INSTITUTE OF
CERTIFIED PUBLIC ACCOUNTANTS
OF UGANDA

FINANCIAL REPORTING GUIDANCE FOR TAKAFUL OPERATORS

AUGUST 2022

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About ICPAU

The Institute of Certified Public Accountants of Uganda (ICPAU) was established in 1992 by an Act of Parliament now the Accountants Act, 2013. The functions of the Institute, as prescribed by the Act, are:

i. To regulate and maintain the standard of accountancy in Uganda.

ii. To prescribe and regulate the conduct of accountants and practicing accountants in Uganda.

Vision

To be a world-class professional accountancy institute.

Mission

To develop, promote and regulate the accountancy profession in Uganda and beyond.

Core Values

Professional Excellence

Accountability

Integrity

Innovation

International Affiliations

The Institute is a member of the International Federation of Accountants (IFAC), the Pan African Federation of Accountants (PAFA), and the Association of Education Assessment in Africa (AEAA).

Purpose of the Guidance

This Guidance has been designed to assist accountants in the application of IFRS to takaful transactions or events without violating Shariah principles. The Guidance clarifies and sets minimum expectations in the application of the IFRS to takaful transactions. It also aims to ensure adequate financial statement disclosures by a Takaful operator as a way of promoting comparability among financial statements and to better facilitate the assessment of the takaful operator's financial position, performance, and Shariah compliance.

The Guidance gives specific requirements on the application of IFRS Standards to takaful transactions as well as minimum disclosure requirements to achieve fair presentation of those transactions by IFRS compliant financial statements.

Applicability

This Guidance applies to a Takaful Operator as defined in paragraph 2.0. We have appended illustrative guidance on the classification of Shariah contracts as well as an illustration of disclosure requirements by Shariah contracts.

A Takaful operator is required to comply with the requirements in this guidance in the preparation and publication of its separate financial statements and consolidated financial statements.

This Guidance is a living document that shall be regularly reviewed and updated to reflect changes in the takaful industry as well as changes in IFRS requirements.

Disclaimer

The information within this Guidance is strictly limited to that which falls within the mandate of ICPAU as stipulated in the Accountants Act, 2013 or any other laws of Uganda prevailing at the time. This Guidance is persuasive rather than prescriptive. The Guidance is not intended to be comprehensive or to deal with all situations that might be encountered. Rather, it is supplementary to and not a substitute for the International Financial Reporting Standards (IFRS) and any other Guidelines that may be developed over time by ICPAU, which should be regarded as the primary source of guidance for accountants. The accounting policies for example; are rather demonstrative and not exhaustive, accountants are thus expected to make full disclosures of accounting policies as applied. Accountants are further encouraged to apply professional judgment in complying with the requirements of IFRS.

1.0 OVERVIEW OF ISLAMIC INSURANCE

Islamic banking, Islamic financing, Islamic Insurance, and Islamic capital market are essentially creatures of Islamic economics. They emerged as a result of Al-Tajdid Al-Islami (Islamic revivalism) i.e., the "cleansing of Islamic practices of all un-Godly elements" in an effort to return Islam to its original pure form (Mawdudi, 1999).[1]

Like Islamic banking, the Islamic insurance system (Takaful) is an essential creature of the same economic system – the Islamic economics formulated and established as a result of the Islamic revivalism efforts in many Muslim and non-Muslim countries. It has been decreed in some countries that conventional insurance is forbidden in Islam. This is premised on the fact that there exist elements of *excessive* uncertainty[2], gambling, and usury that are contradictory to the spirit of Islamic law (Shariah). As such, in contrast to conventional insurance, the operational setup of Takaful is formulated to be free from these three elements. The Takaful system also employs several Islamic elements such as mutual help, the willingness of participants to relinquish their individual rights over the contributions paid, for collective benefits, and either a profit-sharing relationship or a principal-agent relationship between the participants and operator of the fund[3].

