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AN EMPIRICAL STUDY OF TAKAFUL PARTICIPANT'S PERCEPTION OF THE DISTRIBUTION OF THE UNDERWRITING SURPLUS AND ITS IMPACT ON PARTICIPANTS' BEHAVIOUR

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Abstract

Takaful is Islamic alternative of conventional insurance which, is based ontabarru (donation) and agency or profit sharing between the participant and the company. The purpose of this study was to find out the perception of takaful participants about the sharing, and distribution of underwriting surplus in takaful companies in Saudi Arabia. The paper reports results on the perceptions of 420 participants of TOs in Saudi Arabia whether or not they want the company to share underwriting surplus with them. The paper also reflects and compares SAMA regulations with the regulations of the international takaful bodies in terms of distributing underwriting surplus among participants. The findings show a huge variation between participants and shareholders in terms of surplus and profit accumulations, i.e. shareholders profit increases against the interest and right of participants. In other words, if SAMA has followed the AAOIFI standards, takaful participants will be able to participate on the takaful fund with a small amount of contribution for a reasonable expected surplus return, which in away helps in reducing poverty in Saudi Arabia. Limited studies have been conducted to systematically document takaful participants' perceptions and preferences about underwriting surplus. This paper attempts to fill the gap.

Keywords: SAMA Directives, Takaful Operators, Takaful Participants, Underwriting Surplus, Participants' Perceptions

INTRODUCTION

Takaful is derived from the Arabic root word *"kafala",* a verb which means guarantee, bail, warrant or an act of securing one's need (Ali and Odierno, 2008). *Takaful* is also defined in Section 2 of the Malaysian Takaful Act 1984 as; “A scheme based on brotherhood, solidarity and mutual assistance which provides for mutual financial aid and assistance to the participants in case of need whereby the participants mutually agree to contribute for that purpose.”

Accounting Auditing Organization for Islamic Financial Institution (AAOIFI's), also defined Islamic insurance on (2004/2005) as per the Financial Accounting Standard No. 12, in Appendix E; “Islamic insurance is a system through which the participants donate part or all of their contributions which are used to pay claims for damages suffered by some of the participants. The company's role is restricted to managing the insurance operations and investing the insurance contributions.”

By 2007 AAOIFI defined Islamic insurance as in line with *Shariah* Standard 26 (2) 2007;“Islamic insurance is an agreement between persons who are exposed to risks to protect themselves against harm arising from risk by paying contributions on the basis of a “commitment to donate”. Following from that the insurance fund is established and it is treated as a separate legal entity which has independent financial liability. The fund will cover the compensation against harms that befall any of the participants due to the occurrence of the insured risks (perils) in accordance with the terms of the policy.”

It may be thought on first glance that *takaful* does not deviate from conventional insurance, since both types depend on the concept of pooling money from a group for the sake of helping the unfortunate of the same group in the events of encountering financial loss. However, unlike *takaful*, the spiritual mutual support is not a requisite of conventional insurance. Conventional insurance is based on the exchange whereby the insured pay a premium in exchange for protection in case of calamity exposure, with “no compensation” (the insurance value will be so intangible that its value cannot be appreciated) in a case of no loss. However, the *takaful* mechanism is based on the concepts of *tabarru* (donation) combined with the intention (*niah*) to participate in the pooling aid mechanisms. Al-Qaradawi, suggest that donation should be the basis of the contract, if insurance is to be *Shari’ah* compliant (Al-Qaradawi,2003). The spirit embodied in the concept of *tabarru* is that the participants are not thinking only of their own protection but they should also be thinking of helping other participants, without the concept of donation the contract will be that of buying and selling of insurance (Lewis, 2003). Hence, those who participate in the *takaful* mechanism will be less likely to encounter the feeling of receiving nothing if no claim occurs. They will be satisfied enough to help their colleague at the same pooling group in his loss. Another unique function for Islamic insurance is the strong relationship between *takaful* operator and participants, that *takaful* operator will go even beyond the provisions of "spiritual satisfaction needs", by providing a Nobel services which will be rewarded by God only.

While the conventional way of satisfying a customer is accomplished by fulfilling their material or worldly needs with benefits such as low prices, higher returns, faster delivery or even benefiting the deceased's family members after his death in the form of life insurance. However, it does not mean that customer satisfaction in terms of price, quality, delivery and precision are not important to the *takaful* operator; in fact, they are equally important in addition to the customer's spiritual needs satisfaction. So when Muslims buy Islamic insurance they can combine two benefits; (i)- They receive Islamic protection that complies with *Shari'ah* rules against financial loss, in the same way as conventional insurance, (ii) Customers can distance themselves from the possibility of sin (Based on three prohibition elements, Uncertainty of outcome *(gharar),* Gambling *(maisir),* and dealing with Interest *(riba)* which is frowned upon by the *shari'ah* law)incurred by purchasing conventional insurance in line with Shariah law. Although a believing Muslim is required to accept destiny, which may incorporate certain misfortunes, Islam encourages Muslims to take extra precaution to minimize potential misfortune, losses or injury arising from unfortunate events. Thus, having an insurance policy is not considered to be against the will of Allah, rather the will of Allah can be enhanced by holding an insurance policy to eliminate the unexpected risk that exists in day to day life. (Al-Zarqa, 1962; Attar, 1983; Moghaizel, 1991).

DOMINANT *TAKAFUL* MODEL

There are several *takaful* operational models that have been adopted by *takaful* operator companies worldwide namely *mudarabah*, *wakalah*, *waqf*, hybrids of *mudarabah* and *wakalah*, *ta'awuni* and non-profit fund. However the first two models are most dominant, that the *mudarabah* is widely used in Asia, while *wakalah* has become popular in the Middle East (Smith, 2007). Accordingly, this paper focused on the *wakalah* model as it is been used by the majority of the TOs in Saudi Arabia.

This paper will also highlight the operational scheme of the Saudi Cooperative insurance model as it been considered as a key feature of the *takaful* model. The *wakalah* model can be operated according to two main schemes; either General or Family. However, this paper focused on the *wakalah* model on its family form as the participated policyholders on this study were selected from a family *wakalah* model.

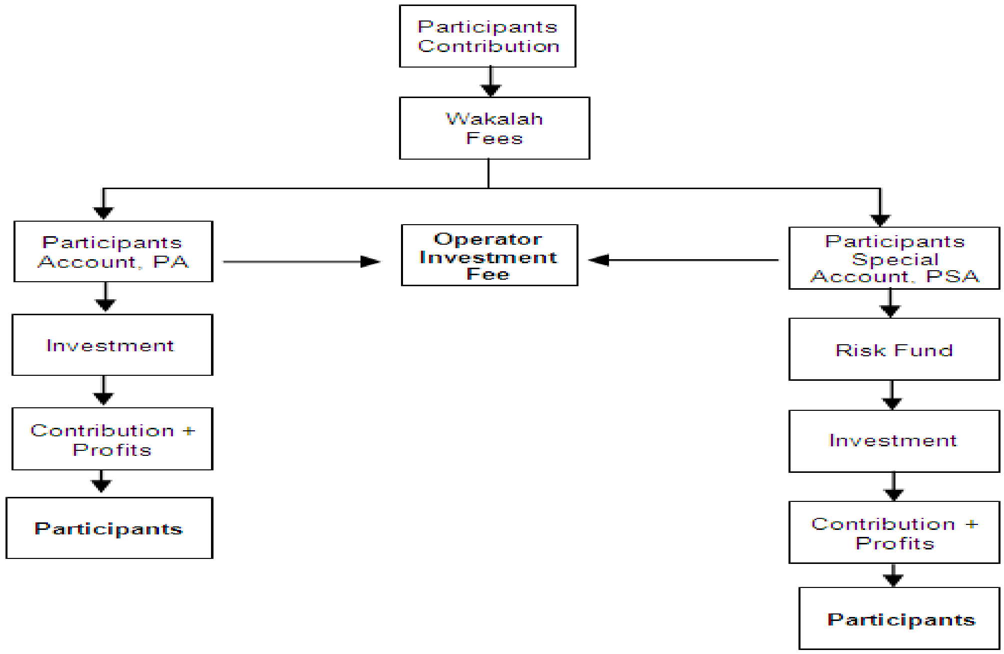
Basic *Wakalah* Model (Family *Takaful*)

There will be separate contracts in the *wakalah* model, of which one is used for underwriting and the other is used for investment activities of *takaful* funds. Although the *wakalah* model has widely been practiced by TOs in underwriting activities, it is rarely adopted for investment activities. In the *wakalah* model as shown in Figure 1, the participants (policyholders) place their contribution into a pool of donations (*tabarru*), hence the*wakalah* operator (agent), is entitled to a *wakalah* fee for their effort to manage the *takaful* fund regardless of the performance of the fund. It is an upfront fee which is calculated based on an agreed percentage of the total fund; nevertheless the TO cannot ask for an additional *wakalah* fee in the future if the calculated fee was underestimated (Tolefat, 2008). The *wakalah* fee should be approved by the *Sharia'h* Supervisory Board (SSB) (CCB Rulebook, 2005).

