notwithstanding the provisions of these standards, a broker shall not pay into the Premium/Contribution and Claims Account money held or received by him from a client:

- for or towards the payment of a debt due to the broker from the client or in reimbursement of money expended by the broker on behalf of the client; or
- on account of costs and services rendered.

Every broker shall maintain at least one Income and Expenditure Account with a single bank or with many banks as he thinks fit.

PAYMENT OF PREMIUM/CONTRIBUTION MONEYS

The broker shall pay to insurers/operators premiums/contributions received (including any payment of premium/contribution) in the Premium/Contribution and Claims Account after deduction of brokerage to which he is entitled as follows:

- for all classes of insurance under Section 84 of the *Financial Services Act 2013* (FSA), or Section 96 of the *Islamic Financial Services Act 2013* (IFSA)t in accordance with the provisions of the section, including any statutory amendments or re-enactments thereof; and
- for all classes of insurance/takaful other than those specified in paragraph (a), no later than fifteen (15) calendar days from the date of receipt of the premiums/contributions. In compliance with these provisions, a broker shall make payment to insurers/takaful operators at least twice (2) a month, one payment to be made during the middle of the month and the other at the end of the month or similar financial period.

Any payment of premium/contribution made to insurers/operators must be identified to specific transactions. No payment shall be made on an account basis. Premiums/Contributions collected in respect of one transaction shall not be applied to settle amounts due under a different transaction unless authorised in writing by the debtor party. Where, for any reason, the broker decides to withhold payment to the creditor party after collecting related amount from the debtor party, the broker shall notify the debtor party of this position and if requested, the broker shall refund the amount to the debtor party.

For reinsurance premiums/retakaful contributions, payment to reinsurers/retakaful operators shall be made within fifteen (15) days from the date of receipt of full reinsurance/retakaful, closings/documentation but in any case not later than sixty (60) days from the date of receipt of the reinsurance premium/retakaful contribution without contravening the premium/contribution warranty applicable to the reinsurance/retakaful contract.

All payments to insurers, reinsurers, takaful operators or retakaful operators shall be deposited with, or dispatched by post or other means as agreed with the insurer, reinsurer, takaful operator or retakaful operator.

PAYMENT OF CLAIM MONEYS

The broker shall pay the client claim moneys received or credited in the account (including any part payment) within fifteen (15) days from the date of receipt of such moneys.

DRAWING FROM THE PREMIUM/CONTRIBUTION AND CLAIMS ACCOUNT

Money may be drawn from the Premium/Contribution and Claims Account:

- money properly required for payment to or on behalf of an insurer, reinsurer, takaful operator, retakaful operator, client or the broker himself; and
- money which by mistake or accident has been paid into the account; and
- money for placement in approved deposits.

No money drawn from the Premium and Claims Account shall be drawn except by:

- a cheque drawn in favour of the insurer, reinsurer, takaful operator, retakaful operator, client or broker in so far as each party is entitled to receive payment; or
- a transfer to a bank account in the name of the insurer, reinsurer, takaful operator, retakaful operator, client or broker in so far as he is entitled to receive payment.

PLACEMENT OF DEPOSIT

The broker may place money in the Premium/Contribution and Claims Account in such approved deposits, subject always to "Payment of Premium Money" and "Payment of Claim Moneys" Standards being complied with. Any interest earned thereon from such deposits shall be retained by the broker for his own benefit. Where a broker receives any claim money in trust for or on account of a client, any interest earned from the deposit of such money shall be paid to the client.

MAINTENANCE OF RECORDS

In respect of its insurance/takaful broking operations, every broker shall maintain a:

- Premium/Contribution register in which will be entered the particulars of every insurance/takaful handled by the broker and the names and shares of insurers/ takaful operators on the risk and the amounts of premium/contribution payable to each insurer/operator thereon; and
- Claims register in which will be entered the particulars of every claim intimated on any insurance/takaful handled by the broker, the estimated amount recoverable from each insurer/ takaful operator concerned and all subsequent settlements and changes in provisions for the claims to the extent the broker becomes aware of such changes.

In respect of its reinsurance/retakaful or broking operations, the broker shall maintain:

- Registers similar to the maintenance of records above in respect of facultative reinsurance or retakaful business; and
- Treaty Ceded Register in which will be entered by particulars of every automatic (including auto-fac) reinsurance treaty or retakaful or excess of loss cover handled by the broker and the names and shares of reinsurers or retakaful operators on each contract; and
- Treaty Ceded Business Register in which shall be entered particulars of all treaty accounts, premium/contribution payments and claims recoveries processed by the broker in respect of treaty reinsurance or retakaful contracts.

The registers referred to under maintenance of records above may be maintained in such form as the broker finds convenient, together with all supporting documents and information which may be necessary to explain and support the information contained in the registers.

ACCOUNTING RECORDS

Every insurance and takaful broker shall maintain separate records for each of the following:

- Direct insurance or takaful insurance transactions relating to its clients, their insurers and operators;
- Reinsurance or retakaful transactions relating to its ceding companies, reinsurers and retakaful operators; and
- Broker's own income and expenditure accounts.

Every broker shall at all times keep and maintain properly written books and accounts as may be necessary to show all his dealings with:

- premium/contribution or claims money held, received or paid by him; and
- any other money dealt with by him through the Premium/Contribution and Claims Accounts.

All dealings referred to in paragraph (2) of Accounting Records shall be recorded in a premium, contribution or claims cash book and no other dealings shall be recorded in such book. Every broker shall ensure that accounting records are kept in such manner and detail with supporting documents as

- to show and explain the transactions;
- to disclose with reasonable accuracy, at any time, the financial position of the business at that time; and
- to ensure that any balance sheet, profit and loss account or other statements of financial position of the business prepared, is capable of giving a true and fair view of the state of affairs of the business.

The accounting records shall in particular contain:

- entries from day to day of all sums of money received and expended in the course of the business and particulars of such receipts and payments; and
- a record of assets and liabilities of the business, and shall be preserved for at least seven (7) years from the date of the last entry therein.

The broker shall prepare a monthly reconciliation between the broker's statement of accounts, and insurer's/operator's company's records. In this standard, the expression "book" shall be deemed to include a loose-leaf book and such cards, other permanent documents or other media as are necessary for the operation of a mechanical or computerised system of book-keeping.

REVENUE RECOGNITION

The income for the insurance and takaful broker shall be recognised as follows:

- **Brokerage on a fee basis** – On due dates for the respective amounts payable;
- **Direct insurance/takaful brokerage as a percentage of premium/contribution** – Simultaneously with the issue of debit note for the premium/contribution to the client;
- **Reinsurance/Retakaful administration fee** – On receipt of quarterly treaty account or facultative closing particulars or upon the issue of debit notes on due dates of an excess of loss deposit premium/contribution;
- **Fees for other services** – Upon completion of service and issue of debit note on dates of interim payments as agreed;
- **Investment and other income** – On accrual basis.

Any revenue which has been recognised but remains outstanding for settlement for six (6) months shall be provided as doubtful. Any revenue due from a party which has suspended payments shall be provided as doubtful.

