

REMEDIES FOR MISREPRESENTATIONS IN TAKAFUL CONTRACT: CURRENT INDUSTRY PRACTICE IN MALAYSIA

**DR. SITI SALWANI RAZALI^I
AHMAD FADHIL HAMDI MOHD ALI^{II}**

^IDepartment of Business Administration,
Kulliyyah Economics and Management Sciences,
International Islamic University Malaysia, Malaysia.

E-mail : salwani@iium.edu.my

^{II}Great Eastern Takaful Berhad, Malaysia.

E-mail : AhmadFadhlHamdiMohdAli@i-great.com.my

Received on 10-02-2021

Accepted on 20-08-21

Abstract

Takaful is a contract whereby the participants commit to contribute an amount of money to a specified fund to mutually guarantee each other in the unprecedented event of misfortune and appoint a takaful operator to manage that fund. In takaful contract, the participants have the opportunity to mitigate or reduce any possible risks that they or their families might face in case of any unpredicted event. As a requirement under Schedule 9 of Islamic Financial Services Act 2013 (IFSA), for individuals or institutions who wish to participate in a takaful contract, a takaful operator as a fund manager may ask certain material questions to underwrite the individual or institution. Under the principle of utmost good faith, it is the obligation of the takaful participant to disclose material matters to takaful operator. In the event of non-disclosure or misrepresentation by a takaful participant, Bank Negara Malaysia (Central Bank of Malaysia, hereinafter referred to as “BNM”) and IFSA have spelled out certain remedies that serve as minimum requirements to be implemented by takaful operators. Hence, some takaful operators may differ in the practices of remedies which are not specified by BNM and IFSA or implement more stringent and stricter remedies in addition to minimum requirements.

This research will provide *Shari'ah* justifications on the disclosure and representation requirements, and study the differences of Malaysia's takaful operators' practises in exercising remedies for misrepresentations in takaful contracts. Seven takaful operators in Malaysia were chosen and the data was gathered from the interviews made with the representatives of the respective companies. The misrepresentations, their types according to IFSA 2013 and the treatment from regulatory body in Malaysia, BNM, were also critically examined. This research focuses on remedies for misrepresentation with regard to termination of contract and refund of moneys only. Takaful operator's duty and other remedies will not be discussed in this research. The study concludes that very few deviations or non-compliances occur in Malaysian takaful market, and identifies that there is a need of policy statement from the regulatory body regarding the issue of unearned *wakālah* fee in cases of misrepresentations.

Keywords: Misrepresentation; Non-disclosure; Remedies; IFSA; *Tabarru'*; Takaful; BNM

1. Introduction

The best way to start with is to examine the takaful contract as a whole. Takaful comes from the Arabic root word *ka-fa-la*, which means to guarantee. Takaful is a practice whereby individuals in community jointly guarantee themselves against financial loss or damage. Takaful practices principles of brotherhood and mutual help for those who need it most in times of financial difficulties.

There are quite a number of models for takaful. One of them is hybrid takaful model of *wakālah - ju'alah* which is formed using the dripping of *tabarru'* (Arabic term which means donation) equipped with surplus sharing. This model is chosen due to the fact that this is the model used by some prominent takaful operators in Malaysia.¹

1.1. Process Flow of Family Takaful Model:

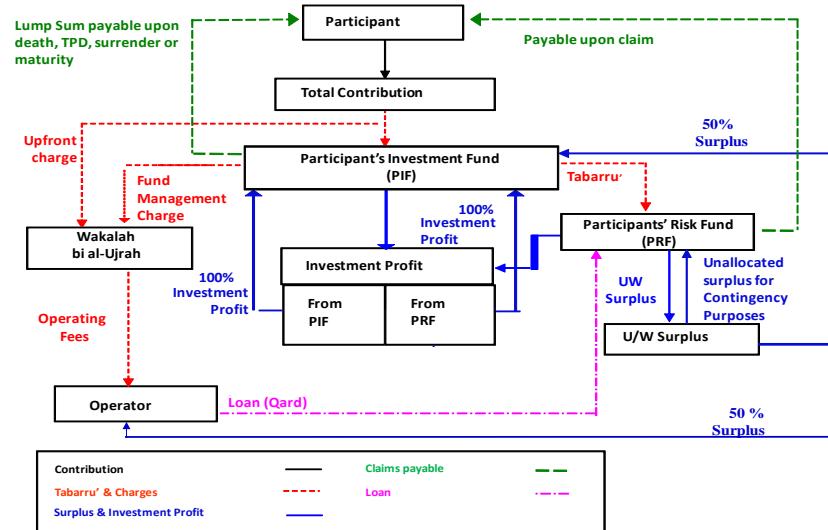


Figure 1: Process Flow of a *Wakālah-Ju'alah* Family Takaful Model in Malaysia

Based on the model, participant will give his/her commitment to contribute to the fund according to the risk carried. The contribution made will be deducted first as upfront charge before going into Participant's Investment Fund (PIF). The upfront charge is a *wakālah* fee which is payable because of the services and expertise that will be provided by the takaful operator. This is where the contract of *wakālah bi al-ujrah* (paid agency) takes place.

The money in PIF will then be dripped into Participants' Risk Fund (PRF). All of the money in PIF and PRF will be invested in *Shari'ah*-compliant portfolios. In this model, the contract used for investment is *wakālah bi al-istithmār* (investment agency). To invest on behalf of participants, the takaful operator can charge the participants for the fund management services rendered. In the model above, takaful operator charges the participant with a performance based Fund Management Charge (FMC). At the end of the financial year, 100% of the investment profit will be given and credited into PIF.