Thereby, most of the TOs will declare their *wakalah* fee at the beginning of the contract, but the loading will be calculated at the end of the year once the actual encountered expenses have been declared for an accurate fee calculation. Like the general *wakalah* model, the model used here for underwriting and investment activities as shown in Figure 1, can deviate according to the nature and sensitivity of the underwriting policy encountered (Tolefat, 2008). For example, if the policy is regarding (i) Risk protection from death, then the contributions split into two channels. The first contribution goes to the *wakil*(Agent), for their management effort and other fees related to the family policy if any, while the second contribution goes to the Participants' Special Account (PSA), in the form of donations (*tabarru*) to participate in the risk of death protection pooling, the donations of the participants varies in accordance to his age at the time of the contract (Hassan and Lewis, 2007). On the other hand, if the policy is written as (ii) Family *Takaful* savings policy, then the contributions split into three channels.

The first two channels follow the aforementioned policy. However, a small portion also goes to the PSA to cover mortality risk, while a substantial portion goes to the Participants' Account (PA) for the purpose of savings and investments. Furthermore, the PSA, and shareholders fund operates the same way as in the general basic *wakalah takaful* model. While the PA represents the savings policies, most of the investments here are accomplished on a long-term basis, thereby the TO deserves a management fee which is calculated as a percentage of the total invested assets and this fee represents their effort to manage such an investment fund. The TO as a result has four sources of income: (i)*wakalah* fee from underwriting activities, (ii) fund investments fee from PSA, (iii) fund investments fee from PA and (iv) incentive performance fee if it followed the operational procedures.

Figure 1: Basic *Wakalah* Model for Family *Takaful* Operational Flow-Chart



Source: IFSB (2009: 28)

SAUDI ARABIAN COOPERATIVE INSURANCE AS A *TAKAFUL* MODEL

SAMA requires all insurance companies to operate under a cooperative insurance business model, which is a key feature of the *takaful* model (E & Y, 2010). *Shari'ah* scholars have indicated that the Saudi cooperative model is similar to a *takaful* model (funds segregation and surplus distribution) (Abouzaid, 2007).

The cooperative insurance model works in the same way as the *takaful* model. The SAMA directives called the Implemented Regulations, Article 70, has identified the surplus distribution between the company and the participants. SAMA has indicated that 10% of the net surplus shall be distributed to the policyholders either directly or in the form of reduction in premiums for the next year. The remaining 90% of the net surplus shall be transferred to the shareholders' income statement. Shareholders' net income shall be transferred to the statement of shareholders' equity similar to the *takaful* model. Furthermore, 20% of the net shareholders' income shall be set aside as a statutory reserve until this reserve amounts to 100% of the paid capital (SAMA, 2005). Therefore, any deficit in the policyholders' fund is borne solely by the shareholders.

Despite SAMA regulations, which are directed towards cooperative insurance, only a number of cooperatives operate as sole TO (E & Y, 2010, 2011). Examples of these operators are (AlJazira, 2008; SAAB, 2009; &AlAhli, 2010). These TOs are using the *wakalah* model to operate their *takaful* scheme and they have appointed *Shari'ah* boards to supervise business operations, including investments and ensure compliance with Islamic law. However, these TOs are following the Saudi cooperative insurance laws, as SAMA did not issue specialized *takaful* laws and directives.

Surplus Distribution as per the International regulatory bodies

AAOIFI on its *Shariah* Standards (2010) defined surplus as excess of the total premium contributions paid by policyholders during the financial period over the total indemnities paid in respect of claims incurred during the period, net of reinsurance and after deducting expenses and changes in technical provisions (*i.e.* Contributions - Indemnities = Surplus). Accordingly, earning underwriting surplus considered as a common requirement for both policyholders and TOs so that the distribution of surplus will be an incentive for participants to enhance their loyalty towards the company. In practise, paying back part of the surplus makes the *takaful* participants responsible and aware not to make false or fraudulent claims that would lower the surplus rate. On the other hand, surplus means a great reward incentive for TOs, as many TOs are very keen to share the underwriting surplus with participants. TOs can argue that the recorded surplus at the end of the financial year is the sign of efficient management and prudent practices.

However, as a *takaful* contract is a combination of *tabarru*' and agency or profit sharing, the *takaful* fund is considered a *musharaka* (partnership) among participants. The relationship between the TO and participants' funds is based on either *wakala* contract to manage the underwriting activities, and/or a *mudarabah* to manage the underwriting or investment activities. Accordingly, the main difference between *takaful* operations and conventional insurance is the concept of underwriting surplus – conventional insurance underwriting surplus means profit for the insurance company, while underwriting surplus is not regarded as profit for *takaful* operators (Hassan, 2008).Therefore, TOs are not entitled to share the surplus of the fund with participants. TOs for the sake of the best benefits and with full consent of the participants use the surplus as reserves, reduction of the contribution, charitable donations and partial/full distribution of the surplus among the participants. AAOIFI *Shari'ah* standard No. 26 (5/5) of 2007, has stated that surplus can only be distributed back to the participants and cannot be taken by the TO; the distribution of surplus will be based on a percentage share of participant's donations.

Despite the fact that TOs are not allowed to share the surplus with participants, until recently, the *mudarabah* model adopted by Malaysian TOs refers to profit as the underwriting surplus plus investment returns. This arrangement marks a departure from the original *mudarabah* model, which will entitle the TO a ratio in the investment returns, without sharing in the underwriting surplus (Soualhi, 2008: 2). Later on, the modified *mudarabah* model justified the sharing of the underwriting surplus on the grounds that such an arrangement would allow TOs to withstand competition and avoid overpricing (Soualhi, 2008: 2).

On the other hand, AAOIFI in its *Shari'ah* Standards (2010) has indicated the following three approaches to allocate underwriting surplus justly among participants:

I. **Pro-rata mode:** Underwriting surplus must be allocated to all *takaful* participants in proportion to the contribution paid by the participants, without differentiating between claimable and non-claimable accounts, since they all contributed to the fund with a noble goal of brotherhood protection with no intention to achieve a surplus. Thus, the surplus must be equally distributed among them.

II. **Selective mode:** Underwriting surplus must only be allocated to those participants who have not made any claims for a given financial year. This mode tends to indemnify non-claimable accounts only and deprive claimable accounts so that they become more prudent in the future. This is meant to apply justice among *takaful par*ticipants as it is unfair to give claimable accounts part of the surplus since they have already received *takaful ben*efits.

III. **Offsetting mode:** Underwriting surplus must only be allocated to those participants where the amount of claims is less than the contribution paid. That is where the claims ratio is below 100%, then the surplus would be distributed after deducting the amounts of claims received in the given valuation period.

The above three approaches to allocate underwriting surplus should be clearly disclosed to participants as per AAOIFI No13, which requires disclosure of the method and the *Shari`ah* basis applied in allocating the underwriting surplus. Participants should also receive relevant, sufficient and reliable information in connection with their participation rights on a timely and regular basis (IAIS and OECD, 2009).

Surplus Distribution as per SAMA Regulations

SAMA has issued a number of laws and regulations that aimed to regulate and standardized the Saudi insurance industry. In August 2005, SAMA issued the Cooperative Insurance Companies Control Law, which contains 25 articles. The main headings for insurance companies operating laws include licensing procedures and conditions, the required capital, key personnel responsibilities, auditing and annual reports, the role of the Ministry of Commerce and the role of SAMA in dealing with insurance companies, *etc.* In the same year SAMA has issued the controlling law that contains 84 articles, which gives an extensive illustration of the previous control laws. SAMA has also issued a number of specific regulations that address certain issues in the Saudi insurance industry, with the aim of strengthening transparency and accountability and to enable SAMA to enforce better business practices in the Saudi insurance market.

Furthermore, SAMA on its directive called the "Implemented regulations" Article 70, mentioned that the surplus distribution shall be conducted as 10% of the net surplus distributed to the policyholders, the remaining 90% of the net surplus shall be transferred to the shareholders' income statement, and 20 % the net shareholders' income shall be set aside as a statutory reserve until this reserve amounts to 100% of the paid capital (SAMA, 2005).Accordingly, as the majority of the TOs in Saudi Arabia are using the *Wakalah* model to run the *takaful* scheme (AlJazira, 2008; SAAB, 2009; AlAhli, 2010) there exists contradiction between SAMA instructions and AAOIFI *Shari'ah* standard No. 26 (5/5) of 2007, as the TO in the *wakalah* operational mechanisms is considered an agent to run the underwriting and investments activities. The TO suppose not to share underwriting surplus with participants and they have only four sources of income only, (i) – *wakalah* fee from underwriting activities, (ii) - fund investments fee, (iii) - investments on the operator's own capital and (iv) - an incentive performance fee, *i.e.* "sharing in the net underwriting surplus of the *takaful* fund" (in case of modified *wakalah* model).

Furthermore, SAMA seems in favor of implementing the net underwriting surplus instead of the gross underwriting surplus (SAMA, 2005), which implies that the investment income is ploughed back into the *takaful* fund and the *takaful* company shares with the participant the surplus from the *takaful* fund (Ali and Odierno,2008; Asaria,2009). Following SAMA surplus distributions instructions will reduce both underwriting surplus and investment return for participants, while shareholders will get the ultimate benefits as per SAMA instructions. This fact was consolidated by the disclosed annual reports of some of the TOs in Saudi Arabia.

Table 1, shown a practical example from ALAhli *takaful* company, despite the fact that participants gross *takaful* contributions has been increased from SAR 115.85 million in 2009 to SAR 208.80 in 2010, with a growth rate of 80 % increase in revenues, with a net loss of only SAR 9.02 million in 2010, however participants fund surplus/deficits figures shown an amount of SAR 0.71 million, reflected a shortage in surplus distribution (AlAhli, 2010: 5).

Table 1. AlAhliParticipants' *Takaful* Operations

Description	2010	2009	2008	Variance ('09 vs '10)	
	SAR millions			SAR	%
Gross Takaful Contributions	208.80	115.86	6.4	92.94	80%
Net Retained Contributions	2.54	1.14	0.04	1.40	122%
Surplus / (Deficit) – from Takaful Operations	0.71	(0.36)	0.02	1.07	297%
Investments & Cash at Banks	238.57	69.77	4.35	168.80	242%
Technical Reserves	229.22	64.27	1.9	164.95	257%
Re-Takaful Balance Payable	4.13	3.62	0.19	0.51	14%

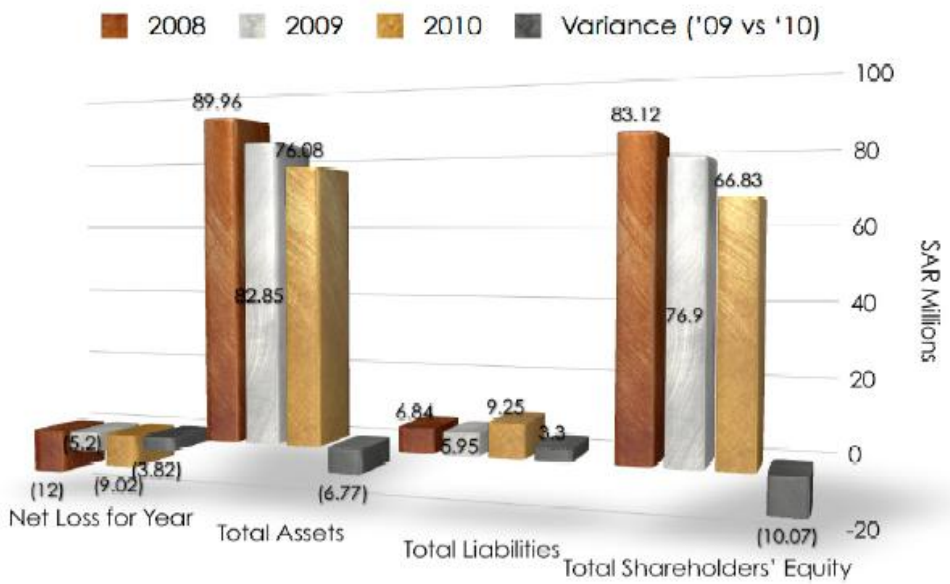
Source: AlAhli (2010)

At the opposite side AlAhli *takaful* company balance sheet as shown in Figure 2 reflected an increase in shareholders assets from SAR 152.82 million in 2009 to SAR 315.09 million in 2010 as a result of the significant increase in policyholders' investment (AlAhli, 2010: 6). The increase in shareholders assets and cash at Bank was due to the increase in investments as a result of increasing participants' value per contract of the new policies acquired and the resultant increase in the investable portion of contributions. While, the encountered increase loss in the *wakalah* operations was due to an increase in General and Administrative expenses (AlAhli, 2010).

The main reason that causes a loss in AlAhli*wakalah* operations is the administrative expenses besides the general *wakalah* model liabilities, which brings another discussion point that the Indirect expenses such as salaries and rents are paid by the operator if there is a surplus in the *takaful* fund that has been shared between the operator and the participants, otherwise it will be paid from the *takaful* fund (Lewis,2003). However, since the sharing percentage of surplus distributions between shareholders and participants has not been followed as per AAOIFI standards, then it will be quite unpractical to deduct general and administrative expenses from the *takaful* fund. Deducting general and administrative expenses from the *takaful* fund will creates a shortage in the participant's fund. The more of the *takaful* fund is used to cover expenses so the lower the underwriting surplus will be which will make it impossible for the participants to enjoy having an underwriting surplus in the future. Accordingly, it is recommended that the TOs to disclose the administration and expenses procedures to the participants to be aware of different kind of expenses that going to be deducted from the takaful fund. AAIFI on its standards No 13, stated that "disclosure of the basis applied by the company in calculating expenses affecting policyholders' funds such as pre-operating expenditures, reserves, costs of assets used in operations, claims and compensations, *etc".*

Furthermore, Figure2 below indicated that despite the fact that shareholders assets has been slightly decreased from 2008 to 2010, however there is a quite huge differences between shareholders encountered liabilities and their accumulated assets. Shareholders encountered liabilities are way less than their accumulated assets. Shareholders accumulated assets would not be positively increase without strong and regular contributions from the policyholders.

Figure 2: AlAhli Shareholders Operations



Source: AlAhli (2010)

On the other hand, SAMA unclear scenarios of distributing underwriting surplus among participants (pro-rata mode, selective mode, offsetting mode) has led TOs in Saudi Arabia to be confused on the proper way to distribute the surplus among participants, which causes a discretion of the Board of Directors to control participants generated surplus. This was clear in SAAB *takaful* (2009: 34) prospectus report, as they clarifies that, surplus distributions among participants will be based on BoDs approvals, despite that fact that *takaful* fund is purely belongs to the participants. SAAB *takaful* report stated that: "A portion of the surplus is distributed to the participants subject to approval of the Company's Board of Directors".

One of the main challenges faced in the *takaful* industry is shareholders and management discretions. Participants' undeserved rights might be due to management prioritizing interest towards shareholders as they are the main stewards of the *takaful* company. Prioritizing the interest of the shareholders might be due to the unclear structure of the *takaful* operational scheme. The *Takaful* operational scheme should follow the two-tier hybrid structure (mutual and proprietorship) as it has been identified by the prominent regulatory bodies such as AAOIFI and IFSB. However, almost all regulators, of which SAMA is one, treat the TOs as a proprietorship, as it can be easily regulated and supervised which requires an identified share capital and shareholders.

Shareholders can exert their power to use participants' fund underwriting surplus to enhance their financial position, as shareholders have the right to appoint the company BoD's. Accordingly, there are acceptable practices in the *takaful* contract, which allow shareholders' intrusion in participants' fund *e.g.* (i) Shareholders are allowed to invest the underwriting surplus with an express provision for an agreed consideration (profit-sharing or fee), with a complete consent for policyholders to either agree or reject the contract, (ii) Shareholders have the right to invest and share the return from investments, (iii) Shareholders have the right to share in the underwriting surplus with policyholders (Ali and Odierno, 2008). However, the three practices relationship between participants and shareholders should be clearly disclosed to the public as per AAOIFI No. 13 which states that disclosure of the bases governing the contractual relationship between policyholders and shareholders that touch on:

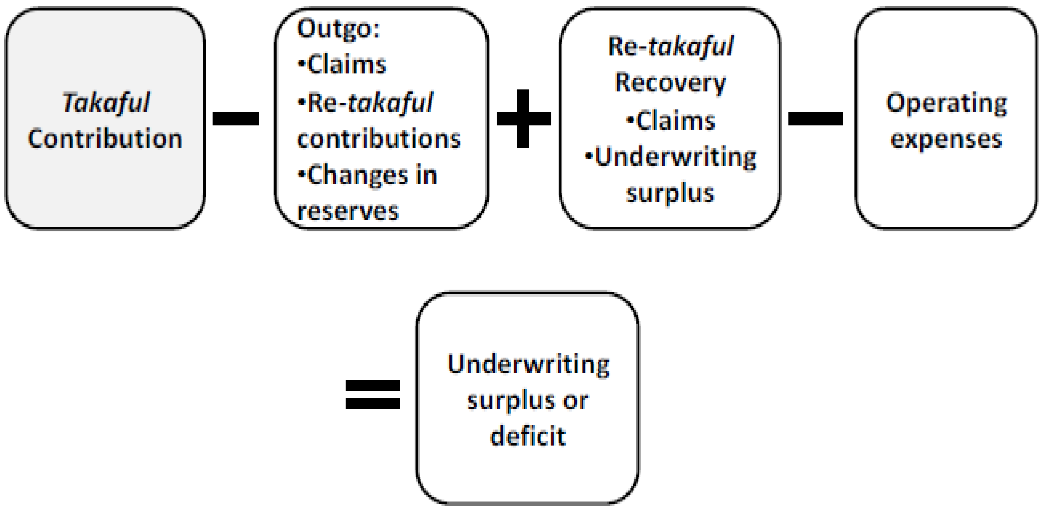
I. Management of insurance operations.
II. Investments of policyholders' funds.
III. Investments of shareholders' funds and the body that approve these bases.

The above discussions reflected a variation between SAMA cooperative insurance directives and the international insurance standards and policies in terms of distributing underwriting surplus. AAOIFI has been stipulated that surplus is purely belongs to the participants, while SAMA stipulated that the participants are allowed to share with only 10 % out of the underwriting surplus. Such a contradictions has made the TOs in Saudi Arabia to exerts some discretions on the *takaful* fund forgetting that the fund purely belongs to the participants. Accordingly, it's vital to hear participants' perceptions about their rights and preferences in receiving underwriting surplus.

METHODOLOGY

The study is primarily based on primary data collected from the takaful participants in Saudi Arabia. Convenience sampling method was used to administer the questionnaire. Figure 3, illustrates that the value of underwriting surplus can be positively or negatively affected by the participants contributions and/or by deductible items (claims, expenses, *re-takaful* arrangement fees, reserves management) from the *takaful* fund. Accordingly, participants' contributions represent an important factor in the analysis of the underwriting surplus. The AAOIFI *Shari'ah* Standards (2010) define *takaful* contribution as the amount of the contribution, which the participant donates, along with its related profits, for the benefit of the insurance scheme; this is the main source for the *takaful* operator to cover the future damages or losses of *takaful* participants.

Figure 3: Formation of Underwriting Surplus in the *Takaful* Operation



Source: Tobias (2009)

Since participants considered the main source of accumulating surplus in the *takaful* fund, it's quite vital to review participants' perceptions on their willingness to gain a surplus out of their contributions to the takaful fund. Therefore, questionnaire was chosen as the method by which the survey was completed. Questionnaires are a useful tool for investigating patterns and trends in data and are frequently used with success in management, marketing and consumer research (Easterby-Smith *et al,* 1991). The questionnaire measured adequate and desired expectations, perceptions of service quality as well as overall feelings, in terms of satisfaction and favourable, or otherwise, disposition. The questionnaire was originally prepared in English and then translated into Arabic by using theback-translation method with great assistant from an expert who is fluent in both languages. Accordingly, a total of 500 questionnaires were distributed, of which 420 completed questionnaires were received, where 120 questionnaires were rejected, leaving 300 completed and usable questionnaires.

Takaful participants in Saudi Arabia were identified to be the main research population for this study. The targeted populations were clients of all TOs in Jeddah, Saudi Arabia, since a number of large TOs have their headquarters in Jeddah. Accordingly, the researcher with the support of an 8 survey distributer team has managed to distribute the questionnaires among 9 branches of 3 TOs in Jeddah. The targeted participants are those with a family *takaful* policy. Thus policyholders are expected to have a long-term contract with the TOs and expected to have a periodic financial returns (Underwriting Surplus & Investment Return). The participants should not possess *takaful* contracts that belong to corporations, *i.e.* the *takaful* contracts are between the TOs and the participants directly.