Conventional insurance involves a customer (the policyholder) paying periodically a premium to an insurance company (the insurer) to transfer the risk arising from unfortunate events to the insurer. Such business structure is prohibited in Islam because it involves three prohibited elements of interest - as the premium paid to and the compensation paid by the insurance companies are not equal; excessive uncertainty - whereby the subject matter of the contract is uncertain until the unfortunate event has taken place; and gambling – in that the occurrence of the unfortunate event is subject to chance. Therefore, conventional insurance is riba-based, as it is a contract of exchange of money in the future subject to the occurrence of the risks and at a different value.

Islamic insurance (Takaful) on the other hand is built based on the concept of mutual responsibility and mutual protection from losses whereby participants' mutual intention

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[1] Mawdudi, A. A. 1999. A Short History of the Revivalist Movement in Islam. Translated by Al-Ash'ari, Petaling Jaya, Malaysia: The Other Press, 1999 [1963]), 24.

[2] Note that there will be a reasonable degree of uncertainty in any transaction such as the amount and timing of profits. Islamic law only prohibits excessive uncertainty and this is what is termed as Gharar. Uncertainty would be excessive in a transaction if one or both parties to the transaction are ignorant of an essential element of the transaction. For example, (i) where deliverability of the subject matter of the sale is excessively uncertain (like the sale of fish in the sea); (ii) a future sale where the consideration will also be determined in the future (like futures and options in financial markets).

[3] Shahul Hameed bin Mohamed Ibrahim (2005) A Review Of Takaful Accounting Regulations And Practices In Malaysia

is to protect each other – i.e., to indemnify any of the participants who is inflicted with a specific risk from an unfortunate event.

The risk-sharing feature of takaful contracts has caused numerous debates on whether they meet the IFRS definition of an insurance contract and whether they can be accounted for using IFRS 4 or IFRS 17. Appendix 1 of IFRS 17 defines an insurance contract as a contract under which one party (the issuer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder. IFRS 17:B16 states that an entity can accept significant insurance risk from the policyholder only if the entity is separate from the policyholder. In the case of a mutual entity, the mutual entity accepts risk from each policyholder and pools that risk. Although policyholders bear that pooled risk collectively because they hold the residual interest in the entity, the mutual entity is a separate entity that has accepted the risk.

The Asian-Oceanian Standard-Setters Group (AOSSG), 2010[4] concluded that takaful contracts meet the definition of an insurance contract since the risk-sharing feature in takaful contracts is similar to mutual insurance, which is within the scope of IFRS 4 and IFRS 17. ICPAU subscribes to this school of thought.

For purposes of financial reporting:

a. A takaful fund shall apply IFRS 17 on the basis that the takaful fund is the party that accepts insurance risk from takaful participants and compensates them if they incur an insured loss consistent with the definition of an insurance contract under IFRS 17.
b. The takaful operator is a service provider to the takaful fund and if it were to prepare financial statements on a standalone basis, it shall not apply IFRS 17. Instead, the takaful operator shall apply IFRS 15 to account for the fees it charges to manage and administer the takaful fund.
c. The takaful company as a whole (combining the takaful fund and the takaful operator) shall apply IFRS 17. This is because, upon inclusion of all the activities conducted by the takaful operator associated with managing and administering the takaful fund, there would ordinarily be a Contractual Service Margin (CSM) since the takaful company aims to profit from participants in conducting its takaful business.

1.1 ETHICS AND ISLAMIC FINANCE

Islamic law rules that if one advances a loan, one is entitled only to the principal amount loaned—nothing more. If one wishes to secure a gain, one should enter into a

[4] Financial Reporting Issues relating to Islamic Finance issued in 2010

partnership and/or become a shareholder. In addition to usury (interest), Islamic law also prohibits excessive uncertainty, and gambling. These prohibitions, however, are not peculiar to the religion of Islam. History suggests that a number of examples of such prohibitions can be found in the early Greek, Roman and Rabbinical thought. Overtime, as industrial, financial and commercial power become concentrated in the hands of giant Western firms, a global dominance of capitalist imperialism followed. This created widespread acceptance of the prohibited practices which then dominated Western law and ethics for over a millennium[5]. Unfortunately, capitalism has caused a terrifying scenario of making the rich richer and the poor poorer due to interest charges.

