



**BANK NEGARA MALAYSIA**  
CENTRAL BANK OF MALAYSIA

# **Financial Reporting for Takaful Operators**

Applicable to:

1. Licensed takaful operators
2. Financial holding companies

Issued on: 29 April 2022

BNM/RH/ED 033-5

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## **PART A OVERVIEW**

### **1. Introduction**

- 1.1 The Malaysian Financial Reporting Standards (MFRS) which serve as a basis for financial reporting in Malaysia have been fully converged with the International Financial Reporting Standards (IFRS) from 1 January 2012. Ongoing improvements in these standards have contributed to a greater alignment between financial reporting and prudential frameworks. Notwithstanding these positive developments, the increasingly more principle-based nature of financial reporting standards and the substantial degree of judgment required under the financial reporting standards can continue to result in divergent outcomes between the objectives of financial reporting and prudential regulation, which is primarily concerned with promoting institutional soundness and financial stability.
- 1.2 Recognising this potential dichotomy, Islamic financial institutions are required under the Islamic Financial Services Act 2013 (IFSA) to prepare their financial statements in accordance with the MFRS, subject to any standards as may be specified by the Bank to reflect specific modifications or exceptions to the MFRS. The Bank envisages that such modifications or exceptions will only become necessary in circumstances where alternative prudential measures would not be adequate to promote the financial resilience of Islamic financial institutions or address threats to financial stability. Where such modifications or exceptions are specified by the Bank, this must be accompanied by a disclosure of that fact by the Islamic financial institutions.

#### **Policy objective**

- 1.3 This policy document clarifies and sets minimum expectations for the application of the MFRS to an Islamic financial institution. It also aims to ensure adequate disclosures by an Islamic financial institution in the financial statements to improve comparability for users of financial statements and better facilitate the assessment of an Islamic financial institution's financial position, performance and Shariah compliance.

#### **Scope of policy**

- 1.4 This policy document sets out:
- (a) the specific requirements on the application of the MFRS;
  - (b) information to be disclosed in the financial statements;
  - (c) application requirements for approval of a dividend payment; and
  - (d) requirements on submission and publication of the financial statements.

### **2. Applicability**

- 2.1 This policy document is applicable to an Islamic financial institution as defined in paragraph 6.2.
- 2.2 Notwithstanding paragraph 2.1, the requirements under Part D of this policy document are not applicable to a professional retakaful operator.

### 3. Legal provision

- 3.1 The requirements and guidance in this policy document are specified pursuant to section 29, section 57(1), section 60, section 65(2) (d), section 73, section 74, section 75, section 127, section 155(2), and section 277 of the IFSA.

### 4. Effective date

- 4.1 This policy document comes into effect on **1 January 2023** and shall apply to financial statements for financial years beginning on or after 1 January 2023, with the exception of Part D of this policy document.
- 4.2 The requirements in Part D of this policy document come into effect on 29 April 2022.
- 4.3 An Islamic financial institution shall notify the Bank (one-time notification) of its intention to apply the fair value option under MFRS 9 *Financial Instruments* (MFRS 9) and the scope of the fair value application to financial instruments as approved by the board, at least one month before the option is first applied. The notification must be supplemented with relevant extracts of board minutes detailing the list of financial instruments approved by the board to apply the fair value option and the intended date of the application of the fair value option.

### 5. Level of application

- 5.1 An Islamic financial institution is required to comply with the requirements in this policy document in the preparation and publication of its separate financial statements and consolidated financial statements.

### 6. Interpretation

- 6.1 The terms and expressions used in this policy document shall have the same meanings assigned to them in the Financial Services Act 2013 (FSA) and the IFSA unless otherwise defined in this policy document.
- 6.2 For the purpose of this policy document:
- “**S**” denotes a standard, an obligation, a requirement, specification, direction, condition and any interpretative, supplemental and transitional provisions that must be complied with. Non-compliance may result in enforcement actions;
- “**G**” denotes guidance which may consist of such statements or information intended to promote common understanding and advice or recommendations that are encouraged to be adopted;

**“foreign policies”** means takaful certificates issued by a foreign professional retakaful operator in or from Malaysia but are not Malaysian takaful certificates;