SETTLEMENTS

On contribution due, the broker shall promptly check and, if found in order, transmit the debit note to the client without any delay. Where the insurer or operator raises a debit note on the broker, the broker shall issue his own debit note to the client in such a manner that the gross premium is debited by the insurer or operator.

- Where a direct insurance or takaful claim has been processed and agreed for settlement, the broker shall secure payment by the insurer or operator to the client. Where the insurer or operator settles the claim in account with the broker in respect of that client, the broker should immediately issue a corresponding credit note and pay the amount to the client without delay provided there is no outstanding premium or contribution due from the client to the insurer or operator.

- The broker shall follow up for closing particulars and immediately on receipt, it will raise a debit on the ceding company and credit the appropriate premiums or contribution net of deductions to reinsurers or retakaful operators. The premiums or contributions and deductions should be the same in the debit and credit advice except for the additional item of deduction of brokerage or administration fee in the credit advice.
- Where a reinsurance or retakaful claim has been processed and has been agreed for settlement, the broker shall pay the ceding company immediately upon the recovery of the amount. Where more than one reinsurer or retakaful operator is involved, the broker should pay to the ceding company as and when recoveries are made without holding up settlement until the last of the recoveries.
- Where a broker on a direct insurance/takaful is also the broker on reinsurance/retakaful of that risk, the broker may, with the agreement of the insurer/operator, simultaneously issue credit and debit notes for the direct insurance/takaful and the reinsurance/retakaful thereon and make a net settlement.
- In respect of proportional reinsurance or retakaful treaties the broker shall issue the appropriate debit or credit note to the ceding company as soon as a treaty account is received and found in order and raise a corresponding credit or debit in favour of the reinsurer or retakaful operators.
- In respect of excess of loss reinsurance or retakaful treaties the broker should raise debit notes on the ceding company for the deposit premiums or contributions promptly on the due dates and for adjustment premiums or contributions as soon as possible after the close of the year and prepare corresponding credit notes in favour of reinsurers or retakaful operators. Excess of loss claims should be processed similarly as in para (4) above.
- All amounts recovered from the debtor parties should be credited to the creditor parties concerned and the balance should be settled once a fortnight together with a statement of account listing all the items included in the settlement. All debit entries (agreed with the debtor party where necessary) which have not yet been settled may be included in the fortnightly account and a net settlement made.

EXPENSE RECOGNITION

Expenses shall be accounted on an incurred basis.

AUDIT

The accounts referred to in Accounting Records section shall be audited annually by an auditor approved by Bank Negara Malaysia.

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CHAPTER 15 SOFT SKILLS REQUIREMENT

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CHAPTER OBJECTIVE

To understand the significance of effective communication and why there is a need to improve soft skills to be a professional insurance broker.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Appreciate the importance of soft skills and the need for such skills in obtaining crucial information for underwriters to provide insurance quotation.*
- *Understand the basics of formal communication and non-verbal communication.*
- *Acquire interpersonal skills in negotiation.*

15.1 INTRODUCTION

15.1.1 WHAT ARE HARD SKILLS?

Hard skills are related to specific technical knowledge and training. They include competencies like how to use a certain machine, software or tool. Hard skills are technical knowledge or training that you have gained through any life experience, including in your career or tertiary education. Every job requires certain technical skills specific to that industry. If you are in the insurance industry, among the important hard skills you must command are the Principles of Insurance i.e. Insurable interest, indemnity, proximate cause, subrogation and contribution.

Some of the important hard skills are:-

a) Mathematics
b) Accounting
c) Microsoft Excel
d) Data mining and data processing
e) Principles of Insurance

15.1.2 WHAT ARE SOFT SKILLS?

Soft skills are desirable qualities that do not depend on acquired knowledge. Soft skills are personality traits and habits that shape how you work on your own and with others to create a positive and functional work environment. Some examples of soft skills that an insurance broker should acquire would be as follows:

a) Communication skills
b) Social graces & active listening
c) Interpersonal skills in negotiations
d) Empathy, tact and attitude
e) Teamwork and positive work ethics

15.1.3 WHAT ARE THE KEY DIFFERENCES BETWEEN HARD SKILLS AND SOFT SKILLS?

The key difference are how they are gained and put to use in the workplace.

- Hard skills are gained through education or specific training.
- Soft skills are seen as personality traits you may have spent your whole life developing. They are called upon when you need to communicate with people or to amicably settle a difficult situation.

Both hard and soft skills are required for you to function professionally as an insurance broker. While hard skills are necessary to successfully perform technical tasks in a job, soft skills are necessary to create a positive and functional work environment. Both types of skills are necessary for you to successfully advance in your career. All employers will appraise your performance based on the combination of your hard and soft skills.

15.1.4 WHY ARE SOFT SKILLS IMPORTANT?

Soft skills are important because they enable people to effectively navigate their environment, work well with others, perform effectively and achieve their goals to the satisfaction of all parties concerned.

A study conducted by Harvard University noted that 80% of achievements in career are determined by soft skills and only 20% by hard skills. With increasing digitalisation and increasing use of algorithms, there is now more focus on creativity which comes under soft skills.

15.1.5 WHY IS THERE A NEED TO IMPROVE SOFT SKILLS?

Our learning years, from primary schools to universities are spent in acquiring technical knowledge (hard skills) such as mathematics, accounting, business management and economics from our teachers, lecturers and books. However most soft skills are not taught in schools and universities. They have to be learnt on the job by trial and error. Although self-improvement books are available these days, there is no easy step-by-step guide to acquire knowledge of soft skills.

Hard skills are skills where the rules stay the same regardless of which circumstances or people you work with. In contrast, soft skills change all the time according to the environment, the people you work with and the level of relationship.

15.2.0 **COMMUNICATION**

15.2.1 THE IMPORTANCE OF COMMUNICATION

The best product in the world cannot be sold if the benefits and features of the product cannot be communicated from the seller to the buyer.

The best organization in the world cannot fulfill their vision if the company's philosophy, business plans and aspirations cannot be conveyed to all their employees through all channels of communication.

Good and effective communication is an essential tool in achieving productivity and maintaining strong, lasting working relationships at all levels of an organisation.

Communication should exist in any organization right from the top management to the lowest level of staff if it is going to be effective

15.2.2 WHAT IS COMMUNICATION?

Communication is seen as a dynamic process which involves the sender at one end and the receiver at the other end. It can either be verbal or non-verbal. The term verbal communication often evokes the idea of spoken communication, but written communication is also part of verbal communication. Verbal communication is about language, both written and spoken. Verbal communication refers to our use of words and verbs both written and spoken (many people mistakenly assume that verbal communication refers only to spoken communication). Non verbal communication refers to communication that occurs through means other than words such as body language, micro expressions, gestures and silence.

Communication can be classified into 3 different categories: -

i) Written (Verbal with words put in writing)

ii) Oral (Verbal with words orally spoken)

iii) Non-verbal (Body language and micro expressions)

Communication involves the process of sending or receiving ideas, thoughts or feelings from one person to another, or more persons in a way that the person receiving it comprehends it in the same way that the sender wants him to understand.

However, very often, the message that is transmitted by the sender is interpreted or decoded wrongly by the receiver thus resulting in miscommunication.

15.2.3 BARRIERS TO EFFECTIVE COMMUNICATION

Barriers to communication are things that get in the way of a message being received.