The Islamic financial system establishes a duty to observe high ethical standards and a corresponding requirement to take into account the wider impact of the transactions financed. This view of ethical conduct, and of wider accountability, as envisioned by Islamic finance thus stands somewhat removed from the notion of a firm that needs only to maximize profits for its shareholders without regard to the social or other consequences of its actions[6].

The Islamic financial system is based on the avoidance of all forms of financial exploitation and on having as its principal object the combined purpose of the creation of wealth and the alleviation of poverty. "The ethical principles on which Islamic finance is based may bring banks closer to their clients and to the true spirit which should mark every financial service".[7]

[5] The Riba Conundrum: The Ethical Appeal of Islamic Banking, (Nico P Swartz, Odirile Otto Itumeleng, Wankie, Anisha Jeelabdeen & R. Kumar, 2013)

[6] Ethics in Islamic Finance: Embracing Duties and Consequences in the Post-Crisis Environment, 2015 https://www.ifac.org/knowledge-gateway/building-trust-ethics/discussion/ethics-islamic-finance-embracing-duties-and-consequences-post-crisis-environment

[7] Pope Benedict XVI (the Vatican's official newspaper Osservatore Romano, 4 March 2009, cited by Bloomberg.com, 2010)

2 DEFINITIONS OF KEY TERMS

The terms and expressions used in this Guidance shall have the same meanings assigned to them in the relevant laws of Uganda unless otherwise defined in this document.

2.1 **Family Takaful** refers to a long-term contract where participants make takaful contributions for their long-term needs such as education and compensation in the event of death, critical illness, or disability of the participants.

2.2 **Foreign policies** mean takaful certificates issued by a foreign professional retakaful operator in or from Uganda but are not Ugandan takaful certificates.

2.3 **Foreign professional retakaful operator** means a professional retakaful operator incorporated outside Uganda.

2.4 **General takaful.** Refers to all takaful contracts that do not come under the ambit of life takaful. A general takaful contract is a short-term renewable contract where participants contribute to motor takaful protection (e.g., coverage for cars, motorcycles, and commercial vehicles) and/or non-motor protection such as home takaful/fire, personal accident, and marine coverage, among others.

2.5 **Hybrid model.** This is a takaful business model that is structured in a combination of two of the previous models, i.e either: Wakalah and mudarabah model; Wakalah and Waqf model; or Mudarabah and Waqf model.

Note: Determination of the takaful model(s) that would apply in Uganda is charged to the Insurance Regulatory Authority of Uganda's Shariah Supervisory Board.

2.6 **Mudharabah (profit-sharing) model** is a sharia-compliant takaful business model where participants, as capital providers, contribute an amount of money periodically (the takaful premium) to the takaful fund which is managed by a takaful operator at a fee based on an agreed profit-sharing ratio between participants and the takaful operator.

Note: Determination of the takaful model(s) that would apply in Uganda is charged to the Insurance Regulatory Authority of Uganda's Central Shariah Supervisory Board (CSSB).

2.7 **Participant's Investment Fund** is a fund to which a portion of the participants' contributions is credited for purposes of investment or savings.

2.8 **Participant's Risk Fund (PRF)** is a fund to which a portion of the participants' contributions are credited for the purpose of donation. The PRF is used to pay participants' benefits.

2.9 **Qard** refers to a benevolent (interest-free) loan extended by a takaful operator to a takaful fund when there is a deficit in the participants' risk fund. A Takaful operator is required to rectify the deficit (i.e., where the assets of the participants' risk fund are insufficient to meet the liabilities) via Qard from the shareholders' fund. The Qard given is expected to be repaid from the excess of assets over liabilities arising in the participants' risk fund in the future years.

2.10 **Retakaful** refers to the Islamic re-insurance business.

2.11 **Separate financial statements** and **consolidated financial statements** shall have the same meaning as set out in IAS 27 Separate Financial Statements and IFRS 10 Consolidated Financial Statements.

