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# Challenges of developing Annuity Schemes for Takaful Providers

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## Where we were last year

- A huge market in Retirement related Takaful products. Population is aging. Baby boomers have started to retire.
- Industry (Takaful & Islamic Capital market players), Sharia and the Regulator (in Muslim countries) need to work together to address the 'missing links' to an efficient and affordable Takaful solution for the individual's retirement needs.
- Can we afford to retire? Or should the question be should there be a change in our working lifestyle?

# Takaful Annuity Experience in Malaysia

## The First and Only Takaful Annuity in Malaysia (perhaps the world?)

- The takaful annuity scheme was introduced in 2000 as part of the State Provident Fund (the EPF) efforts to allow its members to diversify their investment
- In particular, the EPF was concerned with the trend of utilisation of funds (a lump sum was paid at age 55) by retirees where it was found that 70% of their retirees spend the entire savings within 10 years of retirement.
- So the annuity option was a natural choice to mitigate the risk of outliving one's savings and participating members can expect retirement income for life
- Konsortium Anuiti Malaysia comprising 6 conventional insurers and 2 takaful operators were approved by the EPF and the insurance regulator to offer these annuity
- Within a year which the products were launched, nearly USD 1.5 billion (conventional included) was collected from over 200,000 EPF members despite negative press about these products
- However, despite the success the sale of the annuity product was cancelled 18 months from its introduction

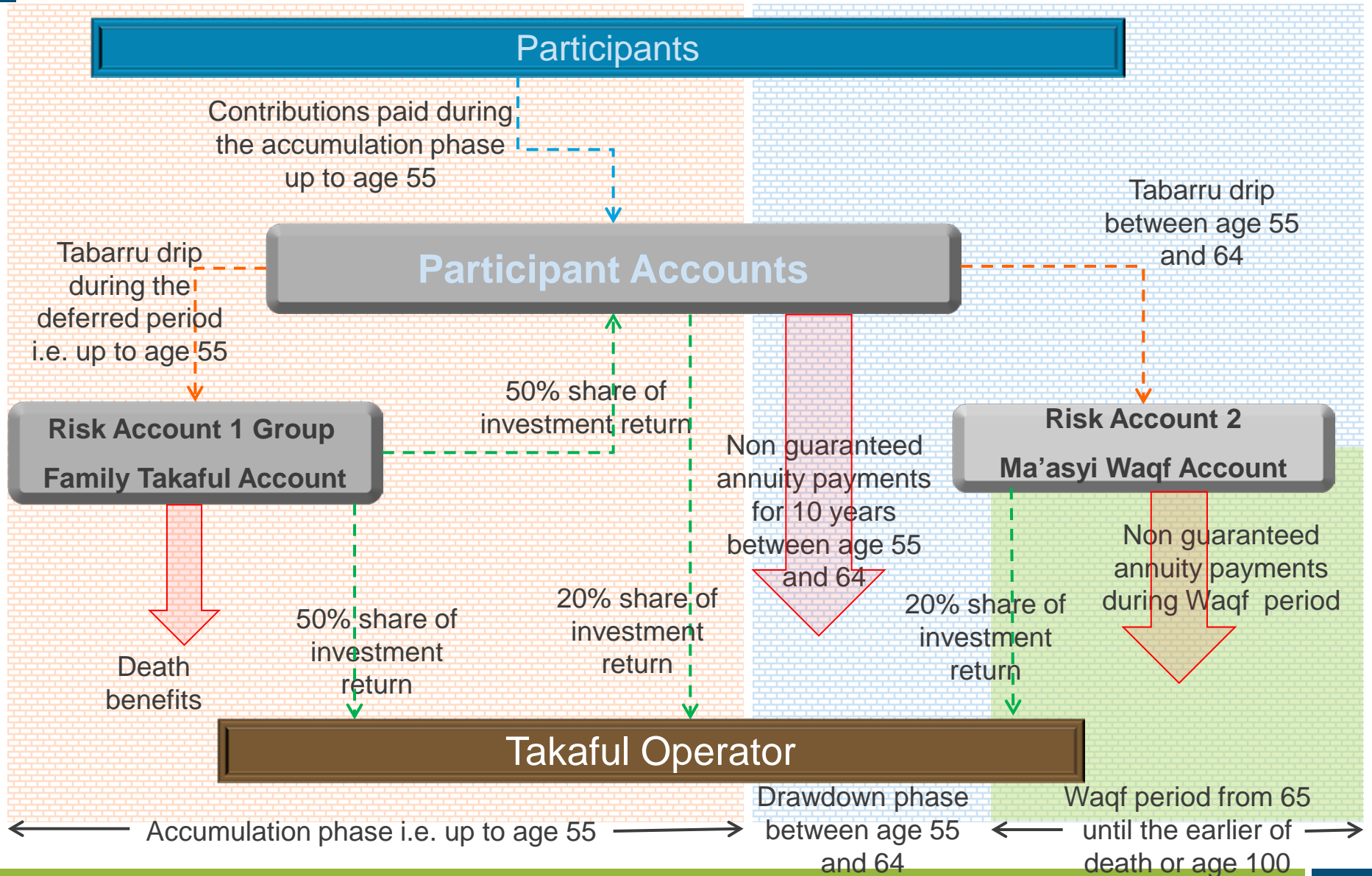


**Skim Anuiti Takaful  
Keluarga (SATK)**

**Skim Anuiti Konvensional  
Keluarga (SAKK)**

# Takaful Annuity Experience in Malaysia

## The Model



# Takaful Annuity Experience in Malaysia

## What Factors Contributed to its Success

- Painless to members as the money was paid directly from their EPF accounts, so no immediate financial impact
- A commission was paid to agents
  - Commission was 2% with an average premium size of USD7 ,000
  - Over 30,000 agents were involved
- Many EPF members see that the product was a good deal for them
- The press coverage (albeit negative) helped increase the public awareness
- The scheme was initially endorsed by the EPF and hence the Government but was later cancelled due to pressures from the trade unions. The concern of the Trade Union was more on the conventional version of the product.
- Investment returns from the annuity fund was exempted from tax



## Can the SATK annuity product be replicated 10 years on?

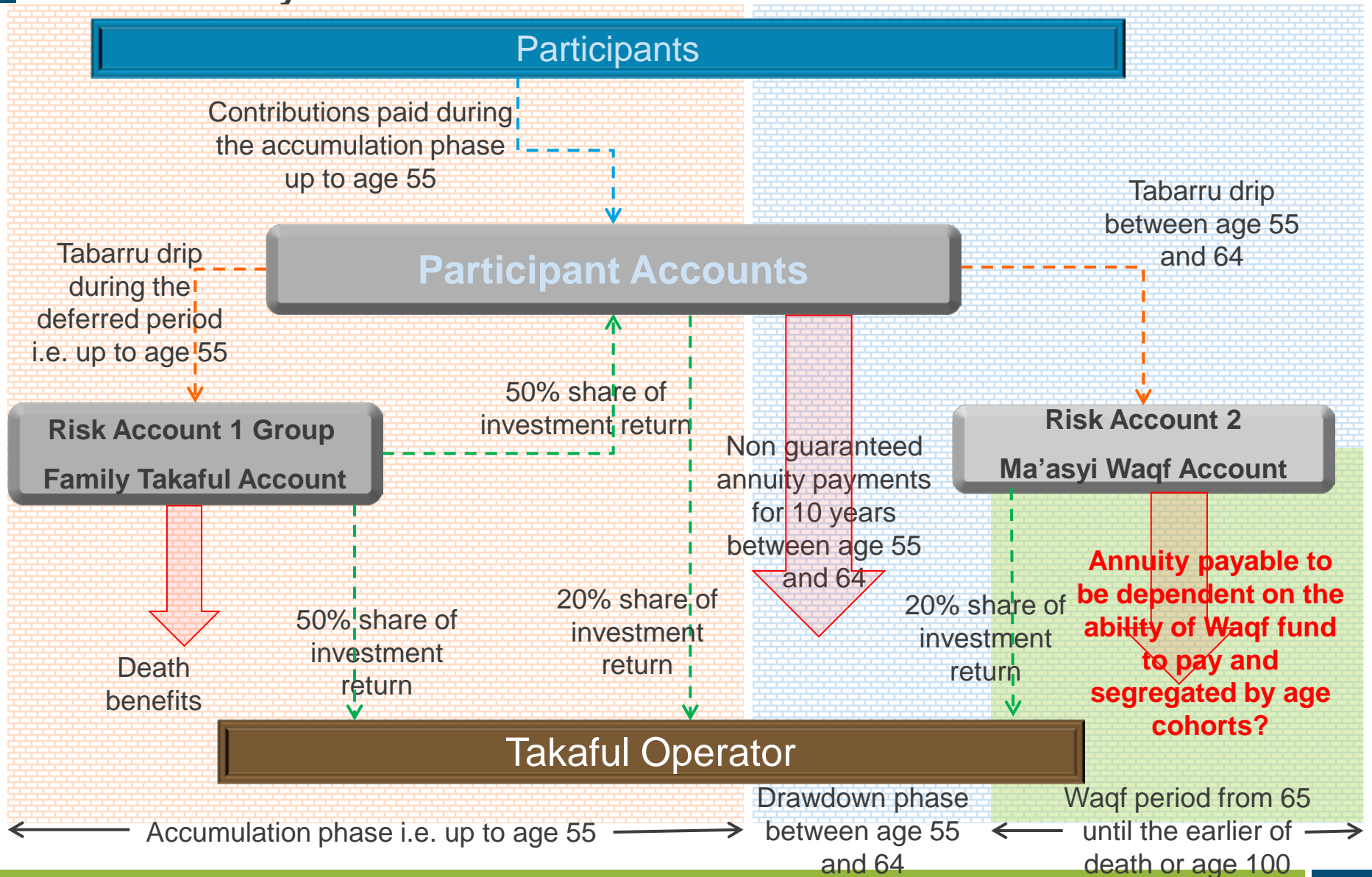
- The Sharia issue on the 3<sup>rd</sup> phase of the product needs attention. The waqf concept should work other than concerns established by some sharia scholars that a waqf should not diminish in value. During the annuity payment phase, assets will be drawn down so that it goes to zero when the last annuitant dies (in theory!).
- There is also the issue whether the annuity can be guarantee as to quantum and that it would be payable for the whole of life. This requires assets which can mirror the subsequent investment guarantee and the ability to manage longevity risk. In a Mutual set up such as a takaful this will require some form of intergenerational sharing of risk.
- The accumulation and payout phase involves monetary transactions a simple interpretation could be it is a transaction involving money for money. The suspicion of riba (interest) can arise when the annuity payments exceed the contribution (premium).

## Recent Developments in Takaful in Malaysia

- Introduction of a Takaful Operating Framework for Takaful Operators which among others places limits/conditions on the wakala fees that can be charged by the Takaful Operator.
- Introduction of Risk Based Capital for takaful operator and takaful funds. There are liability risks and asset risks and a defined Capital Adequacy Ratio
- The Sharia Supervisory Council has ruled that the tabarru' fund can pay out other than benefits on death or disability on the condition that the contributors of the takaful fund are all in agreement. This is justified on the basis of tabarru' and ta'awuni.
  - This ruling was widely viewed as paving the way for the introduction of annuities payable from a dedicated takaful annuity fund.

# Takaful Annuity

## A RBC Friendly Model





## What actually do we need the post retirement income for?

- Food, shelter and health care....



- Annuity premiums are used to invest in assets which are expected to keep with the costs of these basic necessities. There is usually a long investment phase where there are investment and inflation risks followed by a shorter draw down phase also concerned with investment and inflation risks but coupled with longevity risks.

## New Approach to Takaful Annuity

### Go straight to the needs!

- Why not instead we cut off the “middle man” (the investment houses) – the annuity contributions are used as pre paid life membership contributions towards a Care Home established under the concept of a Waqf!
- The recent episode with Southern Cross (the biggest Care giver in the UK with 750 homes and 31,000 residence nationwide) will make care homes more expensive due to the requirement for an insurance bond. An insurer providing care home facilities seems a logical next step.
- There is a going to be a burgeoning need for post retirement care with the break up of the family unit and the rapidly shrinking birth rates.



## New Approach to Takaful Annuity

Go straight to the needs!

- From the Muslim perspective the concept of Waqf can be appealing as the tabarru' that they pay towards the building of the homes may be treated as "sadaqah" and may continue to benefit them even after their death...

Abu Hurayrah rahimahullaah reported that Allaah's Messenger sallallaahu 'alayhi wa sallam said: *"When a human being dies, all of his deeds are terminated except for three types: an ongoing sadaqah, a knowledge (of Islaam) from which others benefit, and a righteous child who makes du'aa for him."* (Muslim and others).



## Go straight to the needs?

- A waqf (a Trust) is set up by the takaful company to which it will contribute an amount sufficient to purchase the necessary freehold land for the community homes – this also ensures that the waqf will not diminish in value over time
- Annuity contributions, less a wakala fee to the takaful company, will finance the construction of the Care Homes and fund the food and health care needs. This will also overcome the limitation of sharia compliant investments as investments are made directly to the services which the Homes will require.
- By providing service rather than money in return to money paid in by the annuitants this can overcome sharia's "money in exchange for money" objection.
- Care Homes can be a "renewable resource" as the occupants have a finite occupancy period!

# Opportunity for Takaful Annuity

## Where is the potential market?

	Population size	GDP per capita	Working age people	Old age dependency ratio	Risk based capital	Social security	Income tax	Annuity penetration	Market for takaful annuity?
Malaysia	27.5 m	\$14,700	65%	7.6%	Yes	Moderate	Low to moderate	None	★★★★★
Brunei	0.4 m	\$51,600	70%	5.0%	No	Moderate	Low	None	★★★
Indonesia	246 m	\$4,200	67%	9.0%	Yes	Moderate	Moderate to high	None	★★★★★
Singapore	4.8 m	\$62,100	77%	12.0%	Yes	High	Low to moderate	None	★★
Sri Lanka	21.3 m	\$5,000	67%	11.7%	No	Moderate	Moderate to high	None	★★★★★
Saudi Arabia	26.1 m	\$24,200	68%	4.4%	No	High	Low	None	★
Qatar	0.9 m	\$179,000	77%	2.0%	No	High	Low	None	★
Oman	3.0 m	\$25,600	66%	4.7%	No	High	Low	None	★
Egypt	82.1 m	\$6,200	63%	7.2%	No	Medium to high	Low to Moderate	None	★★★

## Conclusion

- Malaysia has led the way in preparing the grounds for takaful annuity. The regulations are in place as are most of the asset classes required to support annuities.
- Annuities are more expensive the closer the vesting period. There is a need to start saving early.
- The Care home option should be given consideration where there are restrictions as to Sharia acceptance to the takaful contract applicable and where there is a lack of appropriate Sharia compliant assets to support annuity.
- Islam does not restrict its adherents from following a path without providing for an alternative (and better) path/solution if it is for the good of the Ummah.



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