**“foreign professional retakaful operator”** means a professional retakaful operator incorporated outside Malaysia;

**“takaful operator”** means a person licensed under section 10 of the IFSA to carry on takaful business and includes a licensed international takaful operator and a licensed retakaful operator;

**“Islamic banking institution”** means a licensed person which is:

- (a) a licensed Islamic bank except for licensed international Islamic bank; or
- (b) a licensed bank or licensed investment bank approved by the Bank to carry on Islamic banking business under section 15 of the FSA;

**“Islamic financial institution”** means a takaful operator and a financial holding company of the takaful operator approved by the Bank<sup>1</sup>;

**“separate financial statements”** and **“consolidated financial statements”** shall have the same meaning as set out in MFRS 127 *Separate Financial Statements* and MFRS 10 *Consolidated Financial Statements*.

## 7. Related legal instruments and policy documents

- 7.1 This policy document must be read together with other relevant legal instruments and policy documents that have been issued by the Bank, in particular–
- (a) *Takaful Operational Framework* issued on 26 June 2019; and
  - (b) *Risk-Based Capital Framework for Takaful Operators* issued on 17 December 2018.

## 8. Policy document superseded

- 8.1 The policy document on *Financial Reporting for Takaful Operators* issued on 2 February 2018 is superseded.

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<sup>1</sup> Pursuant to section 124 of the IFSA.

## PART B REGULATORY REQUIREMENTS

### 9. General requirements

- S** 9.1 Pursuant to section 74 of the IFSA, an Islamic financial institution shall prepare its financial statements in accordance with the MFRS to the extent that the standards are consistent with Shariah principles<sup>2</sup> and subject to the requirements specified in paragraph 10 and shall disclose a statement to that effect in the financial statements.
- S** 9.2 An Islamic financial institution shall comply with the rulings of the Shariah Advisory Council of Bank Negara Malaysia (SAC)<sup>3</sup> on the applicability of the following accounting principles adopted in the MFRS as being consistent with the broader view of Shariah principles:
- (a) accrual basis, where the effect of a transaction and other events is recognised when it occurs (and not when cash or its equivalent is received or paid) and is recorded in the accounting records and reported in the financial statements of the periods to which it relates;
  - (b) “substance over form”, where the “form” and “substance” of the transaction must be consistent and shall not contradict one another. In the event of inconsistency between “substance” and “form”, the Shariah places greater importance on “substance” rather than “form”<sup>4</sup>;
  - (c) probability, where the degree of uncertainty that the future economic benefits associated with the transaction will flow to or from the Islamic financial institution is considered in reference to the recognition criteria;
  - (d) time value of money (“TVM”), where a transaction involves time deferment, the asset (liability) is carried at the present discounted value of the future net cash inflows (outflows) that the transaction is expected to generate in the normal course of business. The application of TVM is permissible only in determining the selling price for exchange contracts that involve deferred payment and is strictly prohibited in debt-based transactions (*qard*) in general; and
  - (e) notwithstanding the prohibition on the application of TVM to *qard* in subparagraph (d), specifically for takaful, TVM may be applied in the measurement of a *qard* transaction between shareholders’ fund and takaful fund pursuant to section 95 of the IFSA in meeting the MFRS 17 *Insurance Contracts* and the MFRS 9 *Financial Instruments*, subject to the following:

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<sup>2</sup> Refer to *Statement of Principles (SOP) i-1: Financial Reporting from Islamic Perspective* issued by MASB. Paragraph 6 of *SOP i-1* provides that “Shariah compliant transactions and events shall be accounted for in accordance with MASB approved accounting standards, unless there is a Shariah prohibition”. In line with MASB’s consultative approach, an Islamic financial institution is to refer to MASB, when there are divergent practices regarding the accounting for a particular Shariah compliant transaction or event, or when there is doubt about the appropriate accounting treatment and the Islamic financial institution believes it is important that a standard treatment be established.

<sup>3</sup> Rulings made at the 16<sup>th</sup> SAC meeting (11 November 2000), 57<sup>th</sup> SAC meeting (30 March 2006), 71<sup>st</sup> SAC meeting (26-27 October 2007) and 213<sup>th</sup> SAC meeting (27 April 2021).

