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CIBAFI

المجلس العام للبنوك والمؤسسات المالية الإسلامية
مؤسسة منتمية لمنظمة التعاون الإسلامي
تأسست بمرسوم ملكي رقم ٢٣ لسنة ٢٠٠١م

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Dear Mr. Ansari,

السلام عليكم ورحمة الله وبركاته،،

CIBAFI Comments on the AAOIFI Exposure Draft on Governance Standard "Principles of Assessment of Necessity for Obtaining Conventional Reinsurance by Takaful Institutions"

The General Council for Islamic Banks and Financial Institutions (CIBAFI) presents its compliments to the Accounting & Auditing Organization for Islamic Financial Institutions (AAOIFI) and takes this opportunity to express its appreciation of the work that the AAOIFI does to promote and enhance the Islamic financial services industry.

CIBAFI is the official umbrella for all Islamic financial institutions, whose services and products comply with the Shariah rules and principles. CIBAFI acts as the voice of the Islamic finance industry, and our members comprise more than 140 Islamic banks and non-bank financial institutions, both large and small, from more than 30 jurisdictions.

هاتف: ٣٠١ - ٣٠٠ ٣٥٧ ١٧ ٩٧٣+ فاكس: ٩٠٢ ٣٢٤ ١٧ / ٣٠٧ ٣٥٧ ١٧ ٩٧٣+ ص.ب: ٤٥٦ ٢٤ المنامة مملكة البحرين
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We welcome this opportunity to offer our comments and recommendations on the AAOIFI exposure draft (ED) on the Governance Standard (GS): “Principles of Assessment of Necessity for Obtaining Conventional Reinsurance by Takaful Institutions”. The comments contained in this letter represent the views of the CIBAFI Secretariat and feedback received from our members.

First: Unfortunately, Appendix B, the Basis for Conclusions, is absent. This is particularly problematic since there are points at which it is not easy to see how the conclusions have been reached. Some of these are mentioned below. We should welcome an opportunity to offer further comments when this Basis for Conclusions is available.

Second: the stated objective of the standard goes well beyond the words in the “overview (IN1)”, which suggests a focus on governance principles and internal control requirements. This is not simply a drafting point but reflects the fact that the ED itself goes well beyond governance and internal control requirements. Rather, the early part of the ED deals very largely with the substantive conditions under which conventional reinsurance may be permissible and is, in effect, a substantial elaboration on Shariah Standard 41 in particular. It is arguable that this goes beyond the proper function of a Governance Standard and should be issued, if at all, as a revision of the relevant Shariah Standard.

Third: Preface PR2 appears incomplete as it ends abruptly without concluding the sentence or thought. It appears that the paragraph is in need of a proper conclusion.

Fourth: the ED, in Para 6 (a), defines "necessity". This is a key concept within the ED, and the text here elaborates on the provisions of Shariah Standard 41. Some of this elaboration, for example, the distinction drawn between the interests of the participants and those of the institution, arguably does not belong in a Governance Standard and also needs justification. A further explanation of this might be appropriate; presumably it would have been in the missing Appendix B.

Fifth: The ED, in para 6 (c), defines “reasonable efforts” (to secure reTakaful) and in so doing refers to not incurring “significantly higher cost”. A footnote defines “significantly higher cost” as “33% or higher”, but no basis is given for this figure. Again, an Appendix B would have been helpful.

Sixth: the ED, in para 7-24, defines “core principles for the determination of necessity”. This whole section elaborates on how necessity is to be understood. As such, it is arguably more appropriate to a Shariah Standard than a Governance Standard.

Seventh: in Para 14-17, the ED stipulates minimum retention levels, however, the ED does not delve into the rationale behind the specific percentages. Providing further explanation of the underlying considerations and risk management principles would enhance the understanding of these requirements. For instance, elaborating on why different retention levels are applied to new versus established institutions and business lines would be valuable. (See the earlier comment about the absence of Appendix B.)

Eighth: the ED, in Para 18, recommends the use of co-Takaful arrangements before conventional reinsurance. It appears to envisage that other Takaful institutions may either share in the primary risk or cover part of it through re-Takaful arrangements. However, while syndication of risks is well-established for large commercial risks, it is much less common in the personal lines market, because consumers will not want to have to deal with multiple insurers in the event of a claim. It is also not appropriate as an alternative to excess of loss re-Takaful covering multiple policies (for example the risk of a windstorm causing losses under multiple household policies). As regards re-Takaful in these circumstances, it may be appropriate on a quota-share basis. However, for other forms of re-Takaful, the different risk profiles may raise issues of equity between directly and indirectly covered participants. We believe that further consideration needs to be given to this proposal and to the circumstances in which co-Takaful might be an appropriate response to the needs of participants.

Finally: in Para 19, the ED says that the party to a contract of conventional reinsurance should be the Participants' Takaful Fund (PTF) and not the Takaful institution. CIBAFI and its members note that not all jurisdictions would give a PTF the legal personality necessary to enter into a contract in its own name. Since reinsurance is an international business, there may also be a question of whether the PTF would be an acceptable party from the standpoint of the reinsurer. Some further consideration of the issue of legal capacity appears appropriate.

We would like to express our appreciation to AAOIFI for its great effort and commitment with respect to developing standards that accommodate the interest of the global Islamic finance industry. We are conscious that some of the points we have made could result in fairly substantial changes to the structure and content of the Standard, and we should be happy to participate in further consultation, whether formal or informal.

We remain at your disposal should you need any further clarifications on the above.

The General Council for Islamic Banks and Financial Institutions takes this opportunity to renew to the Accounting & Auditing Organization for Islamic Financial Institutions (AAOIFI) the assurances of its highest respect and consideration.

Yours sincerely,

Dr. Abdelilah Belatik
Secretary General

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