2.12 **Shariah** refers to Islamic law.

2.13 **Takaful** refers to the Islamic insurance business.

2.14 **Takaful operator** means a person licensed under the laws of Uganda to carry on takaful business and includes a licensed international takaful operator and a licensed retakaful operator.

2.15 **Underwriting** refers to the process of selecting, assessing, and classifying the degree of risk of an applicant[8].

2.16 **Wakalah model** is a sharia-compliant takaful business model where participants, who are the owners of the takaful fund, appoint a takaful operator who is an agent (Wakil) to manage the takaful fund based on a pre-agreed wakalah fee (agency fee) that is normally deducted or paid upfront from the contributions received. In addition to the pre-agreed agency fee, the takaful operator is also remunerated with a performance fee (i.e., commission) on an agreed percentage when the fund meets certain expected performance agreed upfront with the participants.

[8] Underwriting is the most important process in takaful business and unfavorable underwriting results may affect the solvency of the risk fund and the takaful operator's profitability. Underwriting consideration consists of age, medical and non-medical (e.g. occupation, lifestyle, insurable interest, habits, and personal finances) risk factors.

Note: Determination of the takaful model(s) that would apply in Uganda is charged to the Insurance Regulatory Authority of Uganda’s Central Shariah Supervisory Board (CSSB).

2.17 **Waqf model.** Waqf refers to an endowment made by a Muslim to a religious, educational, or charitable cause. The Waqf model is a shariah-compliant takaful business model where contributions made by participants are treated as the property of the Waqf fund which can only be used for the benefit of all the participants. Under the Waqf model, a takaful operator is appointed by participants to manage the fund and accordingly, earns a wakalah fee or share of profits.

Note: Determination of the takaful model(s) that would apply in Uganda is charged to the Insurance Regulatory Authority of Uganda’s Central Shariah Supervisory Board (CSSB).

3.0 UNDERSTANDING TAKAFUL (INSURANCE) AND RE-TAKAFUL (REINSURANCE) TRANSACTIONS

3.1 Introduction

3.1.1 Takaful is an arrangement amongst a group of persons participating in a scheme under which the Takaful members (policyholders) jointly indemnify each other against any loss or damage that may arise to any of them. One of the differences between takaful and conventional insurance is that a takaful company does not have policyholders per se. It has 'contributors' or 'participants' since they undertake to participate collectively in the fund for everyone's mutual benefit. In this way, the whole pool of participants is responsible for one another and the burden inflicted by any participant becomes much lighter. The resulting fund (resulting from members' contributions) is used to make compensation (claim) payments for any loss or damage arising to any Takaful member. The claim payments are generally restricted to actual damage or loss and the opportunity costs (such as loss of potential income) are generally ignored. The entire arrangement relating to the receipt of contributions, claims payments, and the management and operation of a Takaful fund are managed by a Takaful company.

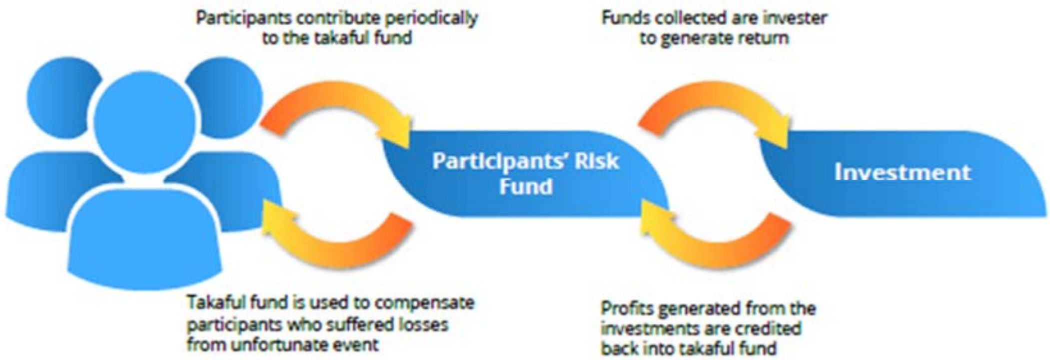
3.1.2 A Takaful arrangement is similar to a mutual insurance arrangement with the difference that Takaful members are typically not shareholders/unit-holders in the Takaful company which operates the arrangement for the Takaful members. The operator company is paid a fee for the services rendered and/or is entitled to a share in the return received on the fund's investments. To attain this goal Takaful adopts several models for general and family insurance. The term General Takaful is normally used as a reference to a general insurance arrangement while the term Family Takaful would normally refer to a life assurance arrangement.