<sup>4</sup> For example, in a sell and buyback agreement (SBBA), due to the substance of the transaction being financing rather than a sale transaction, the overall effect of all the contracts involved in the transaction will be recorded as financing under the MFRS. The financial assets sold under the SBBA will not be derecognised from the books of the seller.

- (i) the total repayment of the *qard* amount must not exceed the total/actual *qard* amount from the shareholders' fund; and
  - (ii) the Islamic financial institution providing a comprehensive disclosure in the explanatory notes to the financial statements in line with paragraph 11.2.
- S** 9.3 The board is responsible for ensuring that the financial statements are drawn up so as to give a true and fair view of the state of affairs and of the results of the business of the Islamic financial institution. This is consistent with the fiduciary and statutory duties placed on the board as persons responsible for managing the affairs of the Islamic financial institution. Hence, the board shall be satisfied that a sound financial reporting structure is in place to ensure the integrity and credibility of the financial statements.
- S** 9.4 For financial instruments that are measured at fair value, an Islamic financial institution shall ensure that sound risk management and control processes<sup>5</sup> around their measurement<sup>6</sup> are in place.

## **10. Specific requirements on the application of the MFRS**

- S** 10.1 The financial statements and financial reports referred to under Part C and Part D of this policy document shall be presented in Malaysian ringgit (RM).
- S** 10.2 For the purpose of disclosures of non-compliance with externally imposed capital requirements, the relevant capital adequacy requirements refer to the supervisory target capital level as set out in the *Risk-Based Capital Framework for Takaful Operators Policy Document* issued on 17 December 2018.
- S** 10.3 A takaful operator that is a member institution of Perbadanan Insurans Deposit Malaysia (PIDM) shall also comply with the disclosure requirements specified by PIDM.
- S** 10.4 An Islamic financial institution shall not account for the investments in associates and joint ventures using the equity method described in MFRS 128 *Investments in Associates and Joint Ventures* in the preparation of its separate financial statements.
- S** 10.5 A takaful operator in the preparation of its separate financial statements shall apply the MFRS 17 *Insurance Contracts* to account for the takaful business managed under the takaful fund and at the consolidated takaful entity level. In doing so, the takaful operator shall present the assets and liabilities of the takaful fund<sup>7</sup> separately from the assets and liabilities of the takaful operator.

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<sup>5</sup> In line with the expectations set forth in the *Supervisory Guidance for Assessing Banks' Financial Instrument Fair Value Practices*, Basel Committee on Banking Supervision, April 2009 and *Supervisory Guidance on the Use of the Fair Value Option for Financial Instruments by Banks*, Basel Committee on Banking Supervision, June 2006.

<sup>6</sup> Refer to MFRS 13 *Fair Value Measurement*.

<sup>7</sup> Refers to family and general funds, as defined under *Takaful Operational Framework*.

## 11. Specific requirements on *qard*

- S** 11.1 *Qard* payable by the takaful fund shall be measured as part of the fulfilment cash flows in the calculation of takaful contract liabilities in accordance with the requirements under MFRS 17<sup>8</sup>.
- S** 11.2 In applying the measurement as required under paragraph 11.1, a takaful operator shall disclose the following information in the explanatory notes of the audited annual financial statements:
- the requirement for the takaful operator to provide *qard* to the takaful fund from its shareholders' fund pursuant to section 95 of the IFSA in the event a deficit occurs in the takaful fund;
  - the nature of the *qard*, the total/actual *qard* amount that has been provided to the takaful fund and the expected repayment period for the *qard* upon the availability of surplus in the takaful fund; and
  - explanation on the accounting measurement in respect of the application of TVM to determine the present value and future value of *qard* and the impact to the total/actual *qard* amount, including any fair value adjustment. The explanation shall also include the "rights of shareholders' fund to receive the total/actual *qard* amount" and the "obligation of takaful fund to repay the total/actual *qard* amount", of which the total/actual *qard* amount shall remain unchanged throughout the *qard* repayment period.