The *Shari'ah* concept applicable would be as follows²:

- i. *Tabarru'*: The amount of donation that the participants willingly relinquish in order to help each other in the events of misfortunes.
- ii. *Wakālah bi al-Ujrah*: The contract of agency where:
 - Participant authorises the takaful operator to manage PRF on behalf of him/her.

- The takaful operator will invest the monies in accordance to *wakalah bi al-istithmar* principle.

The takaful operator is entitled to receive fees for services rendered as agreed at the beginning of the contract.

iii. *Ju'alah*: Literally, it means compensation for a given service. Legally, it is a contract for performing a given task against a prescribed fee in a given period. *Ju'alah* concept is used in a situation where underwriting surplus is shared among the participants and the takaful operator. Entitlement to underwriting surplus depends on a completion of work and delivery of result.

iv. *Qard* (Loan): A loan which is returned at the end of the agreed period. For the purpose of takaful, in the event of deficit in the PRF, takaful operator will arrange for *qard*. The *qard* is repayable from the future underwriting surplus of the PRF.

For individuals and institutions who wish to participate in a takaful contract, a takaful operator that acts as a fund manager will impose certain requirements to them, which they need to disclose based on the concept of utmost good faith.

Utmost good faith or *uberrimae fidei* as defined by Carol Bennett is an obligation upon the insured to disclose material facts, i.e. facts that would influence the insurer before accepting the contract.³ The insurer must reciprocate but in practice, the duty weighs more heavily on the insured.⁴ Under this principle, it is the obligation of a takaful participant to disclose material facts or matters to the takaful operator.

Material matters are important to be disclosed in order to ensure the soundness of the takaful participant from the health and financial perspectives. A material matter is a fact that will influence the judgement of a prudent underwriting in deciding whether to accept a risk for insurance and on what terms⁵.

Participant is required to disclose material facts in two stages, during the new business stage and during contract length. New business is a stage where a takaful operator underwrites a proposer before he or she can be accepted as takaful participant while contract length is the time span during which the takaful participant participates in the takaful contract.

Underwriting in takaful industry is a process normally done by an underwriter that evaluates and assesses the risks that a particular person to be covered has. The evaluation results are subsequently used to determine the contribution for the proposer to participate in takaful contract. Proposer and person to be covered may be a same person, and could be different person.

Underwriting process includes answering relevant and material questions posed by takaful operator on medical conditions, financial situation and occupation type of the proposer. The completed forms will then be passed to the underwriters for evaluation.

Underwriting process aims to ensure fairness to each person covered. A covered person who possess higher risk than the other covered person should contribute more *tabarru'* to the PRF. This is because PRF is a collective fund owned by every person covered.

A takaful contract may span up to 99 years. During this period, the takaful participants should inform the takaful operator and disclose all the important details required by the takaful operator not only before the contract is signed but also after the contract has been in force. These changes include change of occupation type and place, increase in weight and other changes which might increase the participant's risk profile.

There could be instances where the participant fails to adhere to the principle of utmost good faith. This situation will lead to misrepresentation and non-disclosure event which may lead to the takaful certificate to be terminated and rejection of claims.

2. Research Objectives and Methodology:

The awareness of people regarding the need of takaful protection is quite phenomenal nowadays and this is reflected in the increased numbers of participants of the takaful especially in Malaysia. However, one of the problems which might be faced by the takaful operator is the misrepresentation in the disclosure of information of the participants in the takaful contract. The research objectives of this paper are as follows:

1. To provide *Shari'ah* justifications on the disclosure and representation requirements in Takaful Contract.
2. To study the differences of Malaysia's takaful operators' practices in exercising remedies for misrepresentations in takaful contract.
3. To examine the treatment of misrepresentations and its types according to IFSA 2016 and the treatment from regulatory body in Malaysia i.e. BNM.

Seven takaful operators in Malaysia were chosen and the data was gathered from the interviews from the representatives of the respective companies.

3. Literature Review

3.1. Definition of Disclosure, Non-Disclosure, Representation, and Misrepresentation

Currently there is no case law has been reported on the issue of non-disclosure or misrepresentation under Malaysian Law which has been decided by the court. That is among the reasons why the definition of misrepresentation can become a grey area which only can be understood or derived from the dictionary or the definition from the act specifically IFSA 2013.

One of the important factors to determine the full disclosure in takaful contract is the incorporation of the doctrine of utmost good faith. This doctrine requires all parties to reveal any information that may influence their decision to enter into a contract. In takaful the agents must disclose the details of the contract whereby the participants must disclose their details and all materials required by the takaful contract.⁶ Thus, it is duty of both contractual parties to exercise this doctrine and reveal all the information relevant before entering into the takaful contract. This is to ensure that the contract is entered into with clear conscience and full transparency to uphold the real spirit of takaful contract.

In a normal or traditional contract, the duty to disclose any material information of the parties to the contract may not really be of significance and sometimes may even not be required. On the contrary in Takaful contract the full disclosure on any information material to the contract i.e. financial background or medical history is very significant before the contract can be executed.⁷

Disclosure means the full disclosure of any information needed by the takaful operator whereas non-disclosure is defined as a failure to reveal facts, which are material to the subject matter of the contract.

Bennett, in his Dictionary of Insurance, explained non-disclosure as innocent non-disclosure by the proposer before the insurance contract has been concluded. If it relates to a material fact, the insurance will be voidable *ab initio* (void from the very beginning) at the option of the insurer. If the insurer exercises the option, the full premium will be returned.

For the sake of comparison, concealment from Bennett's definition is the wilful failure to disclose a material fact before the insurance contract is concluded. It is a breach of utmost good faith rendering the contract void *ab initio* and entitling the insurer to sue for damages for

deceit. If fraud is proved, the insured is not entitled to a return of premium.⁸

Therefore, it can be understood that any action of not revealing any material matter even though it is innocently made will be termed as non-disclosure, while if the action occurred deliberately, it will be known as concealment. Both will render the contract to be void.

However, the difference between the two terms lies in the returning premium; where for non-disclosure, the premium paid will be returned to the insured, while for concealment, the premium will not be returned; hence by the definition of Black non-disclosure and concealment cannot exist at the same time.⁹

As for representation, Bennett defined it as statement made by the insured to the insurer before the contract is concluded (which) if relating to a material fact, it must be true. Meanwhile, Black defined representation as a collateral statement of such facts or circumstances, relative to the proposed adventure, as are necessary to be communicated to the underwriters, to enable them to form a just estimate of the risks¹⁰.

Hence, representation is a truthful statement made by the insured or person covered to the insurer or takaful operator on the basis of utmost good faith; which gave the same connotation with term disclosure.

On the other hand, misrepresentation as defined by Black is a statement of something as a fact which is untrue and material to the risk, and which assured states knowing it to be untrue and with intent to deceive, or which insured states positively as true, not knowing it to be true, and which has a tendency to mislead¹¹.

However, misrepresentation is defined as any false statement that encourages a person or company to enter into a contract. Misrepresentation may be either fraudulent, *i.e.* deliberate intent to deceive, or innocent, *i.e.* the result of a genuine mistake.¹² Bennett is observed to concur with Clark's definition as Bennett have inserted two terms relating to misrepresentation which coincides with the Clark's definition. The first term is fraudulent misrepresentation and the second term is innocent misrepresentation. Fraudulent misrepresentation means when a false representation is made by a person) who knows it to be untrue, or who has no belief that it is true, or who is reckless as to its truth, whereas innocent misrepresentation means a representation that is neither fraudulent nor negligent.

From the elaborative definitions above, the authors believe that non-disclosure and/or concealment have lesser negative impact compared to misrepresentation because non-disclosure or concealment will lead to unknown information whereas misrepresentation will directly lead to misleading information.

As regards to the definition according to Malaysian Law, the reference will be made to IFSA 2013. IFSA 2013 only uses misrepresentation instead of non-disclosure, even though that the authors believe that the term non-disclosure was also commonly used in Malaysia's insurance and takaful industry before the introduction of IFSA in Malaysia.

Hence, for this paper, to provide consistency and avoid redundancy, the terms that will be used will be disclosure which is a duty of a participant; and misrepresentation will be used to refer to breach of duty of the participant in conforming to principle of utmost good faith.

3.2. Requirements of Duty of Disclosure and Remedies for Misrepresentation in IFSA

There are some criticisms which are made on takaful when *Shari‘ah* compliance by takaful companies seems to develop in much the same manner as other disclosure practices, that is, a tendency to comply with rules rather than with principles.¹³ A lot of research has been done especially on the takaful regulations in Muslim-majority jurisdictions where takaful is offered on a large scale, especially in the area of core takaful principles of good faith, disclosure, non-misrepresentation, insurable interest, reciprocity in claims handling and the ensuing remedies.¹⁴

Even though a lot of articles have been written on the general rules governing the takaful contract but not much is written on the specific issues on requirement of disclosure and remedies for misrepresentation in Takaful contract.

The insurance and takaful industry in Malaysia is currently governed by IFSA 2013 which has replaced the takaful Act 1984. The Act addressed the duty of utmost good faith which indicates that the Act has stressed greatly upon the full disclosure in the contract by every contracting party.¹⁵

When IFSA was introduced, the rights and relation of parties related to the pre-contractual duty were set out in Schedule 9 of IFSA. Schedule 9 of IFSA¹⁶ has been specifically designed to tackle the duty of disclosure and remedies for misrepresentation. Although Schedule 8 of IFSA¹⁷, paragraph 10 did mention about disclosure, it is not a subject of discussion here because it solely sets out rule on disclosure requirements to person who offers takaful, which fall under the duty of takaful operator and its agents.

In Schedule 9, part 2, IFSA lays out the pre-contractual disclosure and representations for takaful contracts. The participant's duty of disclosure shall be reflected by the participant's action in answering any specific questions that are relevant to the decision of the licensed takaful operator on whether to accept the risk or not as well as to determine the rates and terms to be applied. It is the duty of the participant to take reasonable care to avoid misrepresentation to the licensed takaful operator when answering the questions¹⁸.

For renewal of a takaful contract, the participant should also pay the duty of disclosure when answering additional questions, or confirming or amending previously disclosed facts.¹⁹

In Schedule 9, part 3, IFSA lays out the remedies for misrepresentations relating to contracts of takaful. Part 3 comprises paragraph 13 till 19 of Schedule 9 and only came into effect from 1 January 2015. For an uncomplicated grasp of the remedies, it could be visualised as under:

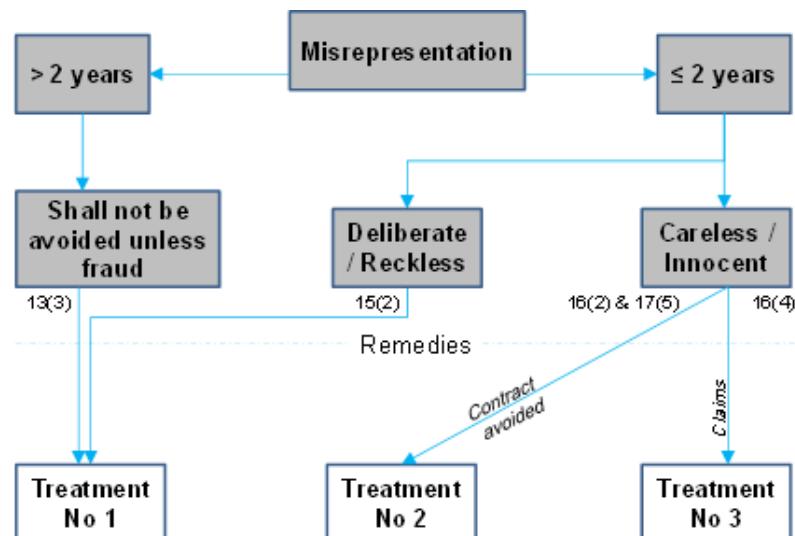


Figure 2: Classification of Misrepresentation and its Treatments*

*Figure 2 is to be read together with Table 1 below, under 2.3 BNM specification

IFSA divides misrepresentation into two; the first is takaful contract which has been in effect for more than two years, and second is takaful contract which has been in effect for a period of two years or less.

For family takaful contract which has been in force for more than two years, the contract cannot be avoided by family takaful operator although

a statement made or omitted is inaccurate, false or misleading unless the family takaful operator shows²⁰:

- i. that the statement was on material matter or suppressed a material fact; and
- ii. that it was fraudulently made or omitted to be made by the participant or person covered.

When a family takaful operator fulfils both of the requirements above, it can avoid the takaful contract as per subparagraph 13(3) of Schedule 9 by terminating the related takaful certificate along with returning moneys as specified by the BNM. This is treatment No 1.

For takaful contract which has been in force for a period of two years or less, IFSA further classified it into two categories; namely deliberate or reckless, and careless or innocent. A misrepresentation is deliberate or reckless if the consumer knew that²¹:

- i. it was untrue or misleading, or did not care whether or not it was untrue or misleading; and
- ii. the matter to which the misrepresentation related was relevant to the licensed takaful operator, or did not care whether or not it was relevant to the licensed takaful operator.

The remedies for deliberate or reckless misrepresentation which are under subparagraph 15(2) will also follow treatment number 1 as per specified by BNM in its letter which will be discussed later.

As for careless or innocent misrepresentation, if the nondisclosure or misrepresentation was made out of negligence with no knowledge of the misrepresentation, its remedies can be further divided into two; the first would be if takaful operator decides to avoid the contract, and the second if the takaful operator goes for avoiding the contract.

If takaful operator avoids the contract, treatment number 2 will be applied in which the certificate will be terminated and applicable moneys will be returned to the participant as specified by BNM.

In contrast, if a takaful operator did not avoid the contract until claim arises, treatment number 3 will apply as per subparagraph 16(4) and will be explained further below.

3.3. BNM Specification

On the returning moneys policy specified for all three treatments, IFSA has given the power to BNM to dictate the portion of moneys applicable to be returned. Hence, BNM in its letter to all takaful operators on 19th December 2014 has made a specification (hereinafter BNM

Specification) to the five applicable subparagraphs 13(3), 15(2), 16(2), 16(4) and 17(5). The Specification is as per table below²².

No.	Types of Misrepresentation	Specification on Remedies/Treatments
1	Deliberate or reckless misrepresentation	<p>(i) Pursuant to subparagraphs 13(3) and 15(2), the amount of money returnable to a takaful participant for a contract avoided by a takaful operator shall consist of the following:</p> <ul style="list-style-type: none"> a) initial contribution in PIF after deduction of <i>tabarru'</i>, excluding profits; and b) unearned <i>wakālah</i> fee. <p>(ii) Profits mentioned above shall be channelled to charitable organization(s) approved by the takaful operator's <i>Shari'ah</i> Committee. This is pertinent to <i>Wakālah</i> and <i>Ju'alah</i> models</p>
2	Careless or innocent misrepresentation	<p>Pursuant to subparagraph 16(2) and 17(5), the amount of money returnable to a takaful consumer for a contract avoided by a takaful operator shall consist of the following:</p> <ul style="list-style-type: none"> (i) value of his own contribution into the PIF, including profits; (ii) all contribution allocated into the PRF, and; (iii) unearned <i>wakālah</i> fee.

No.	Types of Misrepresentation	Specification on Remedies/Treatments
3	Amount to be paid on a claim due to careless or innocent misrepresentation	<p>Pursuant to subparagraph 16(4), the takaful operator may reduce proportionately the amount to be paid on a claim as may be specified by BNM. The amount to be paid on such claim shall be computed as follows (For investment-linked products, the top-up or investment contribution should be excluded from the computation.):</p> $\left[\frac{TC \text{ actually charged}}{TC \text{ that would have been charged}} \right] \times Contract \text{ Claim Amount}$ <p>*TC refers to takaful contribution.</p>

Table 1: Specification on moneys payable by takaful operator due to misrepresentation

For instance, if the takaful operator found out that Participant X has made a deliberate misrepresentation, so treatment number 1 will apply. Assume that Participant X opted for annual payment and the case was found out in the 10th month after the certificate has been in force, the amount associated with the case is as below:

- a) Annual Contribution : RM 100 x 12 = RM 1,200
- b) *Wakālah* Fee : RM 50 x 12 = RM 600
- c) Earned *Wakālah* Fee : RM 50 x 10 = RM 500
- d) Unearned *Wakālah* Fee : RM 50 x 2 = RM 100
- e) *Tabarru'* : RM 40 x 10 = RM 400
- f) Investment Profit : RM 2 x 10 = RM 20

As per treatment No.1, the moneys returnable to Participant X will be:

$$\text{Initial Contribution in PIF} = a - b = \text{RM 600}$$

- deduct *Tabarru'* = RM 600 - e = RM 200.
- add Unearned *Wakālah* Fee = RM 200 + d = **RM 300**

As for Investment Profit, the RM 20 will be channelled to any charitable organisation.

From calculation above, Participant X is not entitled to get Earned *Wakālah* Fee, *Tabarru'* and Investment Profit.