3.2 Key Features of General Takaful Arrangements

The following are the key characteristics of a General Takaful arrangement.

- A company sets up a Takaful fund with contributions from the Takaful members (policyholders). The company records Takaful funds separately from its own share capital and reserves.
- All contributions made by participants are credited into participants' risk fund (PRF) and are treated as tabarru' (donation). This fund is then invested to generate

profits which will be channeled back into the participants' risk fund after the deduction of expected participants' claims.



- Figure 1: The General takaful process[9]

- The policyholders agree to compensate each other for any loss. This is normally set out in the insurance policy or other related documentation.
- The Takaful fund is used to make payments for any loss arising to a Takaful member (claim) and for any payments to a Re-Takaful operator (reinsurance payments). The surplus funds are invested by the company. The return on investments creates a reserve in the Takaful fund.
- The company would normally charge a fee for its services relating to the management and the operation of the Takaful fund. The fee may be fixed or a share in the returns on Takaful investments. It is also possible that the company is paid a fixed fee and is also entitled to a share in the return received on Takaful investments. The arrangement is normally set out in the insurance policy or other related documentation.
- Normally marketing and management expenses and commission payments are paid by the company out of its own funds.
- A loss relating to Takaful funds is normally charged to the Takaful fund and ring-fenced from the company's reserves. Likewise, a loss relating to the company's investments/activities is normally borne by the company and ring-fenced from Takaful funds.
- In case there is a shortfall in the Takaful fund, the company would normally make an interest-free loan to the fund. Generally, the loan is repayable only out of a future surplus arising in the Takaful fund.

[9] Accounting for Islamic Finance by available at https://www.mia.org.my/v2/downloads/resources/publications/2020/01/17/Accounting_for_Islamic_Finance.pdf

- If there is a surplus in the Takaful fund, the surplus is used for repayment of any interest-free loan owed to the company. Any remaining surplus can either be reserved for future losses or the company may decide to make a distribution to the policyholders. The distribution amount may be adjusted against the contribution payment relating to the following year.
- On dissolution or winding up of a Takaful fund, any surplus in the fund may be distributed amongst those who contributed to the Takaful fund or amongst those who are members (policyholders) of the fund on the day of dissolution or winding up. The surplus or any part thereof may also be given to charity. The Takaful funds cannot be diverted to the company.

3.3 Key Features of Family (Life) Takaful Arrangement

A Family (Life) Takaful arrangement works in a broadly similar way to a General Takaful arrangement. It is similar to a conventional life assurance policy. The following are the key differences:

- The contributions made by participants from the Takaful members (policyholders) are split between (a) **participants' risk fund** (a Contribution Account); and (b) **participants' investment fund** (an Investment Account). The split is agreed upon with the policyholder at the time of issuance of the policy and is generally based on the actuarial valuation of the associated risks.

  However. both funds will be invested to generate profits. Similar to general takaful, the participants' risk fund in family takaful is used to meet participants' legitimate claims. In cases where participants no longer contribute to the participants' risk fund, the participants' investment fund can also be used to meet future donations.

  If the Takaful member survives the policy term, the member is only entitled to receive the amount paid into the Investment account and any accumulated profits attributable to such amount.