The main barriers are:-

a) Physical conditions
b) Filtering
c) Selective Perception
d) Information overload
e) Semantics
f) Denotation and Connotation
g) Emotional Disconnects
h) Credibility

Physical Condition

- Loud distraction sounds or loud music that makes it impossible to hear or concentrate.
- General level of background noise can be so intense that it is hard to focus for long in one particular voice.
- A room may be too hot or too cold. Consequently people cannot get comfortable and cannot pay attention.
- Outside activities may be a distraction to those with a view out windows.
- May be too near to lunch time or close to quitting time to keep people focused.

Filtering

Filtering occurs when messages pass through an intermediary in the communication channel. Filtering often can alter the original message, limit its effectiveness or render it incomprehensible.

- A message sender sees the world through one set of filters (experience and values) and the receiver sees it through a different set of filters.
- Personal and particular experiences set up filters on how people view the world and how they communicate.
- The more similar people are in lifestyle, culture, social and economic situations, the lesser their mental filters for distortion of messages.
- Some messages are summarized by a manager and relayed through an administrative assistant who edits the messages before it is transmitted to a group of receivers.
- The fewer people involved in the transmission of a message, the greater the chance it will be received as the sender intended.

Selective Perception

Selective perception is the process by which individuals perceive what they want to in media messages while ignoring opposing viewpoints. In other words, a person sees the picture as he wished to see, and not what the picture is.

An example of selective perception is a self-proclaimed health nut who spends hours at the gym, eats healthy low-fat meals and is a member of online fitness group. However, he is also a cigarette smoker. Though he knows about the health risks of smoking, he believes that he will not have any adverse health risks as long as he exercises, eats healthy and smoke less than one pack of cigarette a day.

Emotional Barriers

Emotional barriers are mental walls that keeps a person from openly communicating their thoughts and feelings to others.

Examples of emotional barriers that prevent individuals from effective communication include: -

- Anger
  - Anger can affect the way your brain processes information given to you. Angry people have difficulty processing logical statements, limiting their ability to accept explanations and solutions offered by others.
- Pride
  - Pride can shut down effective communication as the receiver may be annoyed by the sender's need to be right all the time. Some people have the habit to focus only on their views and shut down views from others. They are not bothered with the view of others.
- Anxiety
  - When a person is anxious or stressed, an expressed concern is more likely to be interpreted as criticism. Your constant worries can hinder your ability to concentrate on the information you are given or receiving.
- Credibility
  - In communication, the validity of the message is tied to the reputation of the sender. If the receiver does not trust the sender, he will view the message itself with scepticism or suspicion. The trustworthiness of a communication regardless of format, is heavily influences by the perceived credibility of the source of the communication.

Information Overload

Information overload is the difficulty in understanding an issue and effectively making decisions when one has too much information about that issue.

Information overload occurs when the amount of input to a system exceeds its processing capacity. Decision makers have fairly limited cognitive processing capacity. Consequently, when information overload occurs, it is likely that a reduction in decision quality well occur.

Sometimes it is not just the quantity of communication but the level that causes overload. If the message contains information that is new to the receiver, including processing or concepts that are not familiar, then the chances of overload increase greatly.

Semantics

Semantics is the study of the relationship between words and how we draw meaning from these words. The same word can be said to two people and they can interpret them differently, "Crash" can mean auto accident, a drop in the stock market, to attend a party without being invited, ocean waves hitting the shore, or the sound of cymbals being struck together.

15.2.4 TYPICAL COMMUNICATION FLOWS

Information can flow in four directions in an organization as follows:-

a) Downward

b) Upward

c) Horizontally

d) Diagonally

Downward Communication

This happens when company leaders and managers share information with lower-level employees. The senders do not usually expect or want to get a response. The most common types of downward communication are everyday directives of department managers or line managers to employees. These can also be in the form of instruction manuals or company handbook.

Upward Communication

It is information moving from lower level employees to high level employees as when workers report to a supervisor or team leaders report to a department manager. Items typically communicated upward include progress reports, proposals for projects, budget estimates, grievances and complaints, suggestions for improvements and schedule concerns. Sometimes a downward communication prompts an upward response such as when a manager asks for a recommendation for a replacement part or an estimate of when a project will be completed.

Horizontal Communication

It involves the exchange of information across departments at the same level in an organization. The purpose of most horizontal communication is to request support or coordinate activities. People at the same level in an organization can work together to work on problems or issues in an informal and as needed basis. Communications between two employees who report to the same manager is an example of horizontal communication.

Diagonal Communication

This is cross-functional communication between employees at different levels of the organization. If a sales representative e-mails the vice president of marketing, then diagonal communication has occurred.

External Communication Flows

Communications do not start and stop within an organization. External communication focuses on audience outside of the organization especially customers.

Senior management with the help of specialized departments such as public relations and legal almost always controls communication that relate to public image.

Middle level management general handle operational business communications such as purchasing, hiring and marketing.

When communicating outside the organization (regardless of the level) it is important for employees to behave professionally. They must not make commitments outside their scope of authority.

15.2.5 WRITTEN COMMUNICATION

Written communication refers to the process of conveying a message through written words or symbols.

The written communication is the most common and effective mode of business communication. In any organization, the electronic mails, memos, reports, documents, letters, journals, job descriptions, employee manuals, etc. are some of the commonly used forms of written communication.

Such communication is used when the information to be transmitted is lengthy and includes some complex terms that cannot be explained orally. Also, the organizations maintain their documents in writings such that these can be used as a reference and evidence of any transaction anytime in the future.

The effectiveness of written content depends on the correct choice of words, their organization into correct sentence sequence and the cohesiveness in the sentences. The information in writing is considered more legal and valid than the spoken words. Also, people rely more on the written content than what has been said orally. But, however, unlike oral communication the feedback of written communication is not immediate since it is not spontaneous and requires time to get into the understandable form.

An Insured buys an insurance policy which is an insurance contract. That few pieces of paper are supposed to give him peace of mind if there is a claim. Operational clause, coverage clauses, conditions, exclusions and exceptions are all expressed in the policy in written form. During the policy period, extensions, endorsements may be required to enhance the policy.

It is the job of an insurance broker to ensure that all written communication by the insurer is explained and conveyed to the insured before and during the policy period.

For an insured to understand or respond to written communication, the insurer and broker must ensure that the contents of the written message contain the following elements:

A. Accuracy
B. Brevity
C. Clarity

Why is Accuracy Important?

i) Because the person you are writing to may not know you
ii) The reader may not be familiar with the circumstances which caused you to write

Why is Brevity Important?

i) Because the person you are writing to do not have the time to wade though a long letter
ii) If the letter is more than two pages, the reader will probably slip it at the bottom of the tray to look at it latter when he has more time

Why is Clarity Important

i) Because if you are not clear in what you need to tell the recipient and what response you expect, you will not receive a reply

ii) The general rule is to organise your letter into three parts:

a) Introduction - Tell why you are writing

b) Body - Present the important facts

c) Conclusion - Describe what you like the recipient to do

The most important sentence is the first sentence

- Because in a large percentage of all letters, it is the only sentence that is read
- Only a few of every hundred circulars/sales letters that reach the average executive's desk are read
- With these odds against you it is easy to see why your letter has to have an interesting and exciting beginning

Give Your Letter the Right Look

- Part of the impression your letter make depends on their appearances
- A messy letter is discourteous, clearly implying a lack of interest and care on the part of the writer which invites a similar reaction by the reader.
- Use proper grammar, spelling and punctuation because it demonstrates your care and attention to detail.
- Spell check and proof read your letter because spell checks alone has a way of passing over errors eg.
  - two much time too much time
  - wind win situation win win situation
- Take care of capitalizing names and titles
  eg. The Malaysian Institute of Insurance (MII)

- As much as possible use active voice rather than passive voice because active voice adds strength and warmth to your letter.