## 12. Investment properties

- S** 12.1 A takaful operator shall ensure that the amount of surplus arising from fair value gains on investment properties of the takaful fund which may be distributed to takaful participants shall be limited to the lower of 30% of the aggregate fair value gains (net of fair value losses) or 10% of the aggregate fair value of the investment properties.
- S** 12.2 A takaful operator shall maintain relevant information supporting the valuations for review as and when required by the Bank.
- S** 12.3 A takaful operator shall ensure that an independent professional valuer is appointed to validate material fair value changes or revaluations at any time as and when the Bank may require, and the cost of such validation shall be borne by the shareholders' fund.

## 13. Minimum disclosure requirements

- G** 13.1 The requirements under the following paragraphs refer specifically to disclosures which form part of the *financial statements* and do not deal with other disclosures provided by an Islamic financial institution as part of the Annual Report (e.g. Director's Report, Statement on Corporate Governance)

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<sup>8</sup> Takaful operator may refer to MASB's *Issue Bulletin 3 on Reporting Qard in the Takaful Fund's column within Takaful Entity's Financial Statements* issued and published on 20 August 2021 in its website.

- S** 13.2 An Islamic financial institution shall make disclosures in the financial statements in accordance with the requirements of the MFRS, and include information specified under paragraphs 13.4 to 13.9 of this policy document.
- S** 13.3 An Islamic financial institution shall comply with the following key principles on disclosure of information:
- (a) information shall be timely and up-to-date to ensure the relevance of the information being disclosed;
  - (b) the scope and content of information disclosed, and the level of disaggregation and detail shall be sufficient to provide comprehensive, meaningful<sup>9</sup> and relevant information to the users;
  - (c) adequate disclosures shall be provided on areas of uncertainty, in particular information on key estimates and if sensitivity analysis is used, a discussion on the assumptions and the probabilities of the occurrence of various scenarios; and
  - (d) disclosures shall allow comparisons over time and between takaful operators<sup>10</sup>.
- S** 13.4 A takaful operator shall present the financial statements<sup>11</sup> according to a columnar presentation format. At minimum, two standalone columns on the takaful fund and the consolidated takaful entity shall be presented in the financial statements.
- S** 13.5 In the event where a takaful operator opts to present an additional standalone shareholders' fund column in its financial statements, the takaful operator shall ensure that all items presented under the shareholders' fund column are in full compliance with relevant MFRS requirements.
- S** 13.6 For placements of funds in an investment account with an Islamic banking institution, an Islamic financial institution shall–
- (a) present the placement, as a separate line item in the statement of financial position, as either “investment account placement” or “investment account placement – asset description”; and
  - (b) disclose in the explanatory notes the nature of the underlying assets for the investment.
- S** 13.7 An Islamic financial institution shall disclose intercompany charges with a breakdown by type of services received and geographical distribution.

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<sup>9</sup> For example, given the heterogeneity of users of financial reporting, background information on the wider economic environment takaful operators operate in is necessary to provide sufficient information to understand the context for specific disclosures. Information should also be useful to support informed decision-making by users.

<sup>10</sup> For example, users shall be informed of the accounting policies adopted in the preparation of the financial statements including any changes in those policies and the effects of such changes. Users need to be able to identify differences between the accounting policies for like transactions and other events used by the same entity from period to period and by different entities. Compliance with MFRS, including the disclosure of the accounting policies used by the entity, helps to achieve comparability.

<sup>11</sup> Takaful operator may refer to MASB's Issue Bulletin 2 on *Columnar Presentation on Takaful Funds in Takaful Entity Financial Statements* issued and published on 2 September 2020 in its website.