For Treatment number 2, let us take an example if the takaful operator found out that Participant Y made an innocent misrepresentation and both parties decided to terminate the takaful contract. For purpose of illustration, let us assume that the assumption for Participant Y is the same with the case of Participant X above. The moneys returnable to Participant Y would be:

Value of Contribution into PIF = a – b = RM 600

- include Investment Profits = RM 600 + f = RM 620
- plus *Tabarru'* = RM 620 + e = RM 1,020
- plus Unearned *Wakālah* Fee = RM 1,020 + d = **RM 1,120**

From calculation above, Participant Y is still entitled to *Tabarru'* and Investment Profit, however Earned *Wakālah* Fee is still owned by takaful operator. This is comprehensible considering that works have been carried out by takaful operator based on the contract sealed.

As for treatment number 3, if takaful operator found out during claim processing that Participant Z carelessly made a misrepresentation, the claim pay-out will be reduced proportionately. Example is as follow:

a) Contribution actually charged	: RM 1,200
b) Contribution that would have been charged	: RM 1,800
c) Claim amount	: RM 30,000

The claim payout would be: $\frac{1,200}{1,800} \times 30,000 = \text{RM 20,000}$

Hence, instead of being paid RM 30,000, Participant Z only receives RM 20,000 as claim.

4. Discussion:

As observed, the remedies are different based on the types of misrepresentation. The question is why the remedies are specified differently? From *Shari'ah* perspective, it is apparent that the reason of the different remedies is to ensure justice prevail by taking intention of the participant into account.

In a famous authentic hadith by 'Umar al-Khattab (*Rađi Allah 'anhu*), Prophet *Hađrat Muhammad Rasūlullah Khātam un Nabiyyīn Ṣallallahu 'alaihi wa 'alā Ḥalihi wa Aṣḥābihi wa Ṣallam* said:²³

"Actions are only (accurately assessed in light of) intentions and every person will earn what he intended."

In his comments on the hadith, Ibn al-Qayyim²⁴ wrote that the first part of the hadith states that an action will not be valid without accompanying with intention, while the second part explains that those who do an action will be requited according to their intention.

Likewise, the same should be applied in the issue of misrepresentation. The remedies should be determined based on the intention of the participant to avoid injustice. If the misrepresentation is deliberate, we could observe that BNM penalised the participant by not giving his *tabarru'* and profit back. However, if the participant innocently had no intention to make a misrepresentation, the *tabarru'* and the profit will be given back accordingly.

This specification from BNM coincides with an Islamic legal maxim which states:

The fundamental requirement in every contract is justice.

Ibn Qayyim wrote that in every contract, justice is fundamental as it is the one principle that Allah Almighty's messengers being sent and holy books being revealed for. He then quoted a Quranic verse:

We have indeed sent Our messengers with clear proofs, and sent down with them the Book and the Balance, so that people may uphold equity. And We sent down iron in which there is strong power, and benefits for the people; and (We did it) so that Allah knows the one who helps Him and His messengers without seeing (Him). Surely Allah is Strong, Mighty.²⁵

In the context of Islamic finance, justice or fairness refers to fulfilment of all financial rights and obligations at the minimum level²⁶. If the minimum level is breached (which in this case, misrepresentation happens), adequate remedies or treatment should be provided to ensure fairness among the contracting parties. The author acknowledges that the writings on this issues are very limited and the main purpose of the article is to concentrate more on the market practice/Takaful operator treatments towards misrepresentation and its adherence to the regulations of IFSA 2013 and BNM.

4.1. Disclosure and Misrepresentation from *Shari'ah* Point of View

The Holy Qur'an as one of the main sources of *Shari'ah* specifies commandment to utter words of truth as per verses below:

*O you who believe, fear Allah, and speak in straightforward words. (If you do so,) Allah will correct your deeds for your benefit, and forgive your sins for you. Whoever obeys Allah and His Messenger achieves a great success.*²⁷

These verses mean that a believer should speak the truth because the word “**سَدِيقًا**” means telling the right things²⁸. In takaful, this can be reflected by requirements that participants need to speak the truth and disclose their health condition and other related information that need to be disclosed such as risk type of the occupation. This requirement is important in takaful to uphold fairness among participants in the *tabarru'* fund. In addition to that, the following hadith also gives out a similar vibe:

*Truthfulness leads to “Al-Birr” (piety, righteousness, and every act of obedience to Allah) and Al-Birr leads to Paradise. And a man keeps on telling the truth until he becomes a “Siddiq” (truthful person). Falsehood leads to “Al-Fujur” (i.e. wickedness, evil-doing, etc), and Al-Fujur leads to (Hell) Fire, and a man keeps in telling lies till he is written as a liar before Allah.*²⁹

One of the ways of being truthful is when the statement made exactly matches the reality. Hence, the participant must disclose every material facts based on queries by takaful operator which is parallel with the actuality.

From the explicit understanding of the verses mentioned earlier, person who purposely wants to join takaful, he or she must disclose all the health details and lifestyle in the proposal form. The participant must state if he or she does receive any medical treatment, suffering from physical impairment, infirmity, congenital abnormality or any other material disclosure in proposal form to get takaful protection. The occupation type and financial situation should also be disclosed.

Absence in implementation of disclosure in takaful will give bad consequence to the *tabarru'* fund. This is because sustainability of *tabarru'* fund is calculated by actuarial department based on the risk carried by all the persons covered and claim history. From the sustainability calculation, takaful operator sets out the suitable amount of contribution based on age, occupation, and health condition of the participant. If a group of participants did not properly disclose material matters, claims experience may fluctuate, hence *tabarru'* fund will deplete faster than it should.

As a result, takaful operator may use shareholders' money to recover the claim made and pump in the money into *tabarru'* fund. From *Shari'ah* point of view, this circumstance will lead to takaful operator being the one that insures the person covered, which will be tantamount to breaching the real takaful contract structure.

Furthermore, takaful should be based on fairness because it is a fact that all participants do not know each other and come from all walks of life. Islam has ordered its followers to always be fair and prevent all forms of tyranny, injustice and aggression. Allah Almighty said in *The Holy Qur'an*:

Allah enjoins to do justice and to adopt good behaviour and to give relatives (their due rights), and forbids shameful acts, evil deeds and oppressive attitude. He exhorts you, so that you may be mindful.³⁰

Justice plays its role in individual and collective life. In takaful industry, as a participant, they need to prepare themselves to be fair with others especially in applying for a takaful protection.

Thus, it is significant from *Shari'ah* perspective to disclose material matters to takaful operator. This will ensure *Shari'ah* compliance of the Takaful contract which the Takaful seeker entered into in the first place.

4.2. Malaysian Market Practice in Remedies for Misrepresentation

A market research had been conducted to see takaful operators' practice in remedies for misrepresentation. The researchers have conducted the interviews with seven representatives from seven takaful operators in Malaysia. The research findings are as follows:

No.	Takaful Operator	Practice of Takaful Operators with Regards to Remedies for Misrepresentation
1.	Takaful Operator A	<ul style="list-style-type: none"> • Slightly different from BNM Specification • No difference of treatment between deliberate/reckless and careless/innocent. • Money returnable to participant are as follow: <ol style="list-style-type: none"> 1. Account value in PIF (including profits) 2. <i>Tabarru'</i> 3. Unearned <i>wakalah</i> fee

No.	Takaful Operator	Practice of Takaful Operators with Regards to Remedies for Misrepresentation
2.	Takaful Operator B	<ul style="list-style-type: none"> • In accordance with BNM Specification • If remedies differ with the Specification, it will be dealt on case-to-case basis subject to <i>Shari‘ah</i> Committee’s decision.
3.	Takaful Operator C	<ul style="list-style-type: none"> • In accordance with BNM Specification • For deliberate or reckless misrepresentation, <i>tabarru‘</i> amount and profit are not returnable.
4.	Takaful Operator D	<ul style="list-style-type: none"> • In accordance with BNM Specification • For deliberate or reckless misrepresentation, <i>tabarru‘</i> amount and profit are not returnable.
5.	Takaful Operator E	<ul style="list-style-type: none"> • Slightly different from BNM Specification • For takaful products with PIF, in case of deliberate/reckless misrepresentation, types of money returnable to participant are as follows: <ol style="list-style-type: none"> 1. Account value, or Initial Contribution in PIF after deduction of <i>tabarru‘</i>, excluding profits (whichever is lower) 2. Unearned <i>wakālah</i> fee • For takaful products without PIF, in case of deliberate/reckless misrepresentation, money returnable to participant are as follow: <ol style="list-style-type: none"> 1. Unutilized <i>tabarru‘</i> 2. Unearned <i>wakālah</i> fee
6.	Takaful Operator F	<ul style="list-style-type: none"> • In accordance with BNM Specification • For deliberate or reckless misrepresentation, <i>tabarru‘</i> amount and profit are not returnable.
7.	Takaful Operator G	<ul style="list-style-type: none"> • Slightly different from BNM Specification • For deliberate or reckless misrepresentation, <i>tabarru‘</i> amount and profit are returnable. • However, this will subject to the investigation finding.

Table 2: Practice of takaful operators with regards to remedies for misrepresentation

Researchers have received responses from seven (7) takaful operators. The names of takaful operators are not disclosed as per the request of takaful operators and for confidentiality purposes. Out of those

seven (7), four (4) of them, takaful operators B, C, D and F declared that they strictly follow the BNM Specifications. Below is the ratio between different practices of the remedies:

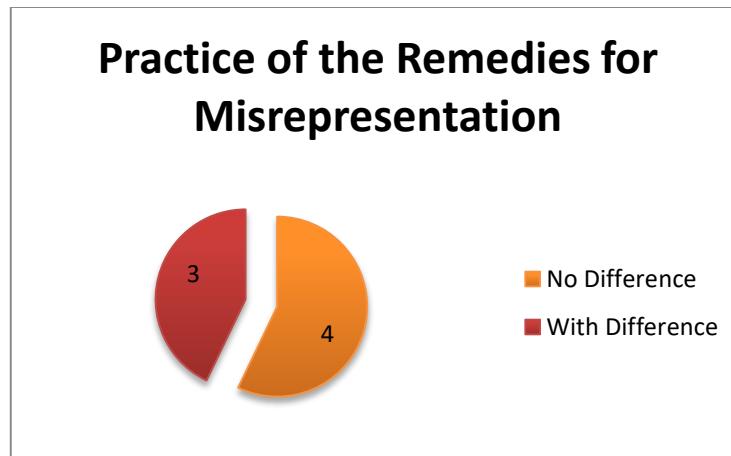


Figure 3: Ratio of takaful operator with regards to their remedies as compared to the BNM specifications.

In addition to that, takaful operator B clarifies that there were instances where cases of misrepresentation are being brought to the attention of their *Shari'ah* Committee (SC). This is to seek the SC's approval especially where the remedies are not as per the standard operating procedure (SOP) or BNM Specifications.

As for the remaining three takaful operators in which their remedies have slight differences compared to BNM Specifications are Takaful Operators A, E and G. For takaful operator A, they regard remedies 1 and 2 as the same. This is because their SC has passed down a resolution that in case of misrepresentation regardless of the intention, takaful operator should return total account value in PIF (including profit), *tabarru'* amount and unearned *wakalah* fee.