EMPIRICAL RESULTS

The main reason behind this research is to reflect how participants are in a real need to reduce their poverty by finding other source of income to support providing a descent future for themselves and their family. Therefore, this section will reflect participants' demographics characteristics and how participants' characteristics indicate their real needs behind their contributions on the takaful fund. This section will also reflect participants' perceptions, knowledge and preferences about their rights in receiving surplus out of their contributions. Accordingly, participants' dominant demographic characteristics are:

- Gender: Male (96.3 %),
- Age: 31 - 40 Years (42.7 %),
- Education level: Bachelor Degree (59.3 %),
- Premium Paid: SAR 0 - 500 (33 %),
- Contract Duration: 0 - 5 Years (46 %),

From the above demographic characteristics it seems that the majority of the *takaful* participants in Saudi Arabia are male between the ages of 30 to 40 years old and paying a monthly premium between SAR 0 to 500, with contract durations that goes up to 5 years. Participants demographic characteristics indicates that the real needs for participants to be rewarded with a surplus out of their contributions as most of them are males which they repeatedly reminded of the responsibilities (as husband and father) awaiting them when they reach the adulthood stage, while girls anticipate marriage, motherhood and housekeeping. The majority of participants are also at an age stage where more responsibilities involving different financial commitments, such as paying back a mortgage loan, or paying children's school fees.

On the other hand, 230 (77 %) participants are using the *takaful* policy for the purpose of investments, while only (33 %) of the participants are contributing to the *takaful* fund for the purpose of risk and financial loss recovery. 256 (85 %) participants are using the *takaful* policy for future plan that can benefited their family. Surprisingly, 193 (64.3 %) participants clarifies that they are not using the *takaful* policy as a reason of *Shari'ah* compliance. Accordingly, it's highly believed that participants are contributing to the *takaful* fund as a reason of the expected financial return. Thus, SAMA should be aware of this fact, that *takaful* participants in Saudi Arabia are in a real need to be rewarded out of their contributions on the *takaful* fund.

Furthermore, 280 (93.3 %) participants replies with don't know to the conditions that made them eligible to receive underwriting surplus in association with claim situations, which reflects participants weak knowledge about the underwriting surplus conditions. Participants weak knowledge is a results of TO shortage in disclosing the required information about underwriting surplus conditions as 290 (97 %) replies with NO, that the TO didn't disclose the required information that allows them to receive underwriting surplus. Despite the fact that participants have a weak knowledge about underwriting surplus conditions because of TO weak disclosure, 224 (75 %) participants are willing to share underrating surplus with other participants regardless their claim conditions. Accordingly, it is recommended that the TOs to disclose enough information about different issues that deals with distributing underwriting surplus among participants, as (AAOIFI) No 13stated "disclosure of the method and *Sharia'h* basis applied in allocating the underwriting surplus".

CONCLUDING REMARKS

The current research has found a clear variation between SAMA cooperative insurance directives and the international insurance standards and policies in terms of distributing underwriting surplus. AAOIFI has stipulated that the surplus purely belongs to the participants, while SAMA stipulated that the participants are allowed to share with only 10 % out of the underwriting surplus. Such a contradictions has made the TOs in Saudi Arabia to exert some discretions on the *takaful* fund forgetting that the fund purely belongs to the participants as they are the ones who contributed to build that fund.

The current research also found that participants are contributing to the *takaful* fund as a reason of the expected financial return and there is no effect at all for religious motivation. Accordingly, SAMA should take into considerations this fact that participants are in a need of a financial reward out of their contribution to the *takaful* fund. Hence, it's highly recommended if SAMA follows AAOIFI directives in distributing surplus among participants for fair treatments of the participants.

Accordingly, it is highly recommended that SAMA issues directives to address the *takaful* insurance as SAMA did not issued a single directive that deals with *takaful* insurance. It's also recommended that SAMA assign a directive to make it obligatory for the TOs to structure a corporate governance framework. The framework should identify the operational scheme of the *wakalah* model in accordance with the international *takaful* organizations such as IFSB or AAOIFI. The framework should reflect the percentage of the distributed underwriting surplus among participants per AAOIFI *Shari'ah* standard that the *takaful* surplus purely belongs to participants and the surplus cannot be taken by the TOs. The framework should also identify the best approach to allocate underwriting surplus among participants as per an appropriate AAOIFI standard, *i.e.* pro-rata mode, selective mode, or offsetting mode. The framework should identify different types expenses and management fee that are going to be deducted from the participants fund, as this might causes a future deficits in the participants fund, consequently prevents participants rights in receiving underwriting surplus. The framework should disclosethe bases governing the contractual relationship between policyholders and shareholders. It's highly believed that if the TOs operating in Saudi Arabia follow the recommended framework; participants can contribute to the *takaful* fund with fewer amount of contributions with the expectations of getting a decent underwriting surplus, which in a way reduces poverty among Saudis.

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