  Active voice – Our underwriter will write the memo
  Passive voice – The memo will be written by our underwriter
- Avoid using incomplete or run-on sentences. Write complete sentences that have a subject and a verb.
  Incomplete – Discuss at the meeting
  Complete – We shall discuss the issues at the meeting.

Make Your Document Look Sharp

- Avoid using too many type faces.
  - Today's word processing programs make it possible for you to set up a letter that features say six or seven fonts. Choose one "display" font for your headlines and subheadings and one text for the main body of your message.

- Keep it relatively formal. Remember that you are writing something that will be received by a business colleague, not a friend. Do not be tempted to inject personal touches as :

  "Bro, whats up".

- Avoid cramming a single page with too much text.

- Proof read to ensure that you have not accidentally omitted an important word or included something that should be deleted.

Avoid Being Negative Avoid phrases like

- I know I shouldn't take your valuable time
- I don't want to inconvenience you.
- I realize I am imposing.

- Phrase like these are red flags, they offer a reader an excuse not to do what you want him to do.

Watch Your Emotions

- If you are determined to write an emotional letter to someone, put it away overnight in order to read it and make sure that you have said nothing that many sound different from what you intended.

- Always remember that written words have permanency and thoughts carelessly put on paper can come back to haunt you.

- Spoken words fade away once the cause is forgiven, written words are fixed on the page forever.

- Letters written under strong emotion should be held for twenty four hours and re-read before being sent.

When Drafting an endorsement be very clear

- ✗ Sum insured increased by RM 200,000 to RM 600,000 with immediate effect
- ✗ Sum insured increased from RM 400,000 to RM 600,000 with effect from 1 Jan 2018
- ✓ Sum insured increased from RM 400,000 by RM 200,000 to RM 600,000 with effect from 1st January 2018

15.2.6 ORAL (SPOKEN) COMMUNICATION

Oral communication is the process of expressing information or ideas by word of mouth. It can be either formal or informal as follows:

Informal oral communication

- Face to face communication
- Telephone conversations
- Discussions that take place at business meeting
- Informal discussions with clients

Formal communication

- Presentation at business meetings
- Budget presentation
- Tender presentation
- Video conferences
- With advancement in technology, new forms of oral communication continue to develop

During a communication process several thinks happen at the same time

- The conscious mind is receiving information
- The sub conscious mind is receiving a different set of information
- Align your words with your tone
- And your entire message with your body language
- Congruency is synchronizing the ways in which you deliver your message
- The words we choose, and use are done on a conscious level and consciously received by the listener
- But your tone and body language are projected subconsciously and received subconsciously by the listener

To make a good impression keep this in mind:

I mage
M indset
P ersonal Grooming
R apport Skills
E nthusiasm
S tance
S mile

Always Remember:

There is no second chance to make first impression

After creating a good first impression, communicate verbally. Remember to PAMPER your listener as it grabs attention and makes listening to you pleasurable

P	rojection	>	Adequate volume
A	rticulation	>	Be expressive
M	odulation	>	Add variety to your tone
P	ronounciation	>	Pronounce all words properly
E	nunciation	>	A combination of the above
R	epetition	>	Repeating key points aids recall

While presenting verbally, enhance with non-verbal expressions

S	mile	>	Reduces Tension
O	pen postures	>	Shows openness and transparency
F	orward lean	>	Encourages prospects to speak
T	ouch	>	Reinforces your rapport eg. handshake
E	ye contact	>	Shows your interest, and concern
N	od	>	Acknowledges that you are listening and in agreement

Active Listening

- People want to be listened to
- Listen attentively. It will make him important.
- Do not interrupt when the other party is talking. Let them finish what they want to say or express
- If you display enough encouraging signs your prospect will tell you what insurance they want, how they want it to be arranged and why they want it
- Many instances, prospects talk to themselves into the sale
- In many cases the prospects even handle their own objections

Ask Questions Politely

- In between listening ask questions
- Ask questions to clarify
- Paraphrase what the party is saying to confirm your understanding
- Always show that you are attentive
- Talk less and listen more
    - Talking is giving information
    - Listening is accumulating information
- Discoveries are made by questioning answers

A void distraction	>	Switch off your mobile phone
C ues observation	>	Observe body language and micro expression
T alk	>	Only when necessary
I nterested	>	Show interest to motivate them to talk more
V iewpoint	>	Understand your prospect's viewpoints
E ye contact	>	Maintain eye contact to show interest and sincerity

Effective Questions

- Open ended questions
  - A question that is answered by more than a simple yes or no
- Leading question
  - A question when an answer is suggested or specifically targeting at an area
- Rhetorical question
  - A question that do not require answers. They are used not to get an answer but to stimulate thoughts and get prospects thinking

Be sincere, built rapport

People Buy Trust First, Products or Service Second

- Customers don't care how much you know until they know how much you care
- Customers buy trust first, products latter

> "We all have different ideas of reality, ways in which we perceive the world.
> And we can really trust people, who look at the world they way we do"
>
> *Professor John Ginder & Dr. Richard Bandler*

- People are not creatures of logic. They are creatures of emotion.

  Dale Carnegie

Advantages of Written Communication

- Written communication helps in laying down apparent principles, policies and rules for running of an organization.
- It is a permanent means of communication. Thus, it is useful where record maintenance is required.
- It assists in proper delegation of responsibilities. While in case of oral communication, it is impossible to fix and delegate responsibilities on the grounds of speech as it can be taken back by the speaker or he may refuse to acknowledge.
- Written communication is more precise and explicit.
- Effective written communication develops and enhances an organization's image.
- It provides ready records and references.
- Legal defenses can depend upon written communication as it provides valid records.

Disadvantages of Written Communication

- Written communication does not save upon the costs. It costs huge in terms of stationery and the manpower employed in writing/typing and delivering letters.
- Also, if the receivers of the written message are separated by distance and if they need to clear their doubts, the response is not spontaneous.
- Written communication is time-consuming as the feedback is not immediate. The encoding and sending of message takes time.
- Effective written communication requires great skills and competencies in language and vocabulary use. Poor writing skills and quality have a negative impact on organization's reputation.
- Too much paper work and e-mails burden is involved.