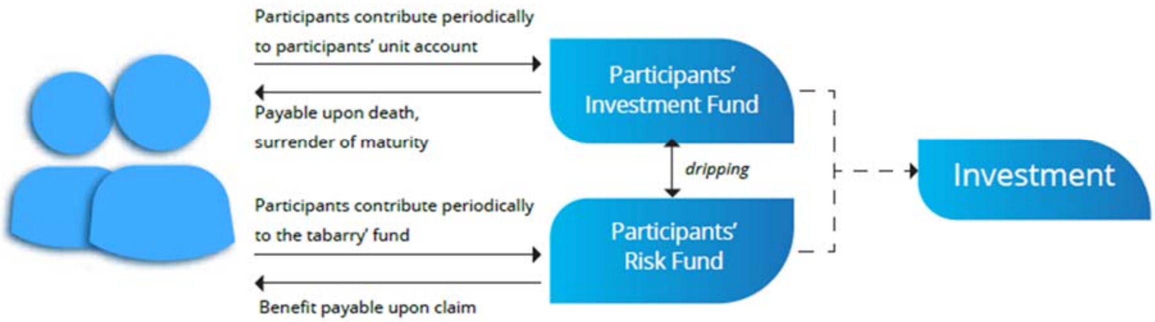


Figure 2: The Family takaful process[10]

- The profit made on Takaful investments is apportioned amongst the policyholders (Takaful members) or retained as a reserve for the future. The arrangement is normally set out in the insurance policy or other related documentation, as is the case with conventional life assurance.

3.4 Key Features of Re-Takaful (Reinsurance) Arrangement

A Re-Takaful (Reinsurance) arrangement broadly works in a similar way to a conventional reinsurance arrangement. Various Takaful companies participate in a Re-Takaful fund set up by a Re-Takaful company. The Re-Takaful company acts as the operator of the Re-Takaful arrangement. The distinction between the company's capital and reserves and Re-Takaful funds is maintained and both are ring-fenced from each other. The Re-Takaful company may be paid a service fee and/or a share in the profit made on investments made out of Re-Takaful funds. Where there is a shortfall in Re-Takaful funds, the Re-Takaful company would normally make an interest-free loan to the Re-Takaful fund which is generally repayable only out of a future surplus arising in the fund.

[10] Source: Accounting for Islamic Finance by available at https://www.mia.org.my/v2/downloads/resources/publications/2020/01/17/Accounting_for_Islamic_Finance.pdf

4.0 GENERAL FINANCIAL REPORTING REQUIREMENTS

4.1 The ICPAU Council is mandated to issue and adopt internationally accepted accounting and auditing standards and promote their usage in Uganda.[11] ICPAU (2009)[12], requires a financial institution (including a takaful company) to prepare its financial statements in accordance with IFRS and not the IFRS for SMEs.

4.2 Since IFRS are principle-based, a takaful company shall take into account the differences between takaful transactions and conventional insurance transactions. A takaful company shall therefore consider both the Shariah and the economic effects of such transactions to determine the most appropriate accounting treatment.

4.3 A takaful company shall comply with the resolutions of the Central Shariah Supervisory Board (CSSB) of the Insurance Regulatory Authority of Uganda on the applicability of the following accounting principles adopted in the IFRS to ensure consistency with the broader view of Shariah principles:

- i. Accrual basis of accounting;
- ii. Substance over form;
- iii. Probability;
- iv. Time value of money.

ICPAU recommends the following guidance on the applicability of the above accounting principles to takaful companies:

S/N	Accounting Principle	Our recommended Applicability
(a)	Accrual basis of accounting.	The effect of a transaction and other events is recognised when it occurs (and not as 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”	The “form” and “substance” of the transaction must be consistent and shall not contradict one another. Unlike IFRS[13], in the event of inconsistency between “substance” and “form”, Shariah places greater

[11] S12 (h) of the Accountants Act, 2013.
[12] Guidelines for Implementation of IFRS for SMEs in Uganda.
[13] Paragraph 2.12 of the Conceptual Framework for Financial Reporting, March 2018.

		importance on “substance” rather than “form”.
(c)	Probability	The degree of uncertainty that the future economic benefits associated with the transaction will flow to or from the takaful company is considered in reference to the recognition criteria.
(d)	Time value of money	Where a transaction involves time deferment, the asset (liability) is carried at the present discounted value of the future net cash inflow (outflow) that the transaction is expected to generate in the normal course of business. The application of time value of money is permissible only for exchange contracts that involve deferred payment and is strictly prohibited in loan transactions (Qard).