- S 13.8** An Islamic financial institution shall ensure that the explanatory notes to be disclosed in the audited annual financial statements include the following information:
- (a) a description on the roles of the takaful operator in relation to its takaful participants based on the underlying Shariah contract (e.g. as a takaful fund manager in a *wakalah* contract and/or investment manager in a *mudarabah* contract);
  - (b) any forms of remuneration paid to the takaful operator for the management of the takaful fund (e.g. upfront *wakalah* fees, performance-based remuneration, profit sharing and compensation for direct costs);
  - (c) the amount of surplus distribution, if any, to both takaful participants and shareholders' fund;
  - (d) any other forms of financial support received by the takaful fund from the shareholders' fund pursuant to section 95 of the IFSA;
  - (e) any *hibah* provided by the takaful operator from its shareholders' fund to its takaful participants as supplementary to the takaful benefits;
  - (f) the required disclosures on *qard* in paragraph 11.2;
  - (g) takaful contract liabilities;
  - (h) reinsurance/retakaful assets;
  - (i) other receivables;
  - (j) total capital available showing separately Tier 1 Capital and Tier 2 Capital<sup>12</sup>;
  - (k) chief executive officer ("CEO"), Directors' and Shariah Committee members' remuneration with a breakdown of types of remunerations (e.g. salary, fees, bonus, benefits-in-kind, retirement benefits), disclosed separately for the CEO and each individual director, distinguishing between executive and non-executive directors, and Shariah Committee members;
  - (l) commitments and contingencies with a breakdown by types and amount distinguishing between contingent liabilities and commitments;
  - (m) amount and nature of earnings (expenditure) from sources or by means which are not permitted by Shariah and how takaful operator intends to dispose of the assets generated by prohibited earnings or acquired through prohibited expenditure; and
  - (n) amount of zakat payable and method of calculating zakat as approved by the takaful operator's Shariah Committee.
- S 13.9** An Islamic financial institution shall ensure that the explanatory notes to be disclosed in the interim financial report of an Islamic financial institution include the following information:
- (a) takaful contract liabilities;
  - (b) reinsurance/retakaful assets; and
  - (c) total capital available.

The breakdown for the above explanatory notes shall be consistent with that specified for audited annual financial statements (refer to paragraph 13.8). In addition, the takaful operator shall disclose items that are material to the understanding of the interim financial report in accordance with MFRS 134 *Interim Financial Reporting*.

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<sup>12</sup> The breakdown shall be consistent with that specified in the policy document on Risk-Based Capital Framework for Takaful Operators issued on 17 December 2018.

**PART C REGULATORY PROCESS AND SUBMISSION REQUIREMENTS****14. Declaration and payment of dividends**

- S** 14.1 Pursuant to section 60(1) of the IFSA, an Islamic financial institution is required to obtain the Bank's written approval prior to declaring or paying any dividend on its shares. For the avoidance of doubt, shares refer to both the ordinary shares and preference shares.
- S** 14.2 Unless otherwise informed by the Bank in writing, approval pursuant to section 60(1) of the IFSA is given to an Islamic financial institution to declare or pay any dividend on its preference shares where the dividend is non-discretionary<sup>13</sup> and non-cumulative<sup>14</sup>. For the avoidance of doubt, where the Bank has, prior to the effective date of this policy document imposed a requirement on an Islamic financial institution to obtain the Bank's written approval prior to declaring or paying any dividend on its preference shares, such approval requirement shall continue to apply and the requirements set out in paragraph 14.4 shall be observed by an Islamic financial institution.
- S** 14.3 Where an application has been made under paragraph 14.1, an Islamic financial institution shall not-
- (a) publish in print and/or electronic form<sup>15</sup>;
  - (b) lay the audited annual financial statements at its general meeting; and
  - (c) in the case of a listed Islamic financial institution, submit to the stock exchange,
- the interim financial report or audited annual financial statements, as the case may be, unless the proposed dividend has been approved by the Bank under section 60(1) of the IFSA.
- S** 14.4 An application for approval made under paragraph 14.1 by an Islamic financial institution must be supplemented with the following:
- (a) where an interim dividend is proposed,
    - (i) its interim financial report, with a review by the auditor of the profit after tax for the period<sup>16</sup>. The explanatory notes to the interim financial report shall be consistent with that specified for audited annual financial statements (refer to paragraph 13.8);
    - (ii) the interim financial report of its principal subsidiaries<sup>17,18</sup>, as applicable;
    - (iii) the limited review report by its auditor;
    - (iv) a written confirmation by the officer primarily responsible for the financial management of the Islamic financial institution that its interim

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<sup>13</sup> The proposed dividend payment is not at the full discretion of the takaful operator.

<sup>14</sup> Any waived dividend must not be made up by the takaful operator at a later date.

<sup>15</sup> For example, newspaper, press release and website.

<sup>16</sup> In accordance with the standards on review engagements issued by the Malaysian Institute of Accountants.

<sup>17</sup> Subsidiaries which are major contributors to the group's profit revenue, assets or profit/loss.

<sup>18</sup> For the avoidance of doubt, the interim financial reports of the principal subsidiaries need not be subject to review by the auditor.

- financial report has been prepared in accordance with the MFRS subject to requirements specified by the Bank in paragraph 10 of this policy document; and
- (v) in the case of a takaful operator, the calculation of the Capital Adequacy Ratio showing the positions separately before and after the proposed payment of dividends;
- (b) where a final dividend is proposed,
- (i) the information specified in paragraph 15.1; and
  - (ii) in the case of a takaful operator-
    - (aa) the calculation of the Capital Adequacy Ratio showing the positions separately before and after the proposed payment of dividends; and
    - (bb) its audited statistical returns<sup>19</sup> reported under the Takaful Operators Statistical System and risk-based capital reporting forms reported under *Risk-Based Capital Framework for Takaful Operators* issued on 17 December 2018.

## 15. Annual financial statements

- S** 15.1 Within three months after the close of each financial year and before the laying of the financial statements at the general meeting, an Islamic financial institution shall submit to Jabatan Penyeliaan Insurans dan Takaful of Bank Negara Malaysia, the following:
- (a) its audited annual financial statements;
  - (b) the audited annual financial statements of its principal subsidiaries, where relevant;
  - (c) its Auditor's Report<sup>20</sup>, including a report on the key accounting and auditing matters tabled to the board audit committee;
  - (d) the analysis of performance by key business segments;
  - (e) a written confirmation by the officer primarily responsible for the financial management of the takaful operator that its audited annual financial statements have been prepared in accordance with the MFRS subject to requirements specified by the Bank in paragraph 10 of this policy document;
  - (f) its Shariah Committee's Report; and
  - (g) the tentative date of the publication of its audited annual financial statements on the website.
- S** 15.2 For the purpose of paragraph 15.1(b), where the audited annual financial statements are in a language other than the national language or English, the copy submitted shall be translated into English.
- S** 15.3 For the avoidance of doubt, in the case of a foreign professional retakaful operator, the information to be submitted under paragraph 15.1 shall relate to its Malaysian takaful certificates and foreign policies of its office in Malaysia.

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<sup>19</sup> This refers to Revenue Account, Income Statement and Balance Sheet.

<sup>20</sup> This refers to the detailed report prepared by the auditor on the audit of a takaful operator's annual financial statements.

- S** 15.4 Where the audited annual financial statements of a foreign professional retakaful are not made available on the website, a foreign professional retakaful operator shall submit to the Bank a copy of its audited annual financial statements within 30 calendar days after the laying of the financial statements at its general meeting in the country in which it is incorporated or established. Where the audited annual financial statements are in a language other than the national language or English, the copy submitted shall be translated into English.

## **PART D PUBLICATION REQUIREMENTS**

### **16. Annual financial statements**

- S** 16.1 A takaful operator shall make available the full set of the audited annual financial statements on its website<sup>21</sup> no earlier than five working days after the date of submission of the information specified in paragraph 15.1 to the Bank but not later than 14 calendar days after its annual general meeting.
- S** 16.2 A financial holding company shall make available the full sets of the audited annual financial statements on its website no earlier than five working days after the date of submission of the information specified in paragraph 15.1 to the Bank but not later than 14 calendar days after its annual general meeting.
- S** 16.3 A takaful operator shall make available a copy<sup>22</sup> of the audited annual financial statements at every branch of the takaful operator in Malaysia.

### **17. Interim financial report**

- S** 17.1 Where an application has not been made under paragraph 14.1, an Islamic financial institution shall make available on its website the interim financial report prepared on a half-yearly basis no later than eight weeks after the close of the interim period.
- S** 17.2 Where an application has been made under paragraph 14.1 and approval from the Bank has been obtained under section 60(1) of the IFSA, an Islamic financial institution shall make available on its website, the interim financial report prepared on a half-yearly basis, no later than eight weeks after the close of the interim period. In the case where the application has yet to be approved by the Bank by the end of the eighth week after the close of the interim period, an Islamic financial institution shall disclose on its website the interim financial report no later than five working days after the approval from the Bank has been obtained.

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<sup>21</sup> Or the corporate website of a takaful operator or a financial holding company.

<sup>22</sup> May be in the form of physical or electronic copy.