Advantages of Oral Communication

- There is high level of understanding and transparency in oral communication as it is interpersonal.
- There is no element of rigidity in oral communication. There is flexibility for allowing changes in the decisions previously taken.
- The feedback is spontaneous in case of oral communication. Thus, decisions can be made quickly without any delay.
- Oral communication is not only time saving, but it also saves upon money and efforts.
- Oral communication is best in case of problem resolution. The conflicts, disputes and many issues/differences can be put to an end by talking them over.
- Oral communication is an essential for teamwork and group energy.
- Oral communication promotes a receptive and encouraging morale among organizational employees.
- Oral communication can be best used to transfer private and confidential information/ matter.

Disadvantages/Limitations of Oral Communication

- Relying only on oral communication may not be sufficient as business communication is formal and very organized.
- Oral communication is less authentic than written communication as they are informal and not as organized as written communication.
- Oral communication is time-saving as far as daily interactions are concerned, but in case of meetings, long speeches consume lot of time and are unproductive at times.
- Oral communications are not easy to maintain and thus they are unsteady.
- There may be misunderstandings as the information is not complete and may lack essentials.
- It requires attentiveness and great receptivity on part of the receivers/audience.
- Oral communication (such as speeches) is not frequently used as legal records except in investigation work.

The seven C's of oral and written communication

Both oral and written communication are used separately depending on the intentions and objectives of the sender. However, sometimes they are used together to reinforce the message.

Irrespective of whether oral or written, to have effective communication one should keep the following 7 C's of communication in mind:-

Clear: ***The message should be clear and easily understandable to the recipient. The message should emphasize on a single goal at a time and shall not cover several ideas in a single sentence.***

Correct: ***The message should be correct, i.e. a correct language should be used, and the sender must ensure that there is no grammatical and spelling mistakes. Also, the message should be exact and well-timed.***

Complete: ***The message should be complete, i.e. it must include all the relevant information as required by the intended audience. The complete information gives answers to all the questions of the receivers and helps in better decision-making by the recipient.***

Concrete: ***The communication should be concrete, which means the message should be clear and particularly such that no room for misinterpretation is left. All the facts and figures should be clearly mentioned.***

Concise: ***The message should be precise and to the point. The sender should avoid the lengthy sentences and try to convey the subject matter in the least possible words. The short and brief message is more comprehensive and helps in retaining the receiver's attention.***

Consideration: ***The sender must take into consideration the receiver's opinions, knowledge, mindset, background, etc. in order to have an effective communication. In order to communicate, the sender must relate to the target recipient and be involved.***

Courteous: ***It implies that the sender must take into consideration both the feelings and viewpoints of the receiver such that the message is positive and focused at the audience. The message should not be biased and must include the terms that show respect for the recipient.***

15.2.7 BODY LANGUAGE

What is Body Language?

- Body language is non-verbal communication projected subconsciously and received subconsciously by the insurer
  - Intentional non-verbal (consciously)
  - Unintentional non-verbal (sub-conciously)
- Reaction from that part of the brain called the limbic system (the honest brain). It is designed to preserve us
- It's sole purpose is our survival and our control of emotions.

How is Body Language Communicated ?

Whenever there is any perceived threat to our survival, our body reacts to the 3F's

- ✓ Freeze
- ✓ Flight
- ✓ Fight

Being Civilized We Do Not Physically Freeze, Flight or Fight

- ➢ Instead we response by having positive and negative gestures and expressions being signs of comfort and discomfort

Important Rules of Observation

1) You have to be a competent observer.
2) Be aware of cultural differences.
3) Look for clusters of behaviours. One swallow don't make a summer.
4) What behaviours are a change from normal. Most people have certain behaviours that they engage in repeatedly.
5) Focus on primary i.e. look for the most immediate expressions as being the most accurate.
6) The observations that we make should be non-intrusive.
7) Determine an individual's baseline and watch for deviations from the baseline.

Comfort and Discomfort

- Our subconscious mind reacts to messages seen through our eyes
- The brain then sends blood to the desired areas resulting in gestures, expressions and micro expressions all over our body
- This is reflected in our face, forehead, eyebrows, eyes, eyelids, nose, ears, lips, neck, shoulders, torso, hands, hips, legs, feet, and every part of our body.
- Violation of space, distancing ourselves
- Adaptive behaviour or pacifiers
    - Twirl your hair
    - Rub your thighs
    - Scratch your neck

Action, Speaks Louder Than Words

- Our impressions of each other are based on more than words
- People can have cordial conversations and not like each other
- A person may dismiss someone using body language and not say anything negative
- What actions can say:
    - Deception
    - Confidence
    - Boredom
    - Attraction
    - Being Open
    - Being Closed Off

15.3 NEGOTIATION

Negotiation is a method by which people settle differences. It is a process by which compromise or agreement is reached while avoiding conflict and dispute.

It is aimed to resolve points of difference, to gain advantage for an individual or collective or to craft outcomes to satisfy various interests.

It is often conducted by putting forward a position and making small concessions to achieve an agreement. Principles of fairness, seeking mutual benefits and maintaining relationships are the keys to successful outcome. For a negotiation to be win-win, both parties should feel positive about the negotiation once it is over.

15.3.1 Process of Negotiation

The following elements must be present for a successful negotiation:

- Preparation
- Discussion
- Clarification of goal
- Negotiate towards a win-win outcome
- Agreement
- Compromise
- Implementation of a course of action

Key skills in Negotiation

- Questioning
- Listening
- Clarifying

15.3.2 Important Negotiation Parties

Underwriter

- To obtain quotation for a difficult risk
- To obtain capacity
- To convince underwriter to write under net and treaty
- To obtain competitive rates
- To obtain additional coverage
- To obtain reasonable excess (deductibles)

Claims Head/Loss Adjuster

- To negotiate for higher quantum
- To create an element of doubt to make a claim payable
- To reason with claims personnel on subjectivities of questionable claims
- To negotiate on ex-gratia basis if technical grounds fail
- To push through a claim on commercial grounds

A high technical knowledge on principles of insurance coupled with proficient soft skills can ensure a successful negotiation outcome.

16

CHAPTER 16 BUSINESS ETHICS

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16.10.1 BREACH OF CODE 241

CHAPTER OBJECTIVE

To understand the Code of Ethics that governs Insurance/Takaful brokers and the consequences of breach of code.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Comprehend the Code of Ethics and Conduct in professional dealings and contracts.*
- *Understand Insurance and Takaful brokers' accounting standards and guidelines.*
- *Learn what happens when there is a breach of code and how to monitor a breach using devices.*

16.1 CODE OF ETHICS & CONDUCT

16.1.1 THE OBJECTIVES OF MITBA

Members should observe the objectives of the Malaysian Insurance and Takaful Brokers Association (MITBA), as set out in the Constitution of the Association *inter alia*:

1) To elevate their status, safeguard and advance their interests, procure their general efficiency and proper professional conduct.
2) To ensure that the employees of its members are professionally qualified, conversant with insurance and/or takaful laws and practices, and acquainted with current developments as they affect the insurance industry in general and insurance and takaful broking in particular.
3) To afford means of reference for amicable settlement of any professional differences and disputes that may arise from time to time.
4) To ensure that members devote themselves to the insurance and/or takaful broking professions and do not carry on businesses inconsistent therewith.
5) To decide on questions of professional conduct and etiquette.
6) To promote the healthy growth of the insurance industry in line with the national objectives.

INTRODUCTION

a) The intention of MITBA in formulating this Code of Ethics and Conduct is to assist in establishing a recognised standard of professional conduct for all insurance and/or takaful brokers who should, in discharging their duties as such, comply with both the provisions and the underlying spirit and intent of this Code. This Code of Ethics and Conduct shall apply to all Members of the Malaysian Insurance and Takaful Brokers Association and their directors and employees.

b) This Code of Ethics and Conduct is intended as an explanatory statement of the principles which are expected to apply to the ethics and conduct of Members and their directors and employees.
The Code, however, does not in any way restrict any Member from formulating more comprehensive sets of rules in maintaining ethical standards if they so desire.

c) The three (3) fundamental principles of the Code are:
   1) Members shall at all times conduct their businesses with utmost good faith and integrity.
   2) Members shall do everything possible to satisfy the insurance and/or takaful requirements of their clients and shall place the interest of their clients above all other considerations. Subject to these requirements and interests, Members shall have proper regard for others.
   3) Statements made by Members or on their behalf in advertisements shall not be misleading or false.

d) Members are the agents of their clients and, as such, they are subject to the general law as it applies to agents. The provisions of the Code of Ethics and Conduct are not intended in any way to derogate from the general law of agency.

GENERAL PRINCIPLES

1) In the conduct of their businesses, Members shall provide advice objectively and independently.
2) Members shall use, or permit the use of, the description " insurance broker" and/or "takaful broker" in connection with a business, provided the business is carried on in accordance with the requirements of the *Insurance Act 1996* and the *Takaful Act 1984* and the Constitution of the Malaysian Insurance And Takaful Brokers Association.
3) Members shall ensure that all work carried out in connection with their insurance and/or takaful broking businesses shall be under the control and day-to-day supervision of a qualified and experienced insurance and/or takaful broker and they shall do everything possible to ensure that their employees are made aware of this Code.
4) Members shall, on the request of their client, explain the differences in, and the relative costs of, the principal types of insurance and/or takaful which, in their opinion best suit a client's need.
5) Members shall ensure the use of a sufficient number of insurers/operators to satisfy the insurance and/or takaful requirements of their clients.
6) Members shall, upon request, disclose to any client who is, or is contemplating to become, the holder of a policy of insurance/certificate, the amount of broking commission/takaful brokerage paid under any relevant policy insurance/certificate. Likewise, the insurance broker and/or takaful broker must reveal to the client all additional fees to be charged in lieu of or in addition to commissions/brokerage for servicing the account.
7) Although the choice of an insurer/operator can only be a matter of judgement, Members shall use their skills objectively in the best interests of their client.
8) Members shall not withhold from the policyholder/participant any written evidence or documentation relating to the contract of insurance/certificate without adequate and justifiable reasons being disclosed in writing to the policyholder/participant.

9) Members shall inform and obtain confirmation from their client of the name of the insurer(s)/operator(s) with whom the contract of insurance/certificate is placed or is to be placed. This shall be done at the inception of the contract/certificate and any changes thereafter shall be advised at the earliest opportunity to the client.
10) Members must ensure that their employees do not engage in any business activity that conflicts or competes with the interests of the member firm.
11) Members must ensure completeness and accuracy of accounting records and reports.
12) Members shall maintain a separate bank account for all insurance premium/takaful contributions and claim moneys received on behalf of clients, insurers or operators and are prohibited from using funds from this account for their own expenses except their share of brokerage. The Rules on the operation of the Premium/Contribution & Claims Account as indicated in Appendix I attached to form part of this Code.
13) Premium/Contribution and terms exactly as quoted and as debited by the insurer or reinsurer/operator or re-takaful operator must be conveyed faithfully by the Member to its client. A Member is not allowed to alter any premiums/contributions or terms quoted without the prior knowledge and consent of the client and the insurer or reinsurer/operator or re-takaful operator, as the case may be.
14) Members are prohibited from negotiating any contract of insurance/takaful certificate with an insurer/operator not registered under the *Insurance Act 1996* or the *Takaful Act 1984*.
15) A Member must transmit funds between its client, insurer or reinsurer operator or re-takaful operator with minimum processing delay.
16) A Member must disclose all material facts as known to him in any negotiation and/or placement of any insurance or reinsurance cover takaful or re-takaful arrangement. Where a Member is an insurance broker or takaful broker as well as a reinsurance broker/re-takaful broker on the same risks, he must disclose this to all the parties concerned.

16.1.2 PROFESSIONAL INDEPENDENCE

1) Professional independence and integrity are fundamental to the insurance and takaful broking professions. Accordingly, Members shall inform all interested parties of any potential conflict of interest.
2) Members completing any proposal form, claim form, or any other material document on behalf of their client, shall do so truthfully and faithfully as instructed, and shall make it clear that all answers or statements are the client's own responsibility. The client should always be encouraged to check the details and be reminded that the inclusion of incorrect information may result in a claim being repudiated.
3) Members shall have proper regard for the wishes of a policyholder/participant or client who desires to terminate any agreement to transact business with them.

16.2 PROFESSIONAL ETHICS AND CONFIDENTIALITY

1) Membership of the Malaysian Insurance and Takaful Brokers Association is an honour and privilege which carries with it duties and responsibilities, which all Members should perform and be accountable for. In accepting membership of the Malaysian Insurance and Takaful Brokers Association, a Member is expected to be fair in all dealings with Insurers/Operators, as well as clients whose interests it must protect and promote as if they were its own.
2) The relationship between Members and clients is confidential and, whilst it is necessary to obtain all relevant facts relating to the insurance and takaful requirements of their clients, all confidential information shall not be disclosed to others beyond that which is material and solely necessary to obtain the insurance and takaful required.
3) Any information acquired by Members from their clients or from any other confidential sources in the course of their professional work is privileged and Members shall not, use or appear to use such information for personal advantage, or for the advantage of a third party, or disclose such information without the prior consent of their client unless there is a public duty or a legal or professional obligation or duty to disclose such information.
4) It is the duty of every Member to endeavour to protect its clients against fraud, misrepresentation or unethical practice in connection with all insurance and/or takaful transactions relating to its appointment as an insurance and/or takaful broker.

16.3 ENTERTAINMENT AND GIFTS

Employees of Members are prohibited from inducing clients in the form of cash or in kind, for the purpose of procuring business.

Employees of Members must not accept expensive entertainment from policyholders/participants or clients unless they are able to reciprocate, either personally or by obtaining reimbursement from their broking companies through a proper expense voucher.

However, Members may give, or Members' employees may accept, token gifts of nominal or no commercial value during festive seasons, provided the giving/acceptance of such gifts does not place the employees or the client in a compromising position, and if refusing the gifts would jeopardise Member/Client relations. Under no circumstances should gifts be given or accepted in the form of cash, bonds, negotiable securities, personal loans or airline tickets.

16.4 ADVERTISING AND PUBLICITY

1) When advertising their services, directly or indirectly, Members shall ensure that statements made in such advertisements and public announcements shall not be misleading or bring disrepute to the insurance and takaful broking professions.
2) Any advertisement made by or on behalf of Members on any matters relating to any insurers', reinsurers', operators' or re-takaful operators' products shall be limited to those given by the insurers, reinsurers, operators, or re-takaful operators as the case may be, provided such matters to be advertised must have been duly considered by the Member in his professional capacity.

3) Members shall display, in the office where they carry on business and to which the public has access, a notice to the effect that a copy of the Code is available upon request and that if a member of the public wishes to make a complaint or requires the assistance of the Association in resolving a dispute, he may write to the Malaysian Insurance And Takaful Brokers Association at its office at:
Unit 303, Block A, Pusat Dagangan Phileo Damansara II,
No. 15, Jalan 16/11, Off Jalan Damansara,
46350 Petaling Jaya, Selangor Darul Ehsan.
4) The words "Member of the Malaysian Insurance and Takaful Brokers Association" should be featured with the name of the Member in all advertisements.
5) Any director or employee of a Member, who is invited to address a public meeting or to write an article for publication on any aspect of insurance and takaful, or insurance and takaful broking, shall identify himself as being a director or an employee of a Member of the Association.

16.5 INSURANCE AND TAKAFUL BROKERS' ACCOUNTING STANDARDS

Members shall adhere fully to the Insurance and Takaful Brokers' Accounting Standards as per Appendix I, approved under Section 90 of the *Insurance Act 1996* and any subsequent amendments thereto.

16.6 INSURANCE AND TAKAFUL BROKERS' BROKERAGE/FEE SHARING GUIDELINES

Members shall adhere fully to the Insurance and Takaful Brokers' Brokerage/Fee Sharing Guidelines as per Appendix II, which are issued by Bank Negara Malaysia pursuant to Subsection 185 (2) of the *Insurance Act 1996*.

16.7 DECLARATIONS

1) **Declaration by All Directors and Executive Employees:** Within one month from receipt of advice by MITBA on the effective date of this Code of Ethics, Members shall secure from each employee including all Directors, a declaration as per Appendix III attached herein. In the case of a person to be employed, such declaration shall be obtained within seven (7) days from the date of appointment. All declarations must be submitted to MITBA within ninety (90) days from the date of such declarations.

2) **Declaration by Chief Executive Officer**: All applications for the annual renewal of membership shall be subject to receipt by MITBA of a cheque in payment of the subscription fee in the stipulated amount together with a declaration signed by the Chief Executive Officer in the form as per Appendix IV attached herein.

16.8 AMENDMENTS AND/OR CHANGES

Any amendments and/or changes to this Code of Ethics and Conduct shall automatically be binding and effective from the date such amendments or changes are approved by Members either through a circular resolution or at a duly convened Extraordinary General Meeting/Annual General Meeting.

16.9 MONITORING DEVICES

To ensure adherence to the Code of Ethics and Conduct, the management of Member companies must establish, as soon as possible, some effective monitoring devices. These should include the following:

1) The Management should assign responsibility to the head of various departments to ensure compliance with the Code on a day-to-day basis and to handle general enquiries from employees on matters relating to the Code of Ethics and Conduct. Breaches observed should be reported to the management and Disciplinary Committee and centralised records should be maintained.
2) Cases of fraud should be reported immediately to Bank Negara Malaysia and the Police.
3) The Management is required to a report to the Association on breaches observed during each financial year and the corrective/punitive action taken within ninety (90) days from the close of each financial year or any other period as determined by Bank Negara Malaysia.
4) The Management, namely the Chief Executive Officer of the Member company, under existing disciplinary mechanism in place within each company, would be responsible for the day-to-day compliance with the Code of Ethics and Conduct, including maintenance of centralised records. Accordingly, it would also be the responsibility of the Chief Executive Officer to ensure that reports on breaches during each financial year and the corrective/punitive actions taken are duly submitted to Bank Negara Malaysia within ninety (90) days from the close of each financial year or any other period as determined by Bank Negara Malaysia.

16.10 BREACHES OF THE CODE AMONGST MEMBERS

A Member who has knowledge of any breach or alleged breach of the Code of Ethics and Conducts amongst Members is required to report such breaches to the Disciplinary Committee of the Association.

16.10.1 BREACH OF CODE

Any breach or alleged breach of this Code shall be dealt with in accordance with Article 19 – Breaches of the Law, Articles, Rules of the Constitution, and Code of Ethics and Conduct of the Constitution of the Association.

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CHAPTER 17 NEW DEVELOPMENTS IN THE INDUSTRY

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CHAPTER OBJECTIVE

To understand the benefits of detariffication when it comes to Motor and Fire Insurance and learn why Malaysia has chosen the path of Liberalisation.

LEARNING OUTCOMES

After you complete this chapter, you should be able to:

- *Know a brief history of Tariff in Malaysia and the revisions brought about in the tariffs.*
- *Understand detariffication of Motor and Fire Insurance according to the BNM roadmap.*
- *Appreciate the benefits of detariffication and the road to Liberalisation.*

17.1 THE TARIFF IN MALAYSIA – A SHORT HISTORY

Given below is a brief history of the tariff in Malaysia:

- In the 18th & 19th centuries, insurances transacted in Malaysia were through trading houses acting for insurance companies from the U.K.
- These trading houses, e.g. Boustead and Harrisons & Crossfield were underwriting agents for large U.K.-based insurers such as Commercial Union and Guardian Royal Exchange.
- It was only in the sixties that insurers began to have their office in Malaysia.
- Thus the basic framework for fire and motor tariff was imported from the U.K.
- Due to unethical practices and poor underwriting, the insurance industry was unhealthy.
- The *Insurance Act 1963* was introduced, and it was under the purview of the Director General of Insurance which in turn was reporting to the Ministry of Finance. It was only in 1988 that the insurance industry came under Bank Negara Malaysia.

17.1.1 THE FIRE & MOTOR TARIFF

- Prior to 1985 the industry was not strictly regulated especially in terms of commission.
- Early 1980 witnessed unrealistic premium and excessive commission.
- The first transformation was to:
    - Reduce the commission allowed from as high as 65% + 15% for fire class I risk to 40% maximum.
    - To reduce motor insurance commission from as high as 45% to 10%.
    - Indirectly, motor underwriting agents were discouraged and eventually underwriting agents for fire & miscellaneous classes were also disallowed.
    - All these were achieved through the Inter-Company Agreement where the ceiling of commissions allowed was fixed and agreed by all insurers.
    - Technical and sound underwriting was encouraged.
- In the late eighties and early nineties, the underwriting results were horrendous and overseas reinsurers refused to write Malaysian treaties, after their treaties were burnt.
- As a result, the insurance industry had no choice but to seek consensus by fellow insurers, and guided by PIAM, to revise the tariff.

- The first revision was conducted in 1992, and the revised blue fire tariff was introduced on 1st April 1992.
- The revision in rate was based on 10 years' claim statistics and was applicable only to certain trades.

The green tariff which had been used for more than 40 years was finally replaced.

17.1.2 FURTHER REVISION OF FIRE TARIFF

- Between 1992 and 2000, the fire tariff had been reduced three times, with average rate reductions of 27.5%, 20.5% and 14.8% respectively.
- However, big corporations complained that their premium was too high, and as a result, the following were introduced:
    - The large and specialised scheme for a sum insured above RM 300 million was introduced in 1993 (which is actually detariffication for a small section).
    - Special rating and self-rating were introduced in 1997.
    - The self-rating limit was increased to RM 30 million in 2000 and RM 50 million in 2013.
    - Risks with a sum insured above the limit were referred to the PIAM rating committee.

17.1.3 RATING FACTORS USED IN MALAYSIAN FIRE TARIFF

Figure 17-1 ***Malaysian fire tariff rating factors***

Rating Factors	Base Premium	Loading/Discount
Occupation	X	
Construction	X	
Cover Required	X	
Hazardous processes		X
Fire extinguishing appliances (up to 12 types)		X
Age and height of building		X
Security/ housekeeping/ management		X
Large sum insured		X
Deductible		X

17.1.4 REVISION OF THE MOTOR TARIFF

- There has been no revision in motor tariff for more than 30 years despite the increase in the price of motor vehicles and spare parts. No consideration was provided for inflation.

- Although insurers had voiced their concerns, it was only on January 1, 2012 that Third Party Premium adjustments were allowed and permitted to be spread over a period of 4 years. The last adjustment was in February 2015.

17.1.5 RATING FACTORS USED IN MALAYSIAN MOTOR TARIFF

Figure 17-2 ***Malaysian motor tariff rating factors***

Rating Factors	Base Premium	Loading/Discount
Engine Capacity	X	
Class of use	X	
Cover Required	X	
Sum insured	X	
Claim free year (NCD)		X
Age of driver/driving experience/occupation		X
Age of vehicle		X
High performance vehicle		X
Multiple claims		X

Rates and loading/discounts carry values that may not reflect the actual risks

17.1.6 COMPARISON OF MOTOR RATING FACTORS

Figure 17-3 ***Comparison of Malaysian motor rating factors***

Developed markets *		Malaysia
1. Accident details	13. Garaging	1. Engine capacity
2. Additional driver details	14. Gender	2. Class of use
3. AD excess	15. Internet quotation	3. Cover required
4. Age of driver	16. Driving experience	4. Claim-free year (NCD)
5. Age of vehicle	17. Marital status	5. Sum insured
6. Area of residence	18. Mileage	6. Age of driver/driving experience/occupation
7. Area of use	19. Multi – policy discount	7. Age of vehicle
8. Bonus/ malus	20. Occupation	8. High performance vehicle
9. Class of use	21. Type of vehicle	9. Multiple claims
10. Conviction details	22. Value of vehicle	
11. Cover required	23. Vehicle modifications	
12. Driving restrictions	24. Vehicle security	

Market norm or regularly used

17.2 WHAT IS LIBERALISATION?

Liberalisation is the process of allowing freedom of pricing of insurance products; in particular, the removal of tariffs for the currently tariffed classes such as fire and motor.

Once detariffication sets in, consumers will be offered differentiated premium rates relative to their risk profile.

What are the Benefits of Detariffication

Detariffication offers the following benefits:

- A policyholder will enjoy flexible options to suit their insurance needs.
- Insurance premium will be reflective of the policyholders' risk profile, risk management and claims experience.

Which Insurance Products will be Detariffed as a Result of Liberalisation

- BNM had announced liberalisation as early as in 2013 for fire and motor insurance.

Why has Malaysia Chosen a Path of Liberalisation

The main objectives of BNM to implement detariffication are:

- **Differentiated rates according to risk profiles for cover not subject to tariff:** Generally, consumers with good risk profiles would enjoy lower rates than those with higher risks
- **Diversified channels of distribution:** To match consumer preferences with increased adoption of more cost-efficient channels, including the internet.
- **The expanded role of intermediaries:** Higher expectation on intermediaries to advise consumers on the purchase of appropriate products.
- **Higher efficiency level:** Healthy competition is expected to result in more efficient service level and greater product innovation that will deliver better value propositions for consumers.
- **A wider range of motor and fire products:** To meet the varied needs of Malaysian businesses and individuals, with continued access to existing products.

17.2.1 ROAD TO LIBERALISATION

BACKGROUND AND PLANNING

- Bank Negara Malaysia (BNM) announced in 2013 that Motor and Fire business would be detariffed in 2015.
- BNM advised PIAM and its members to start preparing a roadmap for liberalisation for BNM's consideration.
- The PIAM/MTA Joint Task Force (JTF) was requested by Bank Negara Malaysia (BNM) to submit its proposal on the liberalisation of the Malaysian general insurance and Takaful industry in late 2013.

17.3 ROADMAP FOR PHASING OUT TARIFFS

Figure 17-4 ***Roadmap for phasing out tariffs***

Timeline	Motor Business	Fire Business
Prior to 1 July 2016	▪ All available products are defined in the Tariffs and are subject to tariff rates ▪ Gradual adjustments to the tariff rates for identified risk groups	
Effective from 1 July 2016 onwards	**Flexibility in product offering** ▪ A licensed person shall continue to offer the same products that were being offered as at 30 June 2016. Such products shall be offered in accordance with the Tariffs ▪ A licensed person may introduce new products at premium or takaful contribution rates as determined by the licensed person (market rates)	
Effective from 1 July 2017 onwards	**Flexibility in product pricing** ▪ The pricing for Comprehensive and Third Party Fire and Theft products[1] will be liberalised. Licensed persons will be able to determine the premium or takaful contribution rates for such products **Third Party product to remain Tariffed** ▪ The pricing for Third Party product[1] shall be in accordance with the Motor Tariff and any pricing adjustments which the Bank may specify for identified classes of vehicle	**Gradual tariff adjustments** ▪ The pricing of fire products[1] specified under the Revised Fire Tariff shall be in accordance with the tariff and any pricing adjustments which the Bank may specify for identified categories of risks
From 2019 onwards	▪ The progress of the liberalisation will be reviewed to assess the impact of these measures and the readiness of consumers and the industry for further liberalisation	

17.3.1 DISRUPTIVE TECHNOLOGY

NEW THREATS

Detariffication brings along disruptive technology and the introduction of new competitors.

- Insurers are encouraged to sell online through the internet.
- Many insurers allow a 10% discount on the motor and a 15% discount on fire if the insurances are purchased online.
- Most insurers have a special bundled motor package for motor insurance purchased through their franchised motor dealers.
- A new threat comes from companies providing aggregators for insurers.
- Currently, new product features for motor insurance fire insurance have been offered in the market.
- All insurers are toeing the line whereby the risk-based rating allows them to reduce the premium by as much as 10%.
- For fire insurance, insurers have reduced the premium rate for certain occupational/trade codes by as much as 30% if the sum insured is RM10,000,000 or higher.
- ‘All risk’ property wordings and non-fire tariff clauses have been introduced by some insurers.
- Some insurers have introduced bundled policies for small and medium industries.
- Attractive insurance packages have also been offered to strata titled properties managed by Joint Management Committees.

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Head Office
The Malaysian Insurance Institute,
Level G, No 5, Jalan Sri Semantan 1, Damansara Heights, 50490 Kuala Lumpur, Malaysia.

MII City Centre @ Wisma Sime Darby
6th Floor of Wisma Sime Darby, Jalan Raja Laut, 50350 Kuala Lumpur, Malaysia.

Telephone : +603 2087 8882/3 | Fax : +603 2093 7885 | Email : customercare@mii.org.my

www.insurance.com.my