This is on the basis that the participant in the first place is not eligible to participate in the takaful, hence *tabarru'* should be retuned back to the participant because they are not supposed to contribute to the fund. This ruling is as per an Islamic legal maxim: *When a thing becomes null and void, what is included in it becomes null and void too.*

Ibn Nujaim in elaborating the above maxim gives several examples which also have been further explained by Ahmad al-Hamwi al-Hanafi³¹. Two of the examples are:

1. A husband renews the marriage contract with his wife. Because the renewal contract itself is considered invalid, the husband would not have to pay any dowry for the new contract.

2. A buyer buys a pillow and a carpet which are yet to be knitted without specifying the delivery date. In this case, this *bai' ta'ati* is considered null or void. [*Bai' ta'ati* is a type of sale contract which usually happens with inexpensive goods (such as grocery items) in retail transaction. Both the buyer and seller enter into a transaction without both parties declaring that they are buying and selling, except the action of the buyer taking goods away and the seller accepting the payment. This type of sale contract is permissible.] Hence, if the seller knitted the pillow and the carpet, and subsequently delivers it, there is still no contractual obligation between the parties. (As such, the buyer should not pay anything if he does not want the pillow and carpet.)

From these examples, we now know that if the contract itself is not executed in the first place (which in the examples are the marriage and *bai' ta'ati* contract), the matter accompanying it should not be executed (which are the dowry and the price of the pillow and carpet). For example the elements of contract are missing, i.e no *ijāb* (offer) or *qubūl* (acceptance). Hence, the same can be applied in a takaful contract whereby the *tabarru'* will be returned to the participant in case the takaful contract is void *ab initio* regardless whether the participant has an intention to misrepresent or not.

On the other hand, any profit realised should be returned to the participant too because takaful and investment in the takaful model is actually two separate contracts. It is true that the participant is not eligible to participate in the takaful, however, the participant should be eligible to be a party in an investment contract.

This separation of contracts is clear cut whereby *tabarru'* pooled in the PRF is used for takaful protection among participants, and the contribution which resides in an individual PIF is for investment. If the contract is void, the investment contract in PIF is still considered valid as there was no breach made by neither participant nor takaful operator.

In a takaful arrangement, participant has agreed to appoint takaful operator to manage his PIF and collective PRF for investment and for protection respectively. Although it is true that the takaful contract has been void *ab initio* (because of misrepresentation), the investment contract should still be in effect as it has been clearly documented. It is unreasonable to disregard both the investment contract and the

participant's entitlement to his profit as it has been clearly stated in the investment contract.

Hence, although automatically, the investment contract is terminated (due to misrepresentation in takaful contract), participant still hold the right to get the profit of the invested PIF.

For Takaful Operator E, their difference in the remedies is on the perspective of the types of family takaful product. Takaful operator E offer two types of family takaful product; the first one is the model which has PIF in place, and the other one without PIF. Other takaful operators might have the same types of takaful products. Notwithstanding that, there are takaful operators that offer this type of product (without PIF) only for group takaful plan as it is solely for protection. Normally, the one without PIF focuses solely on protection without investment or saving function.

For takaful products with PIF, in case of deliberate or reckless misrepresentation, the money returnable to participant is either total account value or initial contribution in PIF after deduction of *tabarru'* (whichever is lower) and unearned *wakālah* fee. The profit will not be returned to the participants and will be channelled to charity by takaful operators.

Takaful Operator E claims that the participant's total account value can sometimes be lower than the initial contribution minus *tabarru'* and profit mainly due to *wakālah* fee. This is something new because BNM did not mention about this account value in their specifications. Takaful operator E takes this stance in view that it is not in the best interest of the takaful operator E to top up the remaining amount (if let say that they have to return the initial contribution excluding *tabarru'* and profits which is higher than total account value), especially when the blame in these cases is on the participant. This is reasonable considering that works have been carried out by the takaful operator.

For takaful products without PIF, in case of deliberate or reckless misrepresentation, money returnable to participants are unutilized *tabarru'* and unearned *wakālah* fee. This is as expected since this type of product did not have PIF, hence the *tabarru'* yet to be utilized should be returned. However, *tabarru'* utilised should not be returned as per BNM specifications. Notwithstanding that, the practice of takaful operator A above on which they return the full *tabarru'* amount regardless utilized or unutilized even though the participant made a deliberate misrepresentation is not wrong either as BNM permits them to do so.

This is due to directive that BNM has issued. As long as the remedies and the treatment adopted by a takaful operator to refund more than what

has been specified in the BNM specifications, there is no restriction. BNM specifications is a minimum requirement set by BNM for takaful operators to comply with.

5. Limitations:

The study broadly focuses on the theoretical aspects of the misrepresentations. However, deeper market scenario with analyses, numbers and figures may be discussed in further research.

6. Conclusion

The researchers have come to the conclusion that, no deviation or incompliance towards BNM specifications took place throughout industry albeit there are notable differences. After taking into consideration the objective of BNM specifications is obviously to ensure uniformity in the practice of takaful operators in dealing with claims or money returnable. Slight differences which have no significant effect should do no harm.

From compliance perspective, unearned *wakālah* fee should be detailed out by the authority to ensure that the implementation of treatment for the remedies is correct. As from *Shari‘ah* point of view, *wakālah* fee should be realised monthly on the basis that it is the takaful business norm in Malaysia in which the shortest contribution payment mode is monthly basis. Hence, the unearned *wakālah* fee is the *wakālah* fee for the future months.