4.4 For financial instruments that are measured at fair value, a takaful company shall ensure that sound risk management and control processes around their measurement are in place as per IFRS 13 Fair Value Measurement.

4.5 A takaful company shall ensure that sound methodologies for assessing credit risk and measuring the level of loss allowance are in place[14]. The methodologies employed must incorporate a sufficient level of prudence and the aggregate amount of loss allowance must be adequate to absorb the inherent losses in the credit portfolio.

[14] A financial institution is encouraged to adopt the principles and guidance set out in the Guidance on Credit Risk and Accounting for Expected Losses, Basel Committee on Banking Supervision, December 2015.

5.0 SPECIFIC FINANCIAL REPORTING REQUIREMENTS

5.1 The financial statements and financial reports referred to in this Guidance shall be presented in Uganda Shillings (UGX).

5.2 For disclosures of non-compliance with externally imposed capital requirements, the relevant capital adequacy requirements shall refer to the minimum capital adequacy ratios as set out in the *Insurance Capital Adequacy and Prudential Requirements Regulations, 2020*.

5.3 The fundamental principle that adequate capital protects against distress applies equally to takaful operators as it does to their conventional counterparts. Regulation 4(1) of the *Insurance Capital Adequacy and Prudential Requirements Regulations, 2020* sets the minimum paid-up cash capital of an insurer engaged in: (a) non-life insurance business as six billion Uganda Shillings; (b) life insurance business as four billion and five hundred million Uganda shillings; and (c) Health Maintenance Organization (HMO) insurance business as one billion Uganda Shillings.

5.4 Furthermore, Regulation 4(2) of the *Insurance Capital Adequacy and Prudential Requirements Regulations, 2020* sets the minimum paid-up capital of a reinsurer engaged in: (a) non-life reinsurance business as nine billion Uganda shillings; and (b) life reinsurance business as six billion Uganda shillings. At the onset, one would thus believe that without any specific minimum capital requirements for takaful companies and given that in the meantime the country does not necessarily have fully-fledged takaful companies but the law allows for Islamic windows, the above minimum capital requirements would apply as a whole.

5.5 For separate financial statements, IAS 27:10 states that an entity shall account for investment in subsidiaries, joint ventures and associates either: (a) at cost; (b) in accordance with IFRS 9, or; (c) using the equity method as prescribed in IAS 28. However, a takaful company **shall not** account for investments in associates and joint ventures using the equity method described in IAS 28 *Investment in Associates and Joint Ventures* in the preparation of its separate financial statements.

5.6 A takaful operator in the preparation of its separate financial statements, as the case may be, shall:

a) present the assets and liabilities of the takaful fund (both family and general funds) separately from the assets and liabilities of the takaful operator;

b) present family takaful contract liabilities (including actuarial liabilities, unallocated surplus, and fair value/revaluation reserves, if any, of family takaful fund) as a liability in its statement of financial position;

c) present its investment-linked contracts as takaful contracts, consistent with the requirements of the industry *Guidelines on Investment-Linked Insurance/Takaful Business*[15];

d) in respect of its family takaful business, account for acquisition costs[16] as and when these are incurred and such costs shall not be deferred;

e) disclose provision for expense liabilities as per industry guidelines[17], as a liability in the takaful operator's statement of financial position;

f) be deemed to have complied with the requirements of a liability adequacy test under IFRS 17 Insurance Contracts if the valuation methods used are in accordance with the industry guidelines[18]; and

g) where a takaful operator is applying the temporary exemption from IFRS 9, in respect of its takaful business and to comply with paragraph 58 of IFRS 9 Financial Instruments: Recognition and Measurement and paragraph 20(a) of IFRS 4, deem objective evidence of impairment to exist where the principal or profit or both for financing/receivables[19] that are individually assessed for impairment, are past due for more than 90 days or 3 months. Impairment allowances for financing/receivables that meet this condition shall be determined in accordance with IFRS 9 or IFRS 4. In the case of treaty reinsurance/retakaful business, the date the statement is provided to the reinsurer/retakaful operator shall be deemed as the 'date due' to comply with this paragraph. This, however, does not preclude a takaful operator from assessing its accounts earlier for impairment if the accounts exhibit weaknesses[20] that heighten the risks associated with these accounts.

[15] We hope the IRA to develop guidance on Investment-Linked Insurance/Takaful Business
[16] Acquisition costs are commissions and agency related expenses incurred in securing contributions on takaful policies.
[17] We hope the IRA develops Guidelines on Valuation Basis for Liabilities of General Takaful Business and Guidelines on Valuation Basis for Liabilities of Family Takaful Business
[18] Same as in reference 14 above
[19] Includes Amount Due from Retakaful/Ceding Companies and Outstanding Contributions
[20] Takaful operators shall also consider the loss events listed under paragraph 59 of IFRS 9.

6.0 SPECIFIC REQUIREMENTS ON QARD

6.1 Owing to differences in the timing of cash flows and/or the inability of the in-force book to generate surpluses over the expected lifespan of the takaful fund, a deficit may arise from either liquidity, accounting, or regulatory considerations. The Insurance Regulatory Authority of Uganda[21] requires the takaful operator to meet the resulting deficit by extending an interest-free loan (qard) to ensure the capital adequacy of the relevant takaful fund. However, the takaful operator would only be a lender of last resort if and only if none of the following sources of funds is available to the takaful fund:

- Future expected liquidity surpluses from contracts currently generating liquidity deficits;
- Accumulated reserves from past surplus contracts; and
- Current/future surpluses from other takaful contracts.

6.2 Both the takaful fund and the takaful operator shall measure Qard at cost less any impairment losses.

At the end of each reporting period, the takaful operator shall assess for any indication that Qard is impaired in accordance with IAS 36. Where Qard needs to be impaired, the impairment loss shall be the difference between the carrying amount of Qard and its recoverable amount.

6.3 A takaful operator shall specify the period over which Qard will be repaid, which shall be determined in line with the industry set requirements as guided by the Insurance Regulatory Authority of Uganda.

6.4 A takaful operator shall ensure that the total assets and total liabilities presented in the takaful company's statement of financial position are net of Qard to avoid double counting of assets and overstatement of liabilities. To facilitate the reporting, the takaful operator shall be guided by the accounting entries for Qard as per Appendix 8.1.3.

6.5 In determining the recoverable amount of Qard, a takaful operator may be guided by the following principles:

a) The recoverable amount is the net surplus of the Participants' Risk Fund (PRF) or part of the PRF where the PRF is managed under smaller sub-funds;

[21] Regulation 37 (3) of the draft Takaful Regulations, 2019

b) The net surplus of the PRF is the amount of the PRF less the best estimate value of liabilities calculated according to valuation methods prescribed in the Guidelines as shall be set by the IRA;[22] and

c) In deriving the net surplus of the PRF, the value of the PRF should be as at that point in time and there should not be an assumption of growth of the PRF.

[22] Same as under footnote 14

7.0 INVESTMENT PROPERTIES

7.1 The amount of surplus arising from fair value gains on investment properties of the takaful fund which may be distributed to 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.

7.2 A takaful operator shall maintain relevant information supporting the valuations for IRA's review as and when required by the IRA.

8.0 MINIMUM DISCLOSURE REQUIREMENTS

8.1 The requirements under the following paragraphs refer specifically to disclosures that form part of the financial statements. This Guidance does not deal with other disclosures provided by a takaful company as part of the Annual Report (e.g., Director's Report, Statement on Corporate Governance, Shariah Committee Report, among others).

8.2 A takaful company shall make disclosures in the financial statements in accordance with the requirements of the IFRS Standards. This shