The Future of
TAKAFUL IN PAKISTAN
A DIAGNOSTIC STUDY

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
SECP

Why This Report?

This report aims to establish a foundation for meaningful engagement and foster informed discussions among industry participants, regulators, policymakers, Shariah scholars, industry experts, consumers, and other key stakeholders. The focus is on identifying the challenges and opportunities within Pakistan's Takaful sector. The insights provided are intended to drive concrete actions to strengthen the Shariah-compliant insurance ecosystem and conversion towards interest free economy.

The report evaluates the current state of the Takaful industry, examines regulatory developments, and offers recommendations. In light of the evolving Islamic finance landscape, along with the Federal Shariah Court's ruling and constitutional amendments aimed at establishing a Riba-free economy by 2027, this report emphasizes the urgent need to build public trust, uphold Shariah governance, and develop enabling frameworks for a sustainable Takaful ecosystem.

Where Do We Go From Here?

The objective of this report is to analyse the current state of the Takaful sector in Pakistan, identify key barriers to its growth, and address operational, regulatory, and awareness-related challenges. Based on these findings, the report presents a strategic roadmap to transition towards a fully Shariah-compliant Takaful ecosystem, outlining the essential steps required for a seamless transformation. The study provides a high-level overview of the following:

- Takaful in Pakistan – A snapshot
- Potential Growth Horizon
- Comparative Study of International Jurisdictions
- Way Forward and Recommendations
- Key Challenges and Growth Deterrents
- Plan of Action

Takaful Sector Snapshot 2023

Takaful Sector Composition

33 Takaful Operators

- 4 Dedicated Family Takaful Operators
- 7 Family Window Takaful Operators
- 2 Dedicated General Takaful Operators
- 20 General Window Takaful Operators

FAMILY TAKAFUL INDUSTRY PREMIUM:
RS. 48 billion

FAMILY TAKAFUL PREMIUM AS PERCENTAGE OF TOTAL LIFE INSURANCE INDUSTRY PREMIUM
12%

GENERAL TAKAFUL INDUSTRY PREMIUM:
RS. 25 billion

GENERAL TAKAFUL PREMIUM AS PERCENTAGE OF TOTAL NON-LIFE INSURANCE INDUSTRY PREMIUM
11%

Family Takaful Segment

97.7% of the contribution was written by private sector

General takaful Segment

100% of the takaful contribution was written by private sector

Family Takaful Maket Share

Family Takaful Share in total first year premium in 2023 was 21% (Rs. 8.82 Billion)	Family Takaful Share in first year premium written by private sector is 45%	Share of Takaful Contribution in Total Regular and Single Premium is 16% (Rs. 41.45 Billion)
Share of Takaful Contribution in Total Regular and Single Premium written by private sector is 37%	Share of Takaful Contribution in Group premium is 4%	Share of Takaful Contribution in Group premium, excluding the social insurance scheme is 34%

General Takaful Market Share

34%	26%	9%	9%	5%
Motor	Health	Marine	Misc.	Fire

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Message from **Commissioner**

I am pleased to share this study on The Future of Takaful in Pakistan. This report represents an essential assessment of the current state of the Takaful sector and comes at a moment of pivotal importance—both for the Islamic finance landscape and the broader socio-economic and constitutional imperatives of our country. It provides a detailed overview of the sector's present status, identifies the key challenges impeding its growth, and outlines the vast potential that remains untapped. Most importantly, the report outlines a forward-looking roadmap with concrete action points to support the development of a robust, inclusive, and Shariah-compliant insurance ecosystem in Pakistan.

The Takaful sector in Pakistan stands at a critical juncture, marked by both significant challenges and immense opportunities. Despite being rooted in Shariah-compliant principles and catering to a more than 96% Muslim population in Pakistan, one can reasonably argue that Takaful is lagging behind in achieving its full potential, as it has contributed a mere 11% to 13% to the overall insurance market over the past five years. This stagnation of takaful contribution to the overall insurance pie pinpoints a wide gap between market potential and actual performance, calling for immediate corrective action to unlock the industry's growth.

Recognizing this gap and the need for action, the Securities and Exchange Commission of Pakistan in its 5-year strategic plan, as an operational outcome, has targeted the share of takaful contribution greater than 30% of the total industry premium by 2028. The operational outcome of 30% share of takaful contributions set under the strategic plan, aligns with the judgment of the Federal Shariah Court of April 2022, requiring conversion of the economy of Pakistan into, equitable, asset based, risk sharing and interest-free economy by December 2027.

The very recent 26th constitutional amendment, requiring the complete elimination of "Riba" before the first day of January 2028, is a further strong call for action for our industry at large to step up and offer takaful solutions, in alignment with national, economic and constitutional goals.

This report provides a comprehensive analysis of the current state of Takaful in Pakistan, offering critical insights and actionable strategies. It evaluates industry performance data, explores lessons from international jurisdictions such as Malaysia, Sudan, the Kingdom of Saudi Arabia and Indonesia, and reviews the legislative history of Takaful in their respective jurisdictions. Additionally, the report examines the structural and operational impediments that have hindered the sector's development, including low consumer awareness, regulatory and Shariah challenges, inadequate capacity, the industry's status quo approach, and the lack of innovation in product offerings.

Looking ahead, the report highlights the promis-ing growth prospects for Takaful and the key policy recommendations to be considered by the policy makers, the regulator, the industry at large and other key stakeholders. The focus of the growth areas and the policy prescriptions is to enable the Takaful industry to fulfil its potential and meet the constitutional and market-driven demands for a robust Shariah-compliant insurance ecosystem.

In conclusion, I would like to express my appreciation for the unwavering support of all members of the Insurance Division in their commitment to advancing the insurance sector. Special acknowledgment goes to the authors of this report, Mr. Jibran Paracha, Joint Director and Ms. Sahar Kanwal, Assistant Director for their dedicated efforts in bringing this report to conclusion!

Mujtaba Ahmed Lodhi
Commissioner – Insurance

1.Takaful in Pakistan – A Snapshot

1.1. Evolution of The Takaful Regulatory Framework

Pakistan boasts the second largest[1] Muslim population in the world with more than 231 million[2], constituting 96.28%[3] of its total population practicing Islam as its religion. Despite Pakistan being an Islamic republic, the concept of takaful was introduced relatively at a later stage i.e. in 2000, given that the first Islamic Insurance company was established in Sudan in the year 1979.

The concept of Takaful was introduced into the Pakistan's legal framework through the Insurance Ordinance, 2000 (the "Ordinance"). However, the Ordinance primarily served as a foundational step, offering only a basic definition of Takaful and provision that allowed insurers to conduct Takaful business in compliance with applicable laws. The Ordinance did not delve into the specificities necessary for the practical implementation of Takaful operations in Pakistan.

The first substantial development on the regulatory framework front, came with the promulgation of the Takaful Rules, 2005 (the "Repealed Rules") notified by the Ministry of Commerce in September 2005. The Repealed Rules laid the foundation of the different concepts underpinning Takaful by coining terms related to takaful business, fund creation and segregation, requirements as to extension of qard-e-hasan, sharing of surplus, investment guidelines, requirement of Shariah Board of company and Central Shariah Board at the Commission level etc.

With the application of the Repealed Rules, issues were raised by market participants, practitioners and Shariah scholars, which lead to the initiation of the review exercise of the Repealed Rules and eventually culminated with the issuance of the Takaful Rules, 2012 (the "Rules") by the SECP.

Importantly, by the year 2007, five takaful operators were registered with the SECP, two operating in the family takaful sphere, whereas, three providing general takaful services. However, post 2007; there was a standstill, with no fresh market entrants in the takaful markets. As a reform measure, the Rules had opened up the takaful market by allowing window takaful operations i.e. conventional insurance companies were permitted to undertake takaful business after seeking authorization from the SECP.

The Rules have been infield for the previous more than twelve (12) years now, however, following are the key reform/salient features of the Rules:

[1] https://www.statista.com/statistics/374661/countries-with-the-largest-muslim-population/

[2] https://www.pbs.gov.pk/sites/default/files/population/2023/tables/national/table_9.pdf

[3] https://www.pbs.gov.pk/sites/default/files/tables/population/POPULATION%20BY%20RELIGION.pdf

Market Development

Introduction of authorisation regime for Window Takaful Operations.

Enabling conversion of transforming a non-life insurer into a General Takaful Operator

Flexibility in adoption of different models of Takaful i.e. Wakala and Modaraba

Shariah Compliance

Establishment of a Shariah Advisory Board at the SECP level.

Mandatory appointment of a Shariah Advisor

Introduction of new roles focusing at Shariah compliance

- Shariah Compliance Officer
- External Shariah Compliance Auditor

Financial Soundness

Maintenance of solvency at the Participant Takaful Fund (PTF) level

Compulsory segregation of funds, with elaboration the different funds created

Requirement of Qard-e-Hasna in case of an accounting deficit in the PTF

Requirement of submission of report to the Commission, in case PTF was in deficit for three consecutive years

Authorization Process

Defined process for authorizing Takaful and Window Takaful operators

Reasons for revoking authorization

With no substantial revision in the Rules for the previous 12 years, one can reasonably comment that the regulatory framework on takaful in Pakistan demands a holistic review.

1.2. Applicable Takaful Model in Pakistan

Globally, Takaful is practised through different models such as the Wakalah model, the Mudarabah model, the Hybrid Model (combining Mudarabah and Wakalah), Wakalah Waqf Model and the Cooperative Model. In Pakistan, whilst the regulatory framework i.e. the Rules, does not dictate any specific model and permits the undertaking of Takaful business under Wakalah, Mudarabah or both, however, the prevalent model practised in Pakistan is the Wakalah-Waqf Model.

Central to the Wakalah-Waqf model is the establishment of a Waqf fund (referred to as "Participant Takaful Fund" or "PTF"), a separate fund that serves as an endowment, with the contributions from participants, also referred to as Tabarru (voluntary donations), being pooled therein. Whilst the payment of Tabarru into the Waqf and the corresponding payment of benefits (claims) by the PTF are independent elements of an arrangement, the contributions are generally explicitly designated for risk-sharing purposes, such as covering claims and related expenses.

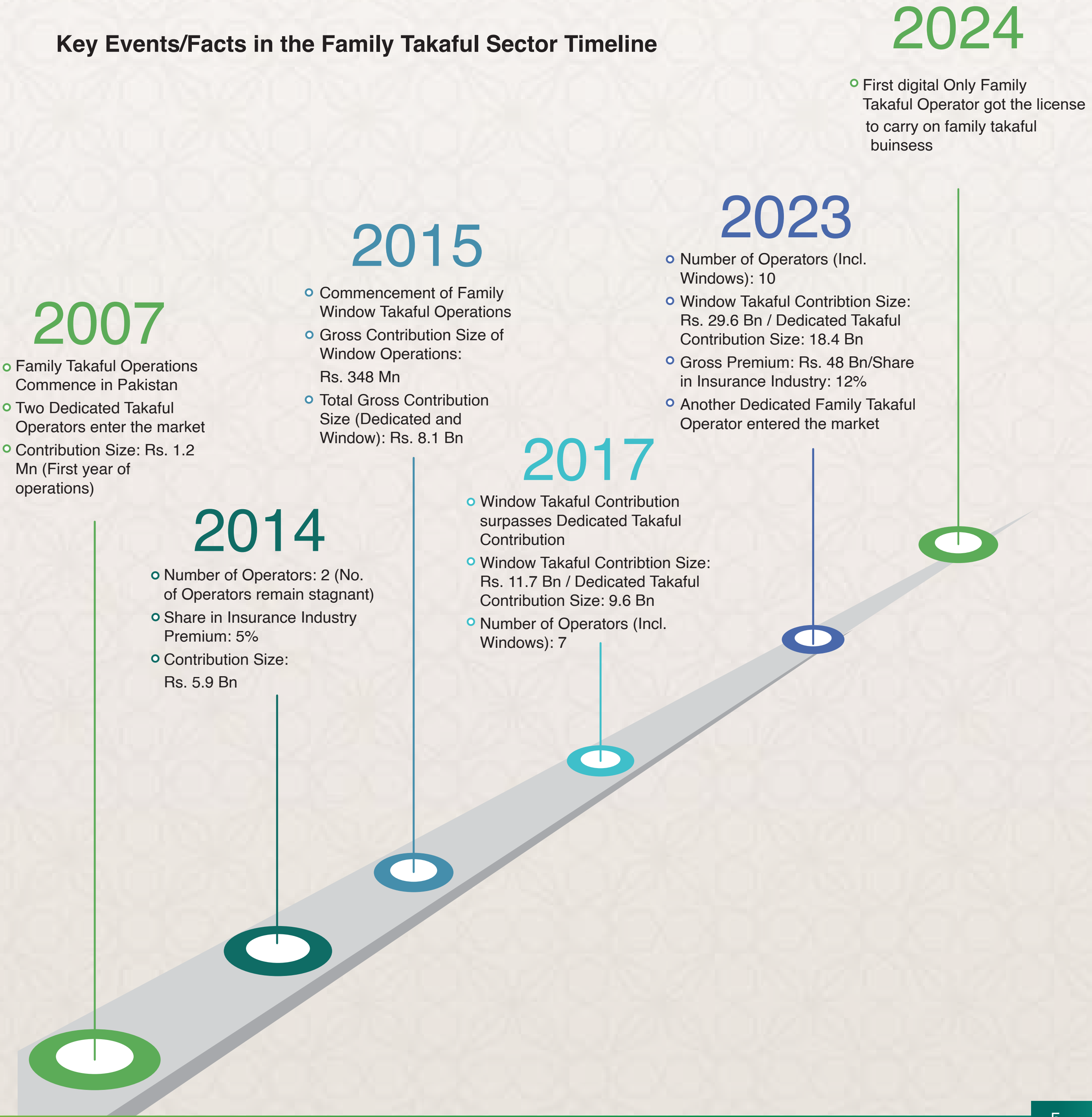
The relationship between participants and the Takaful operator is mediated through the PTF, where the Takaful operator acts as a Wakeel on behalf of the fund. In this capacity, the operator manages all aspects of the PTF, including underwriting, risk-sharing arrangements, claims processing, and compliance with Shariah guidelines etc. Additionally, the operator also oversees the investment of surplus funds of the PTF, generally governed through a Mudarabah arrangement, wherein the Takaful operator, acts as the Mudarib (investment manager) with the PTF being the Rab-ul-Maal (owner of the funds). Both the PTF and the Operator share the profits on investments net of expenses according to a pre-determined ratio. The surplus of the PTF is totally attributable to the takaful participants and the Operator distributes the same to the participants in accordance with the predetermined criteria.

In the case of family Takaful business, the investment component related to the participants are pooled within the Participant Investment Fund or the “PIF”. The investments of the PIF are managed in accordance with Wakalah-ul-Istismar (investment agency) and the operator is entitled to an agreed upon fee computed generally as a percentage of the total assets. The operator charges a Wakalah fee, for managing the Waqf fund and operational activities. This fee covers administrative and operational costs, ensuring the sustainability of the Takaful operator's services.

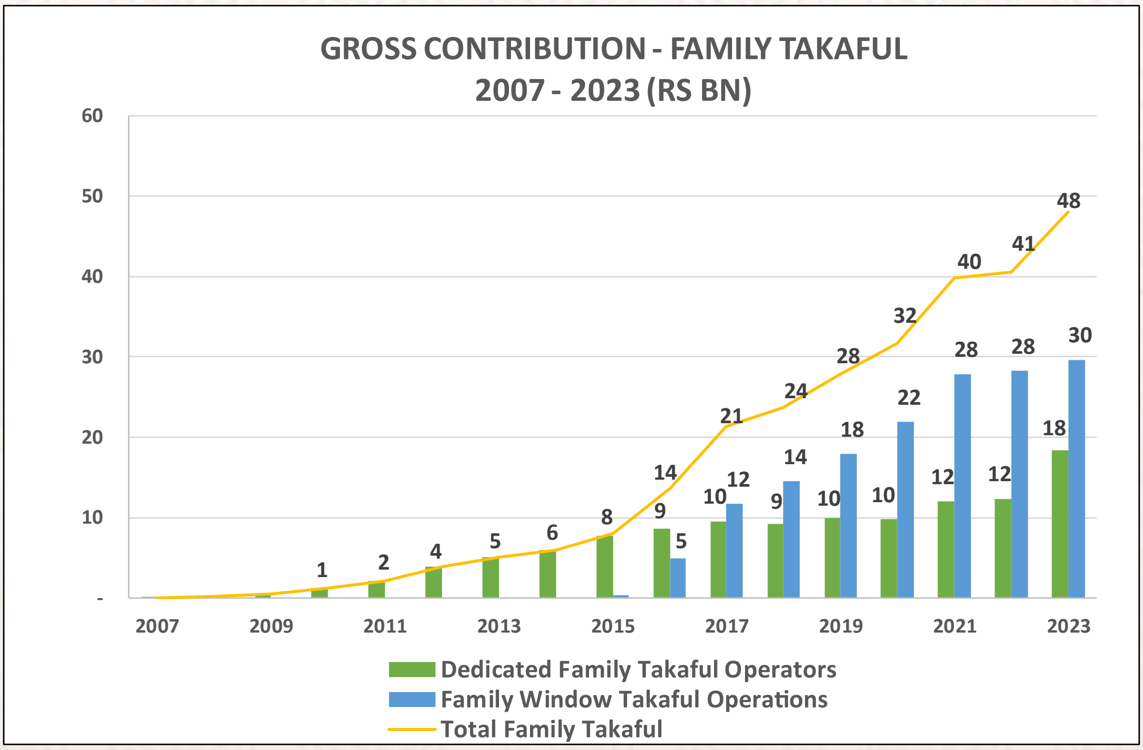
The Wakalah-Waqf Model ensures a clear separation between the risk pool and the investment pool. This model has gained widespread acceptance within the industry, making it a cornerstone of Takaful operations in Pakistan.

1.3. Key Industry Events and Statistics

Key Events/Facts in the Family Takaful Sector Timeline



Timeline of the Family Takaful Sector Contribution Growth



Key Events/Facts in the General Takaful Sector Timeline

2006

- General Takaful Operations Commence in Pakistan
- Three Dedicated Takaful Operators entered the market
- Contribution Size: Rs. 129 Mn (First year of operations)

2014

- Number of Dedicated Operators: 3 (No. of Operators remained the same)
- Share in Insurance Industry Premium: 3%
- Contribution Size: Rs. 2.3 Bn
- Commencement of General Window Takaful Operations. Window authorizations: 3
- Gross Contribution Size of Window Operations: Rs.190 Mn

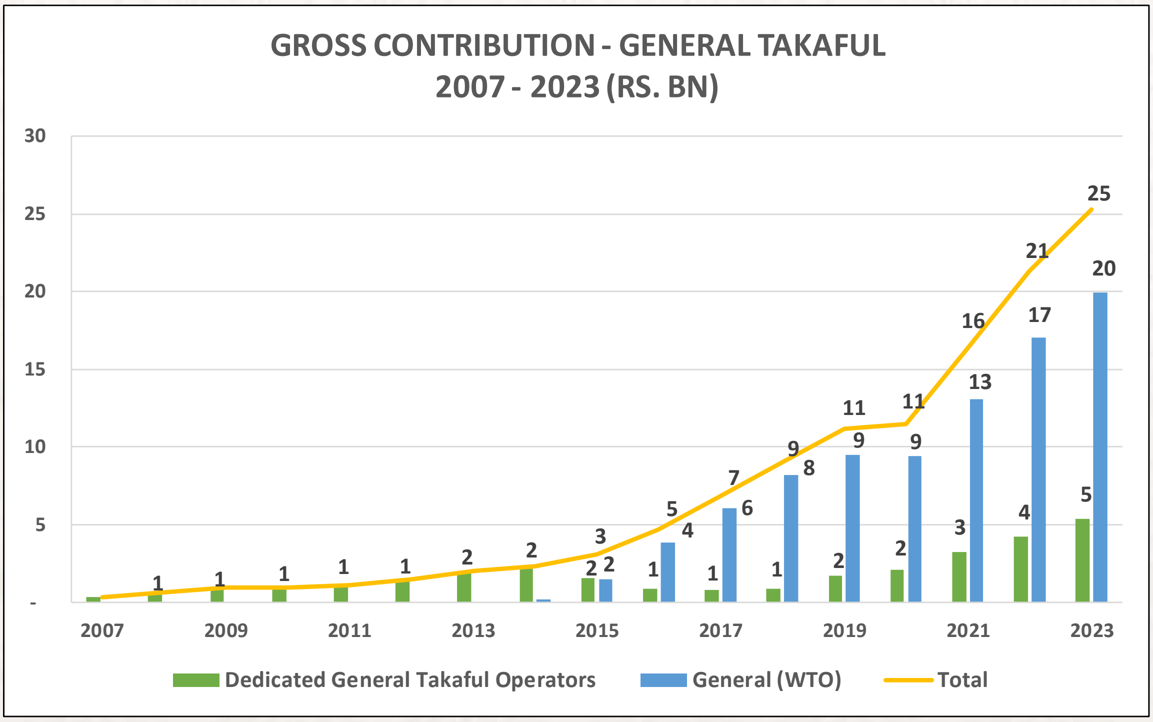
2016

- Window Takaful Contribution surpasses Dedicated Takaful Contribution
- Window Takaful Contribtion Size: Rs. 3.8 Bn / Dedicated Takaful Contribution Size: Rs. 0.87 Bn
- Number of Window Operators: 14

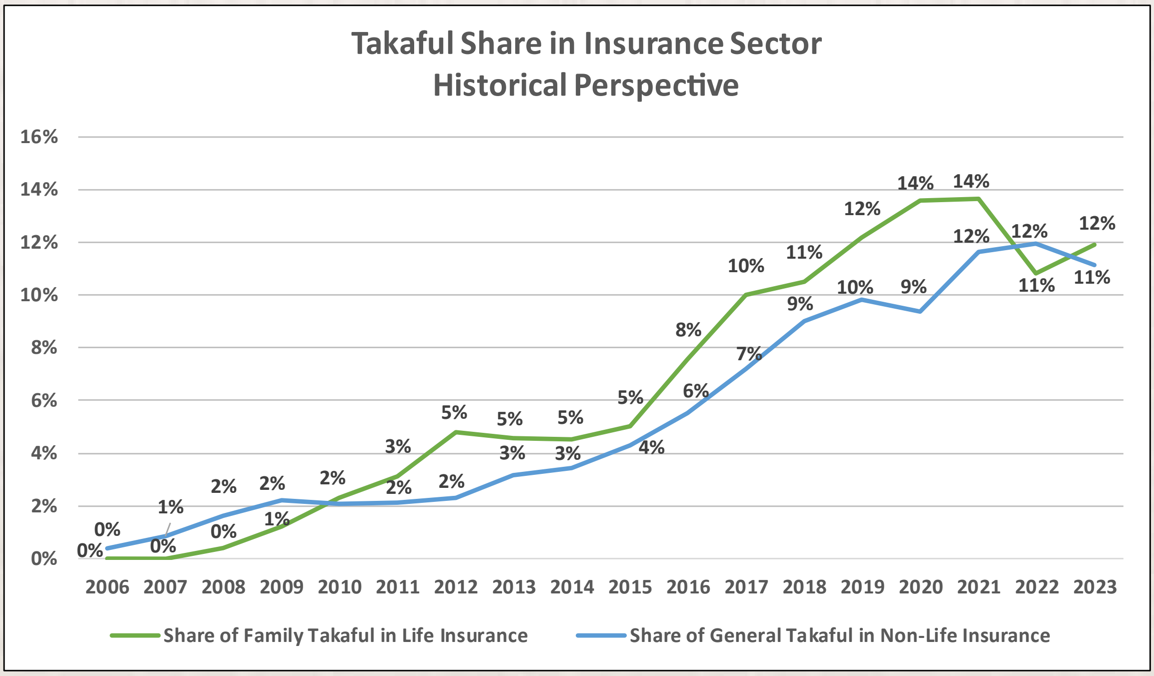
2023

- Number of Operators (Incl. Windows): 22
- Window Takaful Contribtion Size: Rs. 20 Bn / Dedicated Takaful Contribution Size: Rs. 5.3 Bn
- Gross Contribution: Rs. 25 Bn/Share in Insurance Industry: 11%

Timeline of the General Takaful Sector Contribution Growth



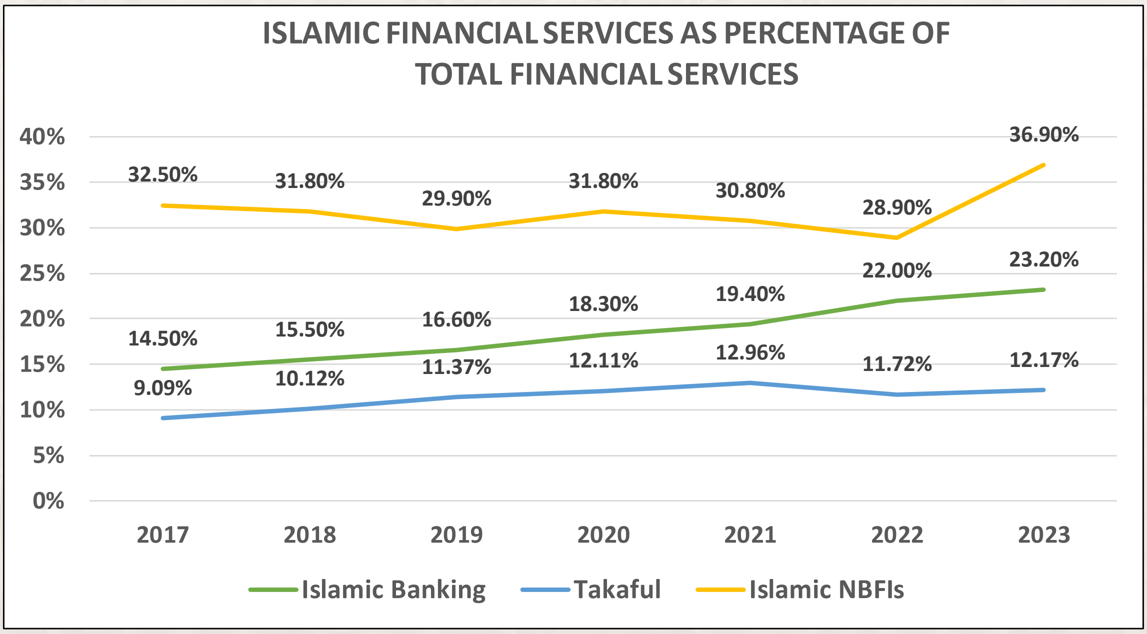
Share of Takaful Sector in the Insurance Industry (2006 – 2023)



Takaful Sector Composition (2023)

Note: * Includes one digital only family takaful operator

Comparison of share of Islamic Financial Services in the overall Financial Services Sector



Sources: SBP Islamic Banking Bulletins/NBFC Sector Summary Report/Insurance Industry Statistics

Data Timeline: Islamic Banking & Takaful Data as of Dec 20XX / Islamic NBFI Data as of Jun 20XX

Note: Data of NICL not included due to unavailability of Financial Statements

An evaluation of the share of the Takaful sector in the overall insurance sector, comparing it with the relative share of Islamic banking and Islamic Non-Banking Financial Institutions (NBFIs) in respect to their respective sectors, reveals Takaful hasn't been able to penetrate that much, as compared to their Islamic financial service counterparts.

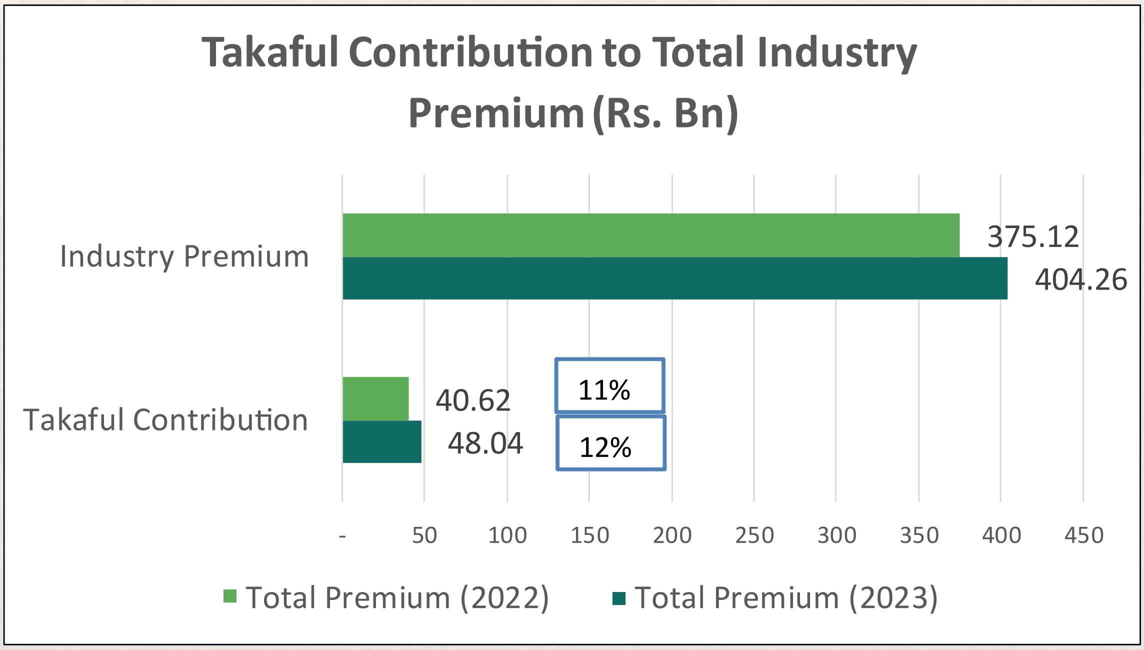
A question then arises as to why Takaful's share, remaining stagnant at around 12%-13% for the previous five years, has not been able to create inroads into the insurance market. This demands insights at a more granular level and requires more detailed analysis to determine the root cause or the issues underpinning the low takaful penetration in Pakistan. In the following paragraphs, we dissect both the family takaful business and the general takaful business at a more granular level.

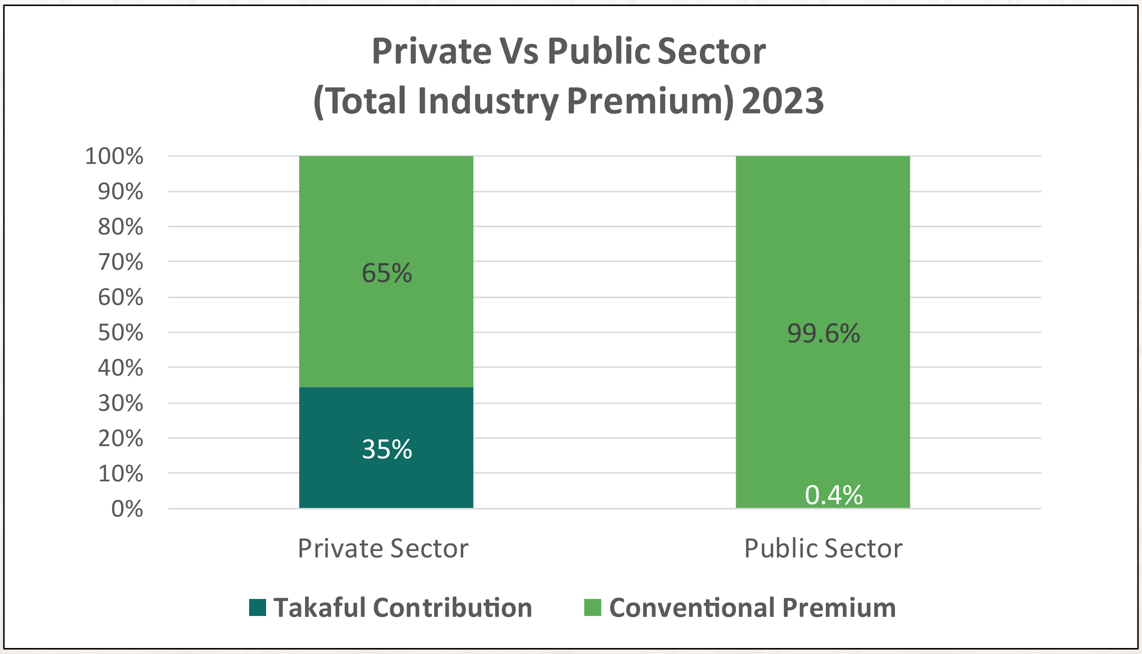
Detailed Analysis of the Family Takaful Market:

The Family Takaful market comprises of three dedicated takaful players and seven players having window takaful operations. Within the seven window takaful operators there is one large public sector life insurance company namely the State Life Insurance Corporation of Pakistan (SLIC). Additionally, in the life insurance sector, there is another public sector insurer namely the Postal Life Insurance Company Limited (PLICL), which does not undertake takaful business, per se.

SLIC is the largest life insurer in Pakistan having a share of 66.5% in 2023 (2022: 65%) in the total life insurance industry in Pakistan. It was, however, noted that SLIC has a very miniscule Takaful business when compared with its overall business, hence creating this compulsion to look at the performance of private sector insurers separately in the Takaful sphere from that of the public sector insurers.

Analysis of Family Takaful Share by Total Premium/Contribution



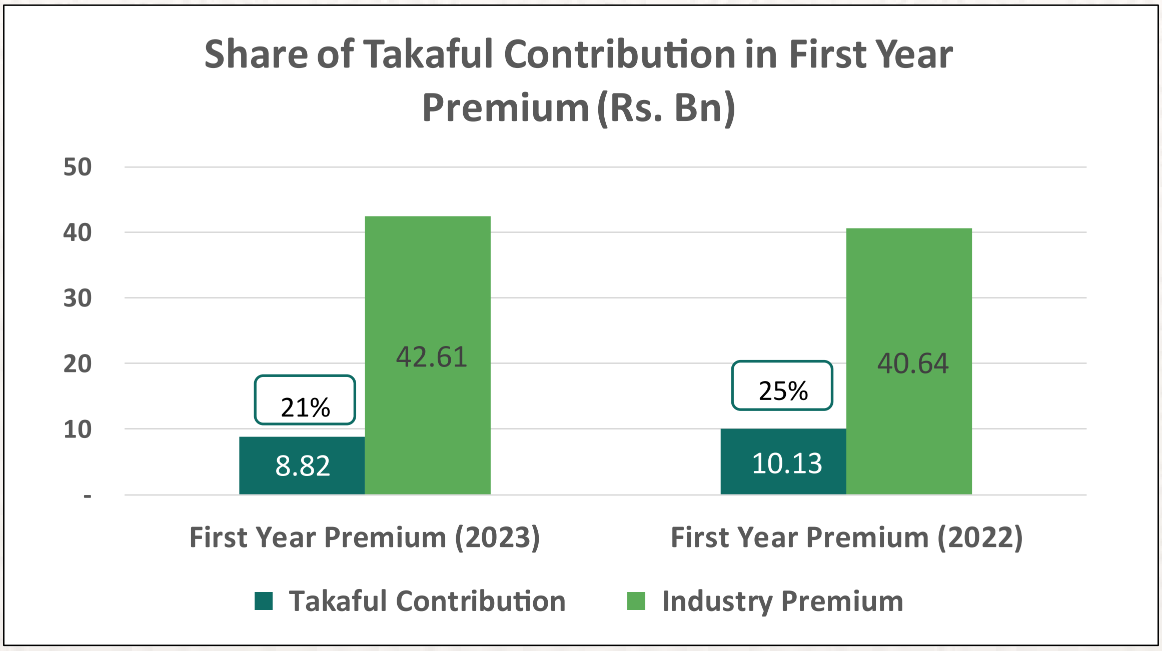


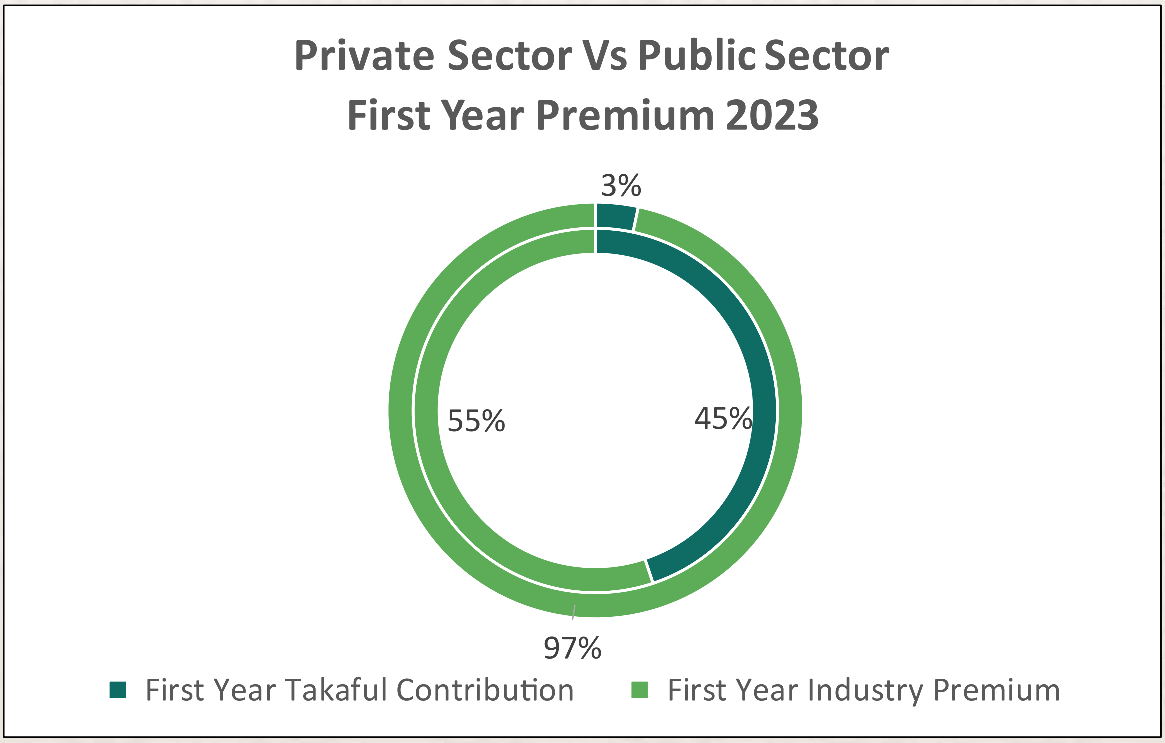
Note: 2023 data does not include data of PLICL due to non-availability.

In 2022, the Takaful sector contribution was Rs. 40.62 billion, representing 11% of the total industry premium, whereas, in 2023, this contribution increased to Rs. 48.04 billion, accounting for 12% of the total industry premium. For the given years, the total insurance industry premium had increased from Rs. 375.12 billion in 2022 to Rs. 404.26 billion in 2023.

As of 2023, it was noted that a significant chunk i.e. 35% of the total private sector insurance premium had come from Takaful business, the share of takaful business in public sector insurers was very meagre and negligible i.e. 0.4% of the total premium. One attributable factor to this low takaful penetration in public sector insurers is the very high business volume of the largest life insurer in Pakistan. However, even if a comparison is drawn based on the total takaful business size only, the takaful contribution of public sector insurers amounts to only 2.34% of the total family takaful business in 2023.

Analysis of Family Takaful Share by Fresh Business or First Year Premium/Contribution

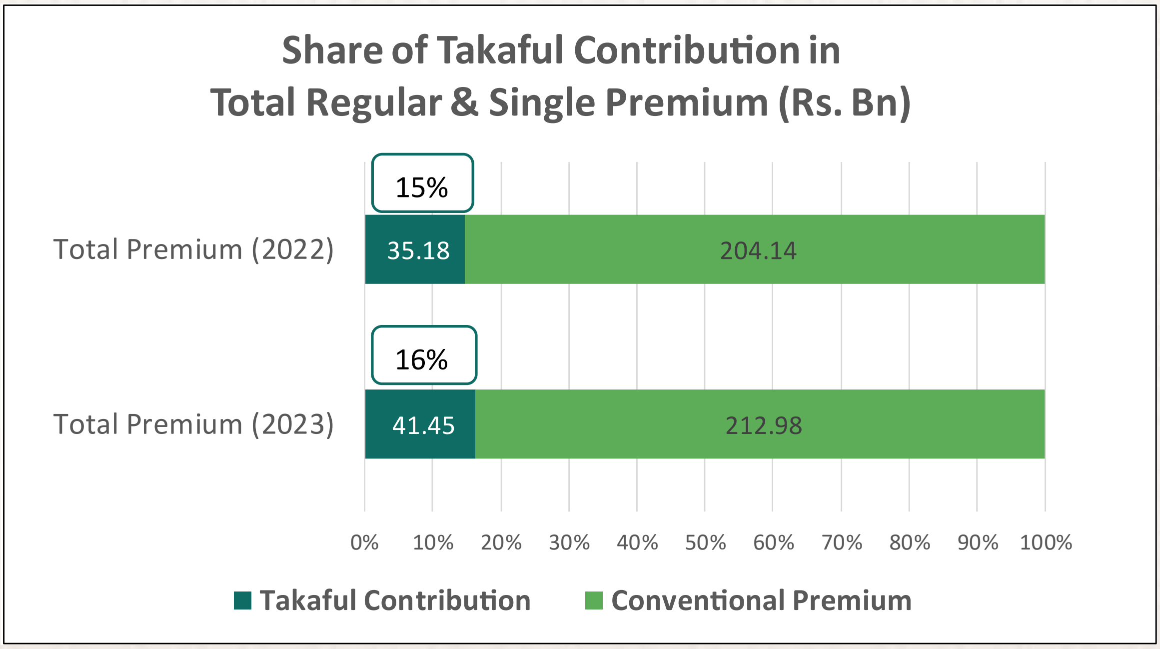


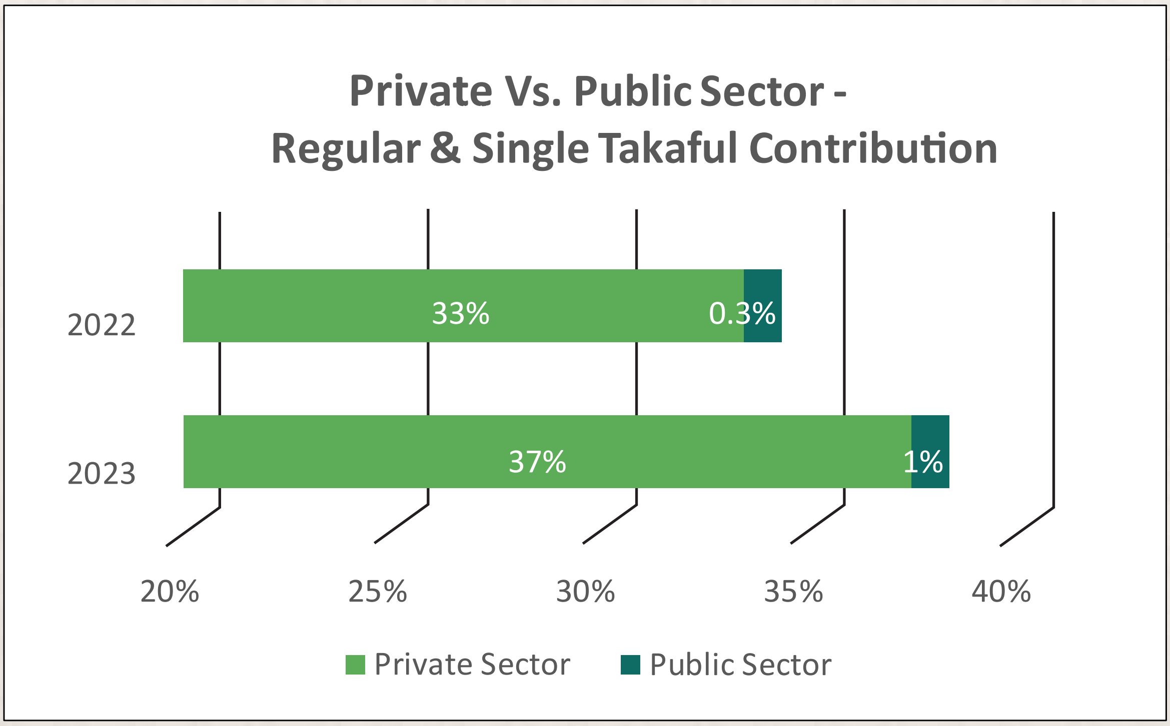


A closer examination of the new business or the first-year premium/contribution in the life insurance sector, highlights Takaful's significant contribution. In 2023, Takaful accounted for 21% (Rs 8.82 billion) of the total Rs 42.61 billion industry gross premium written in the first year. While this represents a slight decline compared to the 25% share recorded in the previous year, it appears that Takaful has started to have a significant share in the new business in the country.

More interesting and overwhelming to note is that in 2023, 45% of the total fresh business of private sector life insurers was Takaful, which is very encouraging to say the least. This also highlights the increased focus, on the takaful front by the private sector insurers. Conversely, the public sector's contribution to the first-year premium through Takaful was a mere 3%, indicating very minimal takaful penetration in public sector's new business strategy.

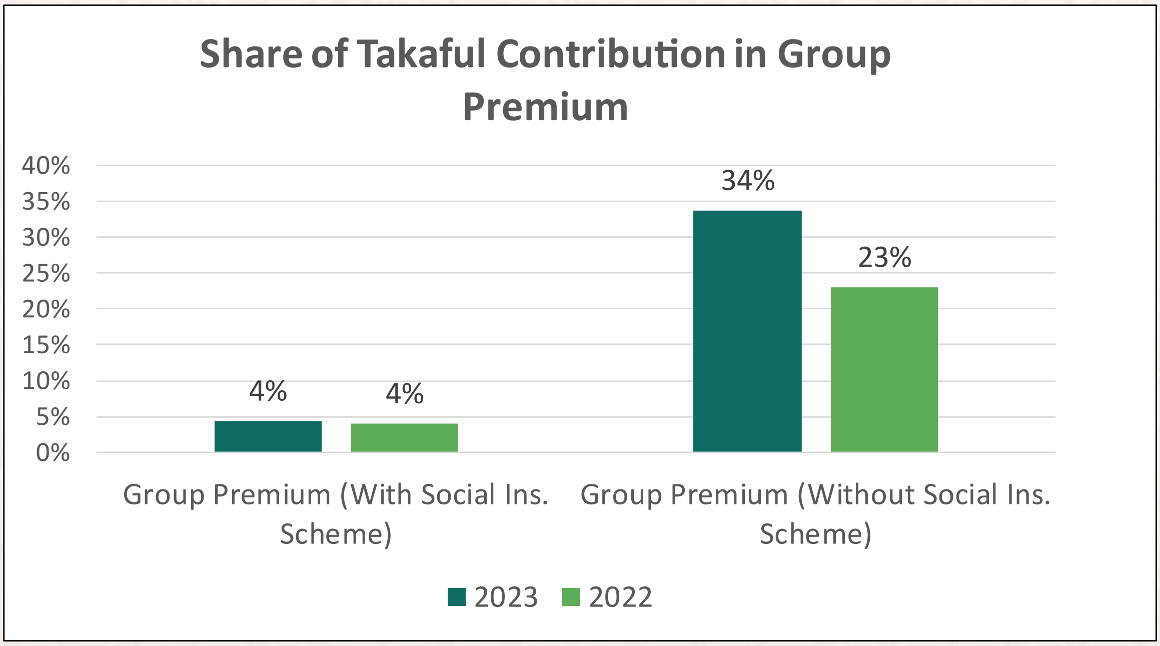
Analysis of Family Takaful Share by Total Regular & Single Premium/Contribution





In terms of the total regular premium i.e. first year premium and subsequent renewals, Takaful contributed 16% of the total pie in 2023 (15% in 2022). Notably, when breaking down the total regular and single premium in the Takaful business, only 1% was contributed by the public sector insurers, whereas, 37% was contributed by private sector insurers.

Analysis of Family Takaful Share in Group Premium/Contribution:



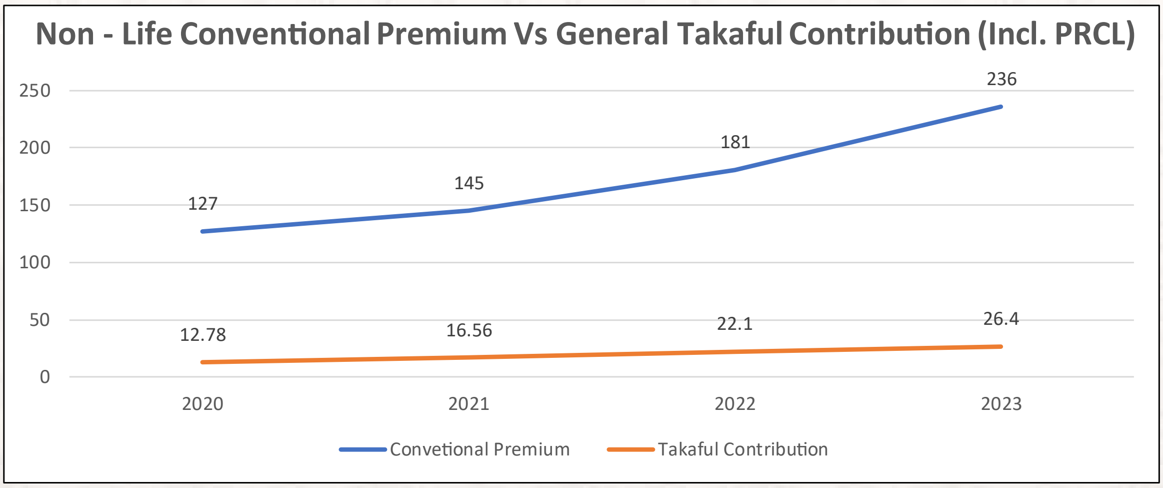
In respect of the group premium in the life sector i.e. group life and group health, the share of takaful policies overall remained stagnant at 4% in the last two years i.e. 2023 and 2022. However, it merits appreciation that the total business volume on the group side includes the social health insurance scheme in Pakistan, which for the year 2023 amounted to approx. Rs. 123 billion, which is currently written on conventional basis. If the numbers related to takaful are considered after exclusion of the social insurance scheme, the share of takaful in 2023 was 34% of the total group insurance market (2022: 23%).

The detailed analysis above highlights the strides that have been made by the private sector insurers in advancing Takaful's adoption and development. Whilst the public sector engagement in the takaful sphere is limited and is yet to grow to create a much bigger impact, it is necessary that public sector life insurers also lay focus on advancing the growth of Takaful.

Detailed Analysis of the General Takaful Market

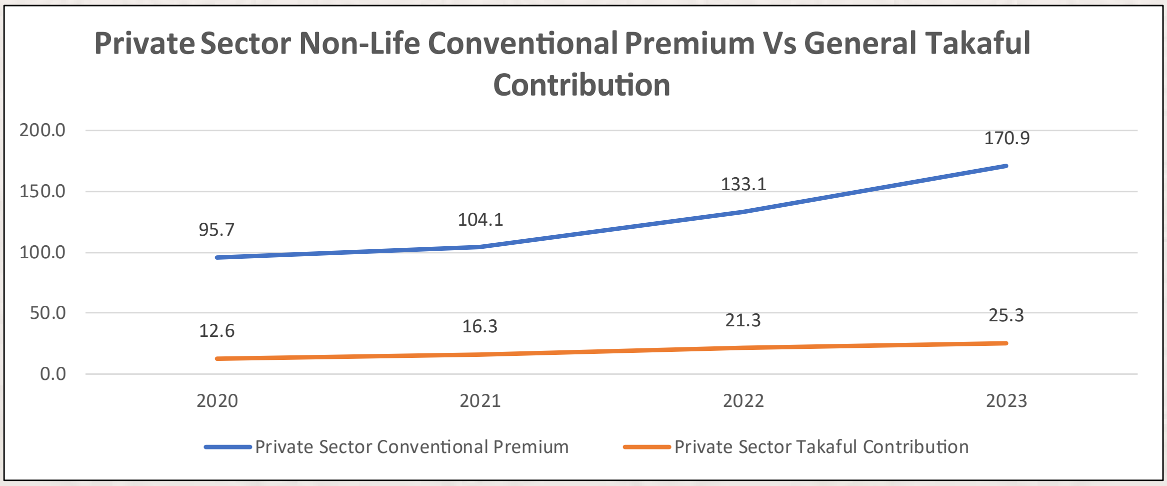
The general Takaful market comprises of two dedicated general takaful players and twenty players having window operations. M/s National Insurance Company Limited (NICL), a public sector non-life insurer, having the sole right to insure public property risks in Pakistan, does not have window takaful operations. Not having window operations by NICL infers that the risks of the federal and the provincial governments cannot be underwritten on Takaful basis.

Further, the sole reinsurer in Pakistan i.e. M/s Pakistan Reinsurance Company Limited (PRCL), offering reinsurance solutions, with legally permitted first right of refusal, does have re-takaful window and underwrites risks on re-takaful basis.



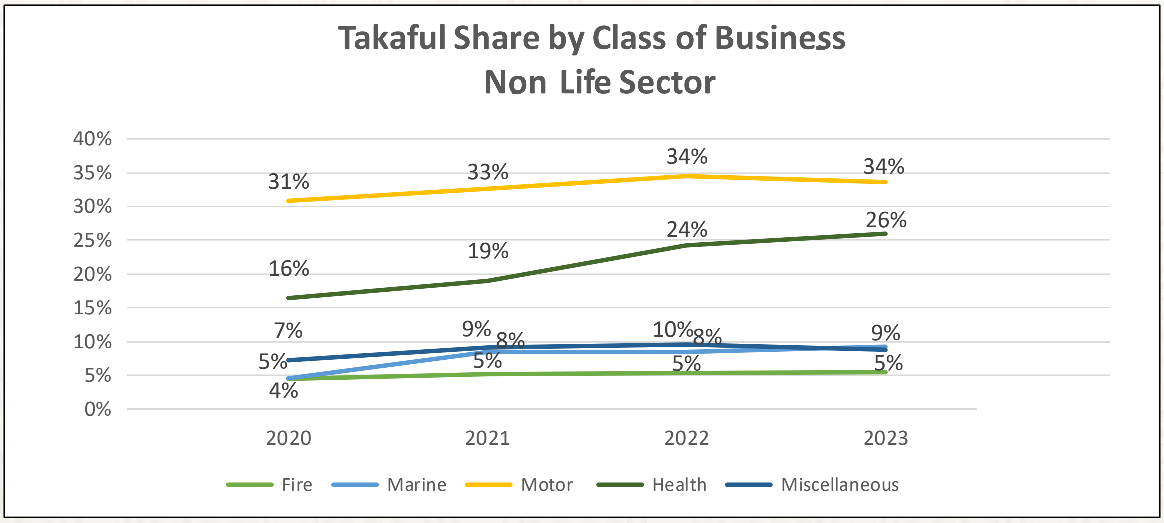
Although general Takaful holds an 11% market share within the non-life insurance industry, its growth trajectory has remained relatively modest over the years. In 2020, the contribution written of Takaful and Retakaful stood at Rs. 12.78 billion, of which Rs. 12.64 billion was contributed by general Takaful operators, while only Rs. 0.78 billion came from PRCL's window Retakaful operations. By 2023, the total contribution had increased to Rs. 26.4 billion, comprising Rs. 25.28 billion from general Takaful operators and Rs. 1.4 billion from PRCL's window retakaful operations—effectively doubling over a span of four years.

Within PRCL's total premium portfolio, only around 4% of the business was generated through its Window Retakaful operations. However, in contrast, when isolating the private sector's premium contribution, it is observed that the share of Takaful business stands significantly higher at 13%.



While the growth in absolute terms is noteworthy, the market share of general Takaful has not expanded significantly relative to the overall insurance industry. It remained at 11% in 2023, compared to 12% in 2022. Within the private sector, general Takaful accounted for 13% of the market share in 2023—a level that, while notable, is not yet substantial enough to create a material impact on the broader insurance landscape.

In order to understand the reason underpinning the stagnancy of the general takaful market as a percentage of the overall non-life insurance sector, a detailed analysis was undertaken in respect of takaful business under different classes of business.



Note: Takaful share computed on the basis of insurance/takaful business underwritten in Pakistan.
Data of NICL not included in due to non-availability.

Amongst the different classes of business, motor takaful leads the chart by contributing 34% in 2023 (2022: 34%), whereas, the most growing segment can be attributed to the health takaful, increasing from 16% in 2020 to 26% in 2023. The least takaful penetration is in the fire class of insurance business contributing a mere 5% in 2023 whereas, marine and miscellaneous classes of insurance business contributed 9% each in 2023.

Notably, motor and health insurance do have an individual or personal lines element attached to it, whereas, fire, marine and miscellaneous are largely risks related to the corporate world. One can therefore assume that personal lines of business have shown more orientation towards takaful solutions as compared to the large corporate risks.

1.4. The Judgment of the Federal Shariah Court and the 26th Constitutional Amendment

The Federal Shariah Court's judgment dated April 28, 2022, declaring riba (interest) in all its forms as prohibited, marked a pivotal moment in the transformation of Pakistan's overall financial system. This ruling not only mandates the complete elimination of riba but also requires the conversion of the economy of Pakistan into equitable, asset based, risk sharing and interest-free economy by December 2027.

> *"Hence, after considering all these arguments and noting all the practical aspects we are of the view that five years period is reasonably enough time for the implementation of our decision completely i.e convert economy of Pakistan into, equitable, asset based, risk sharing and Interest-Free Economy. Therefore we would specify the 31st day of December, 2027 on which the decision shall take effect by way of complete elimination of Riba from Pakistan."*

This judgment not only paves the way for elimination of riba from the country, it in essence sets the stage for the expansion of Islamic financial products, including Takaful, as alternatives to interest-based or conventional financial services.

The very recent 26th constitutional amendment, requiring the complete elimination of "Riba" before the first day of January 2028, is a further strong call for action for our industry at large to step up and offer takaful solutions, in alignment with national, economic and constitutional goals.

> *"38. The State shall-*
> *(f) eliminate riba completely before the first day of January, two thousand twenty-eight"*

As the riba-free financial system takes shape, primarily through the conversion of conventional banking into Islamic banking and conversion of government debt instruments into Shariah-compliant financing, the demand for Islamic financial products, including Takaful, is expected to grow significantly.

The SECP has also published a comprehensive five-year strategic plan for the insurance industry, titled "Journey to an Insured Pakistan." This plan outlines both operational and strategic outcomes that the SECP aims to accomplish by 2028. One of the critical objectives is to boost Takaful's share to over 30% of the total market and enhance public awareness about Takaful. The State Bank of Pakistan under the SBP Vision 2028, also envisions transforming the conventional banking system into a Shariah-compliant banking system and sets it as its "Strategic Goal 4" which then covers multiple targets under it.

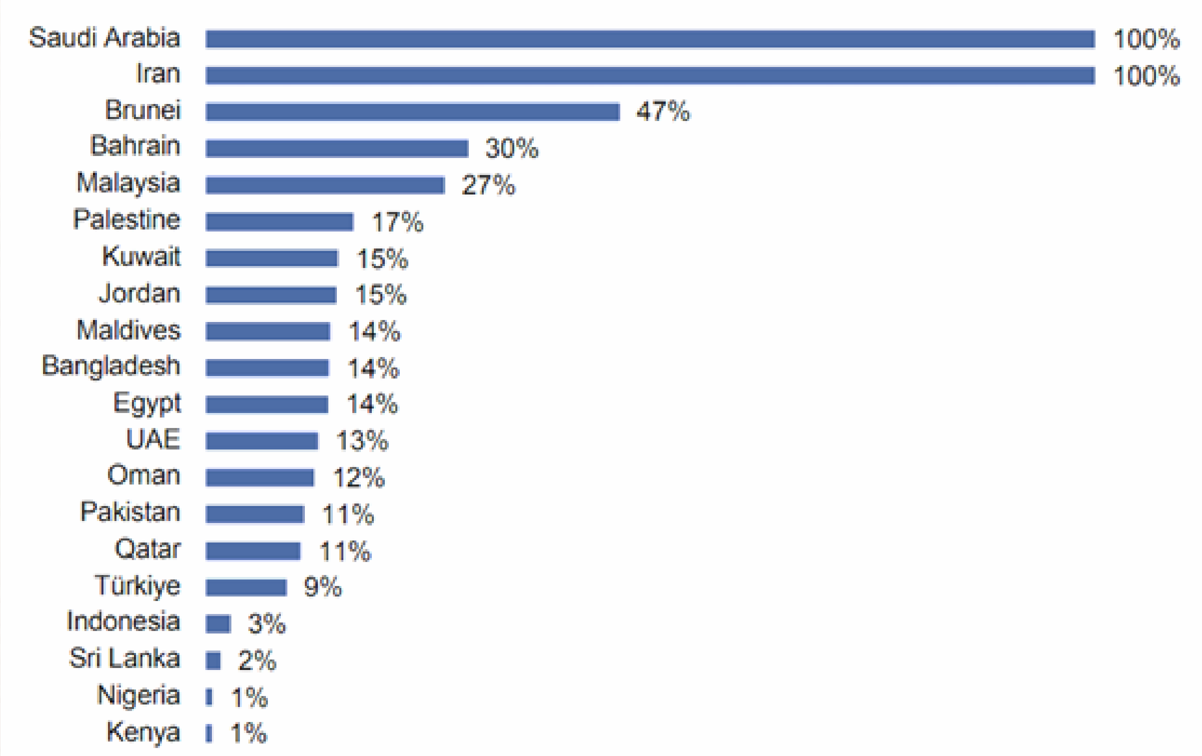
In light of the evolving financial landscape in Pakistan and the overall direction of moving toward a Shariah-compliant financial system, increasing Takaful's share in Pakistan is more than just a strategic goal—it is an essential step. The SECP's vision of raising Takaful's market share to over 30% by 2028 aligns with these needs, focusing on the development of a robust and inclusive Takaful sector.

Achieving this will require concerted efforts to boost public awareness, foster product innovation, and ensure regulatory support. This will ultimately lead to a more comprehensive and Shariah-compliant financial ecosystem that benefits all segments of society.

2. Study of International Jurisdictions

As of December 2021, 47 countries operate Islamic insurance, or Takaful, alongside conventional insurance, with Sudan and the UAE being the first to establish takaful operations in 1979[4] . Currently, Saudi Arabia and Iran have a 100% Takaful market share in their insurance sectors, followed by Brunei with a 47% share, and Bahrain and Malaysia with 30% and 27%, respectively.

Percentage Share of Islamic Insurance industry Relative to the Insurance Sector (%) (Q3 2023)

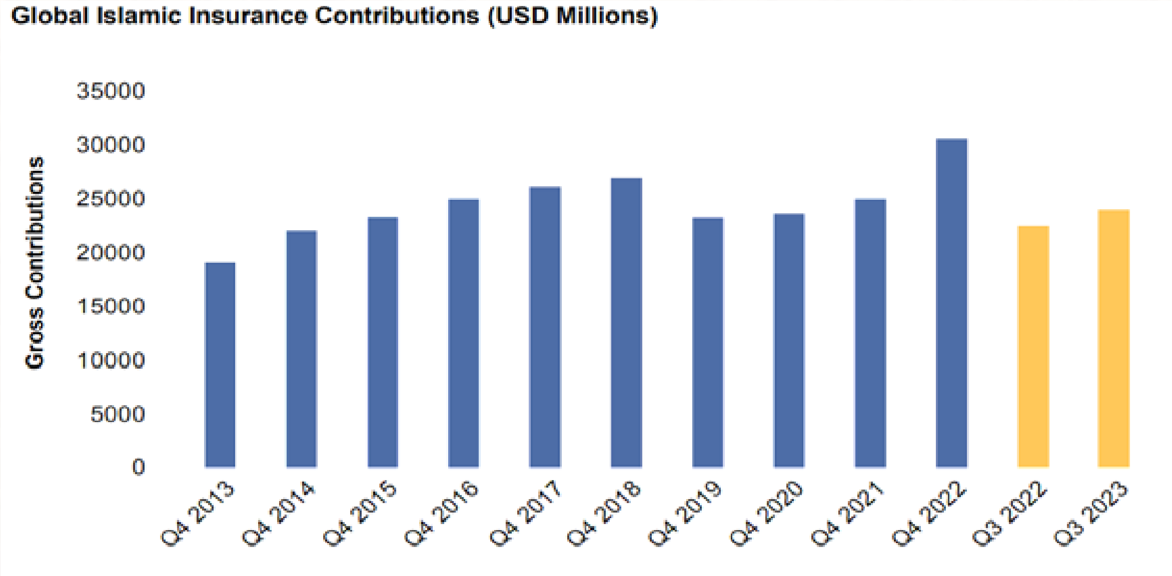


Source: IFSB Secretariat workings based on data from PSIFs, various RSAs' websites, annual financial reports of Islamic Insurance firms and other publicly available sources.

In 2023, global Islamic insurance, or Takaful, contributions grew by an estimated 6.5% year-on-year, reaching USD 24.05 billion. This growth was primarily driven by the general Islamic insurance segment, which experienced an impressive 21% increase. According to the Islamic Financial Services Industry Stability Report 2024 by IFSB, this positive trend is expected to continue in 2024. However, contributions from the family Islamic insurance, or family Takaful, segment grew by only 1% in 2023, primarily due to high inflation eroding consumer savings[5].

[4]https://www.emerald.com/insight/content/doi/10.1108/prr-02-2022-0022/full/pdf?title=takaful-chronology-of-establishment-in-47-countries

[5]IFSB Financial Stability Report 2024



Source: IFSB Secretariat workings based on data from PSIFs, various RSAs' websites, annual financial reports of Islamic Insurance firms and other publicly available sources.

For the purpose of this report, four jurisdictions were studied and compared with Pakistani market. The details of each jurisdiction are as follows:

2.1. Malaysia

After Malaysia's independence in 1957, domestic insurers emerged, and the Insurance Act of 1963 was enacted to regulate the industry. The development of the Takaful sector began in the early 1980s as a Shariah-compliant alternative to conventional insurance, complementing the Islamic bank established in 1983. A ruling by the Malaysian National Fatwa Committee declared life insurance void due to prohibited elements, prompting the government to form a Special Task Force in 1982. This led to the enactment of the Takaful Act 1984 and the incorporation of Syarikat Takaful Malaysia Berhad in November 1984. Regulatory oversight shifted to Bank Negara Malaysia (BNM) in 1988, which established the Shariah Advisory Council (SAC) in 1997 to provide guidance on Shariah issues in Islamic finance, including Takaful. The regulatory landscape evolved with the Islamic Financial Services Act 2013, which replaced the Takaful Act 1984 and strengthened Shariah governance.

Currently, Takaful holds 27% of the market share in Malaysia's insurance industry. In 2023, the sector reported contributions of RM 14.42 billion (USD 3.23 billion), with growth rates of 7.55% in family Takaful and 17.44% in general Takaful. In the non-life insurance sector, general Takaful holds a share of 20.7% while family takaful holds a share of 16.2% in the life insurance market. Malaysia primarily employs a hybrid Takaful model and has 11 Family Takaful Operators and 4 General Takaful Operators[6].

2.2. Sudan

In Sudan, the first Islamic insurance company, founded in 1979, pioneered the use of the mutual concept and Islamic principles in insurance. In 1980, the Insurance Controller, initially part of the Ministry of Commerce, oversaw the regulation of the insurance market. However, it

[6] https://www.bnm.gov.my/regulations/fsp-directory

was later integrated into the Ministry of Finance. The Insurance Supervision and Control Act of 1992 mandated that all insurance companies operate on the Islamic cooperative insurance model. This Act was eventually repealed and replaced by the Insurance Supervision Act of 2001 and its regulations in 2002. Similarly, the Insurance Control Act of 2001 was replaced by the Insurance Control Law of 2018, and its regulations of 2019.

Currently, the Insurance Supervisory Authority (ISA) and African Insurance Organization (AIO) regulate the Takaful and insurance sectors. Takaful is the only form of insurance in Sudan, having a 100% market share. In 2023, the sector reported contributions totalling SDG 60 billion (USD 0.10 billion), highlighting its importance to the national insurance market. The distribution is heavily skewed towards general Takaful, which accounts for 98.6%, while family Takaful represents only 1.4%. Sudan follows a cooperative (Mudarabah) model, with 13 Takaful operators and 1 Retakaful operator in the industry.

2.3. Kingdom of Saudi Arabia

In the Kingdom of Saudi Arabia (KSA), insurance first appeared in the 1950s, through foreign agents and branches. The first local insurer in the market was the Red Sea Company in 1974. the first licensed national insurance company in the Kingdom, Company for Cooperative Insurance (Tawuniya), was established in 1986. It operated in line with cooperative insurance principles. The Cooperative Insurance Companies Control Law was issued in 2005 by the insurance regulator, Saudi Central Bank (SAMA), requiring insurers in the country to operate on the cooperative insurance model in line with Shariah rules and principles. SAMA regulated the insurance market till 2023 and now Insurance Authority (IA) is overseeing the insurance industry in KSA.

The sector is regulated through the Law on Supervision of Co-operative Insurance Companies and associated frameworks, ensuring a Shariah-compliant and cooperative approach. Takaful holds a 100% share of the insurance market, showcasing its integral role in the country's financial system. In 2023, Insurance industry recorded a total contribution of SR 65.5 billion (USD 17.45 billion). The industry is divided into three businesses: Protection and Savings, Health, and General Insurance. Among them health has the highest market share of 59% followed by General Insurance (37.1%) and Protection and Savings (3.9%).

2.4. Indonesia

The history of Shariah insurance in Indonesia dates back to 1994 with the establishment of Takaful Indonesia. However, Shariah insurance in Indonesia lacks a dedicated legal framework and operates under Law No. 40 of 1992, which is based on conventional insurance regulations. In 1999, the National Shariah Council (DSN) was formed by the Indonesian Ulema Council (MUI) to provide Fatwas and supervise their implementation, promoting the development of Islamic finance, business, and economics in the country. Although DSN has issued various Fatwas related to Shariah insurance, these do not hold legal force under Indonesia's national law.

The Financial Services Authority (OJK) oversees the regulation of the insurance industry. As of 2023, Takaful holds only 9% of the market share in Indonesia, with contributions totalling IDR 27.57 trillion (USD 1.74 billion). The market is dominated by life insurance, which accounts for 86% of the share, leaving 14% for general Takaful. Indonesia uses a hybrid Takaful model and offers a variety of Shariah-compliant services. The sector comprises 40 window Takaful operators, 3 window Retakaful operators, 14 full-fledged Takaful operators, and 1 Retakaful operator.

2.5. Comparative Statement of International Jurisdictions

Area	Malaysia	Sudan	KSA	Indonesia
Regulatory Body	Bank Negara Malaysia (BNM)	Insurance Supervisory Authority (ISA) and African Insurance Organization (AIO)[7]	Insurance Authority (IA) (Saudi Arabian Monetary Authority (SAMA) till 2023)	Financial Services Authority (OJK)
Regulatory Framework	Islamic Financial Services Act 2013	Insurance Supervision Act 2001 & Insurance Act 2003	Law on Supervision of Co-operative Insurance Companies and the Insurance Regulatory Framework	Law of the Republic of Indonesia Number 40 of 2014 on Insurance
Share of Takaful Sector's Business Relative to Insurance Sector	27%	100%	100%[8]	3%
Contribution 2023	RM 14.42 billion (USD 3.23 billion)[9]	SDG 60 billion (USD 0.10 billion)[10]	SR 65.5 billion (USD 17.45 billion)[11]	IDR 27.57 T (USD 1.74 billion)[12]
Contribution Growth by Type (2023)	Family: 7.55% General: 17.44%[13]		Protection and Savings: 36.9% Health: 21.4% General: 23.5%[14]	Family: 10.65% General: 52.16%
Market Share	General: 20.7% Family: 16.2% (with respect to conventional insurance)[15]	General: 98% Family: 1.4 – 2.4%	Health: 59% General: 37.1% Protection and Savings: 3.9%[16]	Life: 86% General: 14%
Primary Takaful Model	Hybrid	Cooperative (Mudarabah)	Cooperative (Mudarabah)[17]	Hybrid
No. of Companies	11 Family Takaful Operators 4 General Takaful Operators[18]	14 companies[19]	26 companies[20]	40 Takaful & 3 Retakaful Windows. 14 full-fledged Takaful & 1 Retakaful Company

[7]https://www.globaldata.com/store/report/sudan-insurance-industry-government-regulation-analysis/
[8]https://www.ifsb.org/wp-content/uploads/2024/09/IFSB-Stability-Report-2024-8.pdf
[9]Annual Report 2023 https://takaful4all.org/en/annual-reports/
[10]ISLAMIC FINANCIAL SERVICES INDUSTRY STABILITY REPORT 2023
[11]The Insurance Market Report 2023 by Insurance Authority
[12]https://erwin-noekman.com/2023/02/04/ada-apa-dengan-industri-asuransi-syariah/
[13]https://takaful4all.org/en/annual-reports/
[14]The Insurance Market Report 2023 by Insurance Authority
[15]https://takaful4all.org/en/annual-reports/#elementor-action%3Aaction%3Dpopup%3Aopen%26settings%3DeyJpZCI6IjIxODAxIiwidG9nZ2xlIjpmYWxzZX0%3D`
[16]The Insurance Market Report 2023 by Insurance Authority
[17]ISLAMIC FINANCIAL SERVICES INDUSTRY STABILITY REPORT" 2023
[18]https://www.bnm.gov.my/regulations/fsp-directory
[19]https://gaif.org/FE/Members/Details/bb79673a-fa9c-4996-b34d-d2cd816a68dc
[20]https://edge.sitecorecloud.io/millimaninc5660-milliman6442-prod27d5-0001/media/Milliman/PDFs/2024-Articles/Milliman-Insurance-Industry-Report-YE2023.pdf

3. Key Challenges and Growth Deterrents

3.1.Takaful Awareness Deficiency and Misconceptions

One of the biggest hurdles that affect the uptake of Takaful in Pakistan is the widespread lack of awareness and prevalent misconception among the general public, policymakers and even within the insurance industry. Among the public, a common misconception exists that Takaful, like other Islamic financial services, is similar to conventional insurance and is white labelled as shariah compliant. In a country with limited financial literacy and low insurance penetration, effectively communicating Takaful's mutual assistance and risk-sharing benefits remains a significant challenge.

This lack of awareness also extends to policymakers, many of whom may either not have the requisite level of understanding or may not even have the knowledge of the availability of takaful as a risk mitigation tool and hence conventional insurance is often prioritized as the default solution towards protection and risk mitigation in policy and government level decisions.

3.2. Trust in Takaful Governance Model

The Takaful sector also faces the challenge related to perceptions about the governance and Shariah compliance of Takaful products. Factors such as limited disclosures by operators, adequacy of shariah governance, lack of standardization and inadequate awareness about the underlying mechanisms of Takaful contribute to scepticism among general public and other stakeholders, including policymakers, regarding whether takaful products genuinely adhere to Shariah principles or are merely a repackaged form of conventional insurance.

The extent to which Takaful operators adhere to Islamic finance standards, such as those set by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB), remains a point of concern among stakeholders. Additionally, the implementation of the Shariah Governance Framework (SGF), including the roles of Shariah advisors, Shariah compliance officers, and Shariah audits, is an area requiring further clarity. Assessing whether governance practices are robust, transparent, and aligned with international standards, particularly concerning the independence of Shariah audits and the consistent application of Shariah principles across all aspects of Takaful operations, remains essential for building trust for Takaful.

3.3. Marketing of Takaful Products

There appears to be a significant lack of marketing efforts dedicated to promoting Takaful products by both Insurance Companies and Takaful Operators despite that effective marketing is essential for generating the demand for takaful. While the broader insurance industry faces challenges in effectively conveying the true benefits of insurance through marketing, the situation is particularly dire for Takaful. Marketing efforts specifically designed to highlight Takaful's unique value proposition are almost non-existent.

3.4. Positioning of Takaful Products by Window Takaful Operators

Within the insurance industry, companies with Window Takaful operations have adopted a status quo approach, with many window takaful operators continuing to largely focus on conventional model for business generation. Takaful is generally considered and treated as a supplementary service only, as it is offered where the prospective policyholder either demands takaful as a choice or regrets purchasing insurance due to Shariah concerns. Rather than positioning Takaful as the primary solution to proactively create demand or even placing takaful at the same level as they place their conventional products, takaful is treated as a secondary option, used only when explicit demand arises.

3.5. Capital Adequacy for Takaful operations

There is a widespread misconception that Window Takaful Operations (WTOs) operate with only PKR 50 million in capital, as required under SECP Circular No. 08 of 2014 for initiating such operations. This perception fails to account for the crucial regulatory provision that mandates financial backing from the parent insurer through Qard-e-Hasna in the event of any solvency pressure. As a result, the effective capital base supporting WTOs is much higher than commonly assumed.

In contrast, dedicated Takaful Operators are subject to significantly higher capital requirements — PKR 500 million for general Takaful and PKR 700 million for family Takaful. With recent phased enhancements in minimum capital thresholds for insurers (up to PKR 2 billion for non-life and PKR 3 billion for life insurers), the disparity in nominal capital may appear stark. However, the embedded capital support and financial backing by the conventional insurer mitigates this gap. Misunderstanding this framework can create a misleading impression that WTOs are undercapitalized, potentially affecting their perceived financial strength, market trust, and ability to scale.

3.6. Regulatory & Shariah Guidelines for Conversions

The regulatory framework for Takaful in Pakistan, defined by the Takaful Rules 2012, permits life insurers to offer Family Takaful and non-life insurers to provide General Takaful services. However, should any insurer wish to convert its operations into takaful, there appears to be lack of regulatory as well as shariah guidance, showing the path necessary for initiation and conclusion of conversion.

In this regard, the only provision available is rule 7 of the Takaful Rules, 2012 which deliberates the conversion of a non-life insurer into a general takaful operator. Even the said rule, does not provide insights into the regulatory and shariah requirements for conversion, instead states that the Commission shall on fulfilment of certain requirements, as may be specified from time to time, authorize the registered insurer as a Takaful Operator. Further, no provision is available in respect of conversion of a life insurer into a family takaful operator or the conversion of the regular premium long-term life insurance savings products into family takaful plans.

The SECP has issued Guidelines for Offering Islamic Financial Services, 2023, which broadly covers the requirements for conversion of a conventional financial institution into an Islamic financial institution. However, since the guidelines are aimed at all financial institutions in general, they do not dive deep into the specific shariah and regulatory requirements necessary for conversion of insurance business into takaful business. Without detailed guidance, integrating Takaful into the broader insurance market will remain a significant challenge.

3.7. Availability of Retakaful

In recent times, a number of Takaful Operators and industry stakeholders had approached the SECP highlighting the shortage, or in certain instances complete unavailability, of re-takaful solutions for specific lines of business. Notably, the Takaful Rules, 2012, require all Takaful operators to be reinsured exclusively by Shariah-compliant retakaful operators and no allowance is available for placement of takaful risks on reinsurance basis.

This reflects a growing concern in the market, where operators are left with limited options to prudently manage risk while complying with Shariah principles, due to a tightening reinsurance landscape. There have been suggestions and discussions around allowing placement of takaful risks on conventional reinsurance basis, however, only in exceptional circumstances or out of dire necessity and after full exhaustion of the local retakaful capacity, particularly through Pakistan Reinsurance Company Limited (PRCL).

Without sufficient retakaful capacity or unavailability of retakaful solutions, Takaful operators struggle to manage risk effectively, diminishing their competitiveness and limiting their ability to diversify their offerings. This restrains the industry's potential to meet the evolving protection needs of consumers. With the growth expected in the takaful sector in the coming years, the issue of retakaful inadequacy or unavailability and not allowing conventional reinsurance in dire cases, may create challenges for not only living up to the demand for takaful but also the conversion of the industry by large towards takaful.

3.8. Talent Gap in Takaful Sector

The growth of the Takaful industry in Pakistan is also constrained by a shortage of skilled professionals who possess expertise on Islamic finance (specifically on takaful) and the technical capabilities to leverage on the concept of takaful to develop innovative and disruptive products that can create an impact. The focus has generally and largely remained merely to create shariah compliant alternatives to the conventional insurance products. The lack of comprehensive training opportunities further impedes staff and resource development and whilst one comes across many training courses on the subject of Islamic banking, one seldom comes across structured training opportunities that are takaful oriented.

4. Potential Growth Horizons

4.1. Federal Shariah Court Decision and Economic Transformation by 2027

The Federal Shariah Court's decision mandating a shift towards an interest-free economy presents a significant opportunity for the expansion of Takaful. With the government's commitment to eliminating Riba by 2027, financial institutions, including insurers, would have to act in order to transition towards Shariah-compliant models. This creates a conducive environment for Takaful growth, as both corporate and individual clients seek Islamic alternatives to conventional insurance. The transformation of the economy will likely drive regulatory and infrastructural support for Takaful, accelerating its adoption across all financial sectors.

4.2. Conversion of Conventional Banking – SBP Vision 2028

The State Bank of Pakistan's (SBP) Vision 2028 emphasizes a gradual but complete transition from conventional banking to Islamic finance. This shift will naturally lead to an increased demand for Takaful products, as Islamic banks will require Shariah-compliant risk mitigation solutions. Furthermore, banks play a key role in bancassurance, which contributes a significant amount of premium to the overall pie, and therefore, their conversion will push life and non-life insurers to distribute Takaful solutions only to cater to their clients through bancassurance.

4.3. Public Property Insurance – Takaful Cover

Under the current legal framework, public property risks are solely underwritten by M/s National Insurance Company Limited (NICL), the state-owned non-life insurer. Unfortunately, NICL does not have authorization as a window takaful operator and hence is not permitted to offer takaful solutions. This creates a big gap, since the Government of Pakistan and its institutions do have access to Takaful solutions for public property risks. Infrastructure projects, state-owned enterprises, autonomous and semi-autonomous bodies, municipal properties etc. require extensive insurance coverage, and integrating Takaful into this sector can enhance its acceptance.

4.4. Voluntary Conversions for Growth of Takaful Market

For the Takaful market to grow significantly within Pakistan, the service providers and the service acquirers both can voluntarily opt for conversion of their businesses/requirements towards Takaful, as follows:

- **Mandatory Insurances:** WTO's can consider that coverages under mandatory insurance such as motor third party liability and group life insurance would be covered under Takaful solutions.
- **Social Insurance Schemes:** The Federal and Provincial Governments can consider gradual conversion of government backed insurance scheme such as the Sehat Sahulat Program, Crop Loan Insurance Scheme, Livestock Insurance Scheme for Borrowers etc.
- **Personal Lines Non-Life Insurance (Travel, Motor, etc.):** Non-life WTO's can also consider that coverages under personal lines non-life insurance such as travel insurance, health insurance and motor insurance be gradually covered under Takaful solutions.
- **Life Insurance – Regular Premium:** Life WTO's can also consider gradual and wider conversion of their regular premium portfolio to be underwritten on Takaful basis.
- **Branch conversion:** Insurers can also consider step wise conversion of their branches (area wise) to Takaful to meet the expected increased demand in the future.

4.5. Standardized Takaful Products

While term life and health insurance and Takaful products are available in Pakistan, there are currently no standardized offerings that ensures uniformity across the industry. Each insurer/Takaful operator designs its own versions of these products, resulting in variations in coverage, pricing, eligibility criteria, and exclusions.

The introduction of standardized Takaful products as a mandatory offering across the industry can serve as a game-changer in expanding market reach and financial inclusion. The underpinning idea is that a simple, low-cost insurance product is made available by all takaful operators with uniform policy terms. The goal is to ensure affordability, transparency, and ease of access, thereby increasing Takaful penetration among lower and middle-income groups.

5. Policy Recommendations and Way Forward

5.1. Takaful Adoption and Conversions

Transition Plan for Takaful Adoption

In line with the 26th Constitutional Amendment and the Federal Shariah Court's directive for a riba-free economy by 2027, it is crucial that both SECP and individual insurance companies take proactive steps towards the transition to Takaful. SECP, in consultation with Shariah scholars and industry stakeholders, needs to formulate a comprehensive, industry-wide Strategic Transition Plan to facilitate the insurance industry's transition to Takaful. This plan may outline SECP's approach to supporting the transition process, including stakeholder engagement, provision of regulatory support, and identification of key areas for facilitating the industry-wide conversion to Takaful. It may also highlight the necessary actions that insurers need to take to align their operations with Shariah principles. This plan may address the conversion of insurance products, investment structures, and operational processes, for ensuring alignment with Shariah principles. The plan may have defined timelines, milestones, and action items to ensure a smooth and consistent transition across the industry within time. Additionally, to ensure effective implementation, SECP may consider establishing a Takaful Committee comprising of SECP representation, Shariah scholars, industry experts, and other relevant stakeholders. This task force may help in developing the Transition Plan, providing oversight, and ensuring compliance with Shariah governance standards throughout the transition process.

At company level, the insurers need to develop comprehensive Takaful Adoption Plans, approved by their board and Shariah advisor, outlining their strategy for transitioning to Takaful and aligning with the SECP's plan. These plans may start with an assessment of the insurer's preparedness to meet evolving sector demands, including a gap analysis of policies, products, services, infrastructure, human resources, and areas needing improvement for successful conversion.

The adoption plan may also specify the strategy for transition, whether through geographic (branch-wise) conversion or business-specific conversion targeting certain classes of business. Such plans will enable companies to assess their current operations and identify areas for transformation in both product offerings and operations. This assessment, followed by clear action items for converting existing products and restructuring investment portfolios to align with Shariah principles, will provide a solid foundation for the transition to Takaful. Additionally, the plan should address the transition of operational processes, such as underwriting, claims management, and policyholder surplus distribution.

Facilitation for Takaful Licensing and Product Approval

To enhance Takaful penetration and foster a more Shariah-compliant insurance ecosystem, SECP may facilitate and promote Takaful licensing and product approvals. SECP could encourage new entrants to obtain licenses as full-fledged Takaful operators rather than conventional insurers, creating a more conducive environment for Shariah-compliant insurance. Additionally, SECP may consider prioritizing the approval of new life insurance products under the Takaful model, encouraging companies to focus on Takaful product development. These measures would support the industry's natural progression towards an Islamic financial framework, contributing to a smoother transition toward a Riba-free economy by 2027.

Window Takaful Authorizations of Insurers

As discussed earlier, the general Takaful market comprises of two dedicated general Takaful operators and twenty companies with window operations, while the remaining eight non-life insurance companies, including the public sector insurer NICL, do not have Window Takaful Authorization. Considering the significant business volume of companies like NICL, which insures all public properties, it is essential for SECP to encourage them to obtain window Takaful Authorizations.

SECP needs to engage with the Ministry for NICL and with other insurance companies, demanding their plan for having window takaful authorization to remain relevant in the transitioning market. This will not only facilitate a smoother transition of the industry toward Takaful but will also enable companies to tap into the customer base of Islamic banks. Without any Shariah-compliant products, these companies risk losing potential bancassurance business, as Islamic banks will exclusively sell Takaful rather than conventional insurance products.

Comprehensive Policy Guidelines for the Transition to Takaful

As highlighted earlier, there is a lack of clear guidance for the complete conversion from conventional insurance business to Takaful. It is about time that SECP, in collaboration with the Shariah Advisory Committee and industry players, considers developing comprehensive guidelines for both entity-level and product-level conversions.

At the entity level, a clear roadmap is needed for insurers undergoing conversion, including phased strategies for companies operating Window Takaful Operations (WTOs) and a defined framework for those without WTOs. Adopting a transitional approach will ensure business continuity while gradually phasing out conventional operations.

At the product level, guidelines may be established for converting long-term conventional life insurance products with investment components, such as participating (with-profit endowment) policies, unit-linked insurance, universal life policies, and whole life policies.

A dedicated working group, comprising industry experts and Shariah scholars, may be established to oversee the transition process and provide necessary support to insurers undergoing conversion, including guidelines on restructuring investment portfolios in compliance with Islamic finance principles.

A structured and collaborative approach will ease the transition process and support the growth of Takaful as a viable alternative to conventional insurance.

Conversion of Conventional Insurance Products

Another critical area requiring attention is the conversion of conventional insurance products into Shariah-compliant Takaful alternatives. As the industry prepares towards Shariah-compliant transition, insurers must explore the feasibility of offering takaful variants for their existing product lines. While Shariah-compliant alternatives already exist for unit-linked, whole life, term life, and health plans, a significant gap remains in the availability of Takaful-based participating or with-profit endowment products.

According to SECP's Insurance Industry Statistics 2023 report, participating (with-profit) endowment products accounted for nearly 30% of the total life insurance premium in 2023—highlighting their critical importance in the overall product mix. Despite this sizable market share, no genuine Shariah-compliant equivalent currently exists.

To address this gap, Companies, specially SLIC, with close consultation with shariah scholars needs to consider initiating efforts to develop a Shariah-compliant model for participating products. Such an initiative is essential not only to preserve policyholder value and ensure market continuity, but also to support a seamless and inclusive transition toward a fully Islamic insurance ecosystem in Pakistan.

Conversion of National Level Scheme

Large-scale national insurance schemes offer a significant opportunity for accelerating Takaful adoption. The Sehat Sahulat Program, which contributes 38% of the total life industry premiums, along with other government-backed schemes like the Crop Loan Insurance Scheme (CLIS), Livestock Insurance scheme for Borrowers (LISB), and Punjab Fasal Beema, may be considered for transitioning to Shariah-compliant models. SECP may consider engaging with federal and provincial authorities to encourage gradual conversion of these schemes, whilst aiming that future national-level insurance schemes are launched exclusively under Takaful model.

5.2. Governance

Alignment with International Standards on Takaful

On the international front, the standard setting bodies on the subject of Islamic Finance are the AAOIFI (Accounting and Auditing Organization for Islamic Financial Institutions) and IFSB (Islamic Financial Services Board). Unfortunately, in Pakistan not a single international standard on Takaful has been adopted.

These standards provide comprehensive frameworks for governance, financial reporting, and risk management tailored specifically for Islamic finance. Implementing AAOIFI and IFSB standards can enhance comparability, improve investor confidence, and support the sustainable growth of the Takaful industry by ensuring alignment with globally recognized Islamic financial principles.

In this regard, SECP may consider reviewing international standards in relation to the current regulatory framework to identify gaps and strengthen it, particularly regarding Shariah compliance. This would involve aligning the current Takaful regulatory framework with the standards set by AAOIFI and IFSB.

Additionally, SECP may explore the formulation of a dedicated Shariah Governance Framework for Takaful operators. This framework would enhance Shariah compliance across the sector and align with the AAOIFI and IFSB guidelines. It could include comprehensive guidelines on establishing Shariah compliance departments, appointing qualified Shariah advisors, implementing rigorous internal Shariah audit functions, and ensuring effective Shariah compliance review mechanisms, as seen in international jurisdictions.

Aligning with AAOIFI and IFSB standards may help strengthening the regulatory framework, ensuring higher governance, transparency, Shariah compliance and may help in boosting the consumer as well as investor confidence.

Shariah Advisory/Supervisory Board for Takaful Operators

Rule 10 of the Takaful Rules, 2012, requires Takaful operators to appoint a Shariah Advisor to handle Shariah-related matters. However, there is currently no requirement for establishing a Shariah Advisory/Supervisory Board (SSB). Relying solely on a single Shariah Advisor in a Takaful company, rather than an SSB, presents several drawbacks that can adversely impact governance, compliance, and market confidence.

One of the primary concerns is the absence of collective decision-making and diverse expertise. Relying on a single advisor increases the risk of conflict of interest, as the advisor may face pressure to approve transactions that prioritize commercial interests over strict Shariah compliance. Furthermore, the lack of peer review or internal accountability mechanisms heightens the likelihood of compromised decision-making.

To address these concerns, SECP may consider introducing a requirement for Takaful operators to appoint a Shariah Advisory/Supervisory Board instead of a single Shariah Advisor. Such a board could comprise multiple scholars specializing in various fields, including Islamic jurisprudence (Fiqh), finance, risk management, and legal affairs. This diversity would ensure comprehensive and well-reviewed decisions, minimizing the risk of errors, personal biases, or inconsistent rulings.

Application of IFRS 17 on Takaful Contracts

The implementation of IFRS 17 for insurance contracts presents an opportunity to develop specific guidance for Takaful operators to align with global best practices while preserving Shariah principles. Due to the unique structure of Takaful, which involves risk-sharing rather than risk transfer, direct application of IFRS 17 may present challenges. The lack of standardized guidance tailored to Takaful operations can lead to inconsistencies in financial reporting, affecting stakeholders' confidence and regulatory oversight.

The SECP in coordination with the Institute of Chartered Accountants of Pakistan is working on the development of Takaful Accounting Regulations tailoring the requirements of IFRS 17 for Takaful contracts under ICAP's IFRS 17 Working Group. A standardized approach should be established for recognizing Takaful contributions, managing policyholders' and operators' funds, and ensuring transparent surplus and deficit management. Disclosure requirements should be enhanced to provide detailed financial information on the nature of Takaful contracts, measurement models used, and risk adjustment methodologies that align with Shariah principles.

Application of IFRS 17 on Takaful also requires capacity-building initiatives to equip Takaful operators, auditors, and financial professionals with the necessary expertise for effective implementation. Takaful business, at its core, is fund based i.e. there are different funds representing: (a) the interests of shareholders; (b) the risk sharing between participants; and (c) the participants investments. Hence, an important point for consideration remains the presentation of these distinct funds in the financial statements of takaful operators, i.e. whether the presentation is to be made by combining all the funds or the presentation is to be made of these funds distinctly.

Further, the presentation of takaful results in case of window takaful operations in the financial statements of the insurance company also requires consideration i.e. whether the presentation is to be made by consolidating the takaful and conventional results on a line by line basis or on the takaful operations are to be reported distinctly as a single line item.

Surplus Distribution

A key unique selling proposition (USP) of Takaful is that any surplus in the Participant Takaful Fund (PTF), after maintaining adequate reserves, rightfully belongs to the participants (policyholders) and should be distributed to them. However, data reveals that over the past five years, only two general Takaful operators have distributed the fund's surplus to policyholders, and that too, only once. This low distribution rate warrants a thorough investigation into the underlying reasons within the non-life sector, including factors such as high charges, imprudent underwriting practices, or inadequate investment returns.

SECP may consider reviewing underwriting practices and PTF management to ensure that only reasonable charges are applied to the funds and that investment strategies are prudent. Furthermore, SECP could issue guidelines on transparent surplus distribution, outlining clear methodology, frequency, and Shariah-compliant investment practices, while also setting standards for applying charges and ensuring timely distribution. Such measures will help build participant trust, promote financial sustainability, and reinforce the Shariah principles that form the foundation of the Takaful industry.

5.3. Capacity Building for Risk Absorption

Adequacy of Capital for Window Takaful Operations

The SECP in its five-year strategic plan for insurance industry, as mentioned in previous sections, has set the objective of increasing Takaful's market share to over 30% by 2028, and with the Federal Shariah Court ruling requiring the banking sector to be fully Shariah-compliant by 2028, Takaful operators have a great opportunity to expand their operations in takaful. However, without enough capital, they won't be able to develop the requisite level of risk-taking capacity, spend on marketing and image building of takaful products, or invest in the technology and infrastructure needed to stay ahead in a fast-changing market.

To support the growth of the Takaful sector and strengthen window operations, it's crucial to increase the minimum capital requirement for window Takaful operators. This would not only help them remain financially stable, increase their capacity to underwrite risks but also allow them to take full advantage of the growth opportunities in the market. A stronger financial foundation will ensure window Takaful operators can play their part in meeting SECP's goals and supporting Pakistan's transition to a fully Shariah-compliant financial system by 2028.

More than a decade has passed and the requirement of PKR 50 million as initial capital for window operations remains the same. Whilst the regulatory requirements for window takaful operations demand the support of the insurer in the case of solvency strain through qard-e-hasna¸ hence providing financial backing, still the capital requirements for window operations remain extremely modest.

Considering that the initial requirement was suitable for the industry landscape a decade ago, there is a need of revising and increasing the minimum seed capital requirement for new WTO's and gradually enhancing the requirement for existing operators.

Retakaful Capacity Building

As Pakistan moves toward a fully Shariah-compliant insurance ecosystem, the availability and adequacy of Retakaful capacity will become increasingly critical. To support this transition, non-life insurance companies—particularly the Pakistan Reinsurance Company Limited (PRCL) having window retakaful operations — need to take concrete steps to develop and enhance domestic Retakaful capabilities that enable greater local retention of risk.

Given its central role as the national reinsurer, PRCL needs to take the lead to expand its retakaful capacity in order to meet the evolving needs of the Takaful industry. Building robust local Retakaful infrastructure will reduce dependence on foreign operators, and promote national financial resilience.

In parallel, other non-life insurers are also encouraged to assess and enhance their own Retakaful arrangements to prepare for the anticipated surge in demand. A well-developed domestic Retakaful market will ensure that the entire risk-sharing value chain—from underwriting to reinsurance—supports the sustainable growth of the Takaful ecosystem in Pakistan.

Allowing Conventional Reinsurance for Takaful Risks on Dire Need Basis

Whilst the first and foremost action is to work towards increasing the retakaful capacity of the local market, nonetheless, in exceptional circumstances where local and Shariah-compliant international capacity is demonstrably insufficient or unavailable, the takaful operators, Shariah Advisors and the Commission may consider allowing Takaful Operators to engage with conventional reinsurers strictly on grounds of necessity.

It is important to understand that re-takaful operators, like their conventional counterparts, manage their exposure based on per-company, per-country, and per-region capacity limits. These are hea-ily influenced by claim history, macroeconomic volatility, geopolitical risks, and sovereign credit rating. Given Pakistan's recent economic shocks, reinsurers have become increasingly cautious, further narrowing available capacity. In such cases, regulatory accommodation, subject to rigorou us disclosure, justification, and Board-level oversight, may serve as a pragmatic response to ensure business continuity while preserving the long-term vision of a resilient, Shariah-aligned risk management framework

Solvency of Participant's Takaful Fund

Under the existing solvency framework for general takaful and general Window Takaful Operators (WTOs), the Participant Takaful Fund (PTF) is only required to maintain net admissible assets in excess of its liabilities. This means that solvency margins are not currently mandated within the PTF to enhance its financial resilience or reduce reliance on qard-e-hasna in times of deficit.

As previously noted, when the PTF experiences solvency strain, the takaful operator is obligated to provide qard-e-hasna to restore its solvency. However, to support the development and anticipated growth of the takaful sector, as outlined earlier, it is essential to build financial resilience within the PTF. Doing so not only strengthens the fund and enhances its risk-bearing capacity, but also reduces the burden on shareholders to inject qard-e-hasna in the event of financial distress.

Therefore, the current solvency regime for PTFs warrants a reassessment to reinforce risk management, bolster market confidence, and secure the long-term viability of the takaful industry. A thorough review of the solvency framework by the SECP, in collaboration with industry stakeholders, is necessary to ensure adequate liquidity and financial stability in the face of claims volatility.

Furthermore, the proposed Risk-Based Capital (RBC) regime for the insurance sector in Pakistan, must carefully consider the unique features of Takaful, particularly the distinct separation between the Participant Takaful Fund (PTF), the Participant Investment Fund (PIF) and the shareholders' fund (SHF) or the operator fund (OPF). Unlike conventional insurance, Takaful operates on the principles of mutual risk-sharing and qard-e-hasna support in the event of deficits. Therefore, the RBC model should adequately capture the financial dynamics and risk exposures inherent in Takaful structures, especially those related to the treatment of solvency within the PTF.

To ensure fair and effective implementation, the RBC framework should be adapted to reflect the operational and Shariah-compliant nature of Takaful. This includes recognizing the absence of shareholder capital within the PTF, the conditional nature of qard-e-hasna, and the need for sufficient risk buffers within the fund itself. A tailored approach would not only strengthen the financial soundness of Takaful operators but also support the long-term development of the industry in line with its ethical and cooperative foundations.

5.4. Takaful Awareness and Availability

Launch of Takaful Specific Awareness Campaign

As discussed in earlier sections, the lack of Takaful-specific awareness remains a key barrier to its wider adoption, even within the broader Islamic financial products. To address this, SECP and the Insurance Association of Pakistan (IAP), should work towards a targeted Takaful awareness campaign. This initiative should focus on educating the public about the Shariah principles governing Takaful, its risk-sharing model, and how it differs from conventional insurance. Focused awareness campaigns targeting academia, students, incubation centres and business circles through the Chambers of Commerce and Industry should be developed.

The campaign should leverage digital platforms, mainstream media, and community engagement programs to ensure wider reach and impact. By enhancing public understanding, we can foster greater acceptance of Takaful, ultimately supporting its growth and penetration in the market.

Furthermore, tailored training programs should be developed for the regulator, industry professionals serving the financial services market in general and the insurance sector in particular, academia and students to develop more knowledgeable and skilful human resource.

Launch of Standard Takaful Plan(s)

The availability of multiple term life products with varying terms and conditions makes it challenging for customers, especially those with limited time and knowledge, to make informed decisions. Additionally, suitable coverage may not always be accessible for the intended sum assured. To address these issues and enhance consumer protection, SECP in consultation with the industry, may consider developing a standardized term life Takaful product and health Takaful product with simplified features and uniform terms and conditions under a common name, such as “Assaan Takaful or Sehal Takaful (Simple Takaful).”

This standardized offering, made available by all Takaful operators, would promote transparency, ease of choice, and accessibility for customers, while also reducing the risk of mis-selling and minimizing potential disputes during claim settlements. Such an initiative would enhance consumer confidence and contribute to the sustainable growth of the Takaful industry.

This further not only creates inroads for Takaful in the masses, but would assist the greater agenda of financial inclusion by offering a simple, low-cost, and widely recognized protection plans, which are shariah compliant. The SECP being the regulator of the industry may also consider to offer its patronage in marketing of the products to the masses.

Takaful Product Availability

In light of the aforementioned macroeconomic changes, which mandate the transition of Pakistan's economy to a Shariah-compliant, interest-free system by 2028, it is crucial for insurance companies to review and strengthen their Takaful product offerings. Companies need to ensure that their Takaful products are well-positioned to meet the anticipated demand arising from this mass transition.

Particularly, those companies that have limited Takaful offerings and smaller takaful business as compared to conventional one, must prioritize the development and innovation of new products to cater to emerging consumer needs, shifting economic conditions, and untapped market opportunities. State Life Insurance Corporation (SLIC), for example, may consider increasing its focus on Takaful. Currently, only 0.4% of SLIC's total business is derived from Takaful. Given that SLIC holds 66.5% of the overall market share in the industry, it is imperative for the company to start planning the expansion of its Takaful business.

Product availability will be a key factor in ensuring that the Takaful sector is adequately positioned to address the demands of a rapidly evolving financial ecosystem. By proactively aligning their product offerings with the broader goals of a Shariah-compliant economy, the industry can play a pivotal role in establishing a robust and inclusive Islamic finance framework in Pakistan.

Human Resource Capacity Building

As the Takaful industry expands in line with Pakistan's transition to a Shariah-compliant insurance framework, building sector-specific human resource capacity is also essential. There is a pressing need for trained professionals with expertise in Takaful operations, Shariah compliance, and Islamic finance alongside core insurance functions such as underwriting, risk management, and actuarial science.

SECP, in collaboration with the Pakistan Insurance Institute (PII), Institute of Financial Markets of Pakistan academia, and global standard-setters like AAOIFI and IFSB, may develop specialized training and certification programs for industry professionals and regulatory staff. Insurers are also encouraged to invest in internal capacity building through dedicated training tracks, Shariah compliance teams, and talent development programs.

A skilled workforce will ensure operational efficiency, Shariah integrity, and long-term sustainability of the Takaful ecosystem.

Takaful Specific Committee

The Insurance Association of Pakistan (IAP), as the representative body of all insurers in the country, should establish a dedicated Takaful Committee at the association level to effectively address Takaful-related developments and industry-specific challenges. This committee should serve as a unified platform for coordinating efforts to enhance Takaful penetration, standardize practices, and provide industry-wide guidance on compliance with Shariah principles. Additionally, the committee should actively collaborate with SECP, Shariah scholars, and other stakeholders to support the implementation of the Takaful Transition Strategic Plan and facilitate the industry's smooth transition towards achieving full Shariah compliance by 2027.

Takaful Sub-committee under Apex Islamic Finance Committee

With the objective of steering the transformation of conventional financial markets, institutions, and services towards an Islamic framework, the SECP has constituted an Apex Islamic Finance Committee to provide strategic guidance for the implementation of the Federal Shariat Court's judgment on Riba. Given the technical nature of the insurance business and the specialized expertise it requires, it is proposed that SECP may consider forming a dedicated sub-committee under the Apex Committee to oversee the transition of the insurance industry towards Takaful.

This takaful sub-committee may include representation from industry experts, Islamic finance scholars, relevant stakeholders, and regulatory authorities. Its mandate would include formulating a comprehensive transition plan for the insurance sector, addressing both operational and technical aspects of the conversion, including the development and conversion of long-term life insurance products in line with Shariah principles.

6. Plan of Action

S. No.	Action Points	Responsibility
1	Develop and implement an industry-wide transition plan to a Shariah-compliant insurance ecosystem.	SECP
2	Prepare and review of individual Takaful Adoption Plans at the company level, including operational and strategic transformation.	Insurance Companies/SECP
3	Issue comprehensive policy guidelines for complete transition of conventional insurance to Takaful.	SECP
4	Conversion of conventional insurance portfolios to Shariah-compliant Takaful products.	Insurance Companies
5	Formulate and implement conversion strategy for national-level insurance schemes (e.g., Sehat Sahulat).	SECP / Relevant Ministry
6	Align the regulatory framework with AAOIFI and IFSB international standards.	SECP
7	Apply IFRS 17 standards to Takaful contracts for consistent financial reporting.	SECP / Insurance Companies
8	Issue detailed guidelines on surplus distribution including methodology, frequency, and governance.	SECP
9	Review the minimum capital requirement for Window Takaful Operators	SECP
10	Expand Retakaful capacity within PRCL to meet domestic Takaful needs.	PRCL
11	Assess and build Retakaful capacity across all non-life insurers.	Non-life insurance Companies
12	Allowing Conventional Reinsurance for Takaful Risks on Dire Need Basis	Insurance Companies / SECP
13	Amend solvency framework to account for the unique risk-sharing nature of Takaful.	SECP
14	Launch a nationwide Takaful-specific awareness campaign	IAP / SECP / Industry
15	Develop and launch standard Takaful Products to improve accessibility and uniformity.	SECP / Industry
16	Ensure availability of diverse and innovative Takaful products across all lines of business.	Insurance Companies
17	Establish a Takaful Committee under IAP to coordinate industry-level Shariah and operational issues.	IAP
18	Facilitate licensing of new full-fledged Takaful operators	SECP
19	Facilitation in new life insurance product approvals	SECP
20	Window Takaful authorization by all insurers	Insurance Companies / SECP
21	Takaful-Specific Human Resource Development and Training Programs	SECP, PII, IFMP, Academia, Insurance Companies, AAOIFI, IFSB
22	Takaful-Commitee under Apex Islamic Finance Committee	SECP

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COMMISSION OF PAKISTAN

NIC Building, Jinnah Avenue, Blue Area, Islamabad.
www.secp.gov.pk