In addition to that, as there are no explicit specifications from regulator on the unearned *wakālah* fee definition, takaful operators may propose to their *Shari‘ah* committee not to include incurred expenses as unearned *wakālah* fee. These incurred expenses such as agents’ commission and management fees are real costs. Another important point to note is that the purpose of disallowing misrepresentation is to make sure that the contract of takaful entered into is made with transparency so that all parties to the takaful contract namely takaful operator and all participants are treated with fairness and justice and no injustice may occur to any parties involved.

From the paper, we may understand the need of having this research to interpret and realize the objectives of takaful as a whole. However, the study is limited to the jurisdiction of Malaysian country due to the fact that Malaysia is considered as a significant hub for Islamic Banking and takaful with robust regulatory framework governing the industry. Most

importantly it is hoped that other countries may gain a lesson from the Malaysian current industry practice especially relating to treatment of misrepresentation issues in takaful. In the future further study can be made on this issue beyond jurisdictional or geographical boundaries so that we can learn from each other in order to uphold the spirit of takaful in its true sense and to comply with the *Shari'ah* sanctity of the takaful contract.

Notes and References

¹ “The Great Eastern Takaful Company Malaysia” <https://www.greateasterntakaful.com/en/index.html>, accessed on 13-06-2021; “Etiqa Takaful Malaysia”, <https://www.etiqa.com.my/v2/homepage>, accessed on 13-06-2021; “Prudential BSN Takaful Malaysia”, <https://www.prubsn.com.my/en/>, accessed on 13-06-2021

² Great Eastern Takaful Berhad. *Product Disclosure Sheet*, 1.

³ Carol Bennett, *Dictionary of Insurance 2nd Edition*. (Great Britain: Financial Times Prentice Hall, 2004), 314.

⁴ Bennett, *Dictionary of Insurance*, 314.

⁵ International Centre for Education in Islamic Finance (INCEIF), *Takaful: Realities and Challenges*, (Selangor: Pearson Malaysia Sdn Bhd., 2012), 292.

⁶ Daniel Liberto, Doctrine of Utmost Good Faith, Investopedia, <https://www.investopedia.com/terms/d/doctrineofutmostgoodfaith.asp#>, accessed 05-02-2021.

⁷ Low Peh Fern, Don't Cover Up It Will Blow Your Cover, SKRINE Insight Newsletter, (Dec 2016), <https://www.skrine.com/insights/newsletter/december-2016/don-t-cover-up-it-ll-blow-your-cover!>, accessed February 2021.

⁸ Bennett, *Dictionary of Insurance*, 70.

⁹ Henry Campbell Black, *Black's Law Dictionary (Revised Fourth Edition)*, (USA: West Publishing Co., 1968), 1152.

¹⁰ Black, *Black's Law Dictionary*, 1465.

¹¹ Black, *Black's Law Dictionary*, 1152.

¹² John Clark, *Dictionary of Insurance and Finance Terms*, (Kuala Lumpur: SAM Publishing Sdn Bhd., 2000), 223.

¹³ Nor Aziah Abu, "Disclosure of Shariah compliance by Malaysian Takaful Companies", *Journal of Islamic Accounting and Business Research*, 3 no. 1, (2012),20-38.

¹⁴ Haemala Thanasegaran and Mohammad Shaiban, "Harmonisation of Takaful Regulations, A Realistic Goal or Improbable Deal", *Singapore Journal of Legal Studies*, no.(Dec 2014), 328–354.

¹⁵ Haemala Thanasegaran, *Good Faith in Insurance and Takaful Contracts in Malaysia*, (Springer, 2016),2.

¹⁶ Islamic Financial Services Act 2013, Schedule 9, “Pre-Contractual Disclosure and Representations, and Remedies for Misrepresentations”, 83.

¹⁷ IFSA 2013, Schedule 8, “Provision Relating to Takaful Certificates”, 82.

¹⁸ IFSA 2013, Schedule 9, Sub-para 5, (1) – (2),168.

¹⁹ IFSA 2013, Schedule 9, Sub-para 5, (4), 168.

²⁰ IFSA 2013, Schedule 9, Sub-para 13, (2), 172.

²¹ IFSA 2013, Schedule 9, Sub-para 7, (4), 170.

²² IFSA 2013, Schedule 9, “*Pre-Contractual Disclosure and Representations, and Remedies for Misrepresentation of the Islamic Financial Service Act 2013 (IFSA) – Specification Pursuant to Schedule 9*”, Bank Negara Malaysia to all Chief Executive Officer of every takaful operators dated 19 December 2014.

²³ *Sahīh Bukhāri* (1:1), Book of Hadith, trans. Muhammad Muhsin Khan, (Riyadh: Darussalam Publishers and Distributors, 1997).

²⁴ Ibn Qayyim, *I'lām al-Mūqi 'īn*, Vol 3, (Beirut: Dar al-Kutub al-'Ilmiyyah, 1991), 91.

²⁵ *The Meanings of the Holy Qur'ān* (57:25), translated by Mufti Muhamad Taqi Usmani, (Karachi: Maktaba Ma'ariful Quran, 2010).

²⁶ Mohamad Akram Laldin, *Islamic Legal Maxim and Their Application in Islamic Finance*, (Kuala Lumpur: ISRA., 2013), 22 – 23.

²⁷ Usmani, *The Meanings of the Holy Qur'ān* , (33:70-71).

²⁸ Ibn Manzur, *Lisān al-Arab*, 2nd edition, vol 3, (Beirut: Dar Soder, n.d.), 210.

²⁹ Khan, *Sahīh Bukhāri*, (69:6094).

³⁰ Usmani, *The Meanings of the Holy Qur'ān*, (16:90).

³¹ Ahmad al-Hamwi al-Hanafi, *Ghamzu 'Uyun al-Basairi fi Sharhi al-Ashbahi wa an-Nazā'ir*, vol. 4, (Beirut: Dar al-Kutub al-'Ilmiyyah, 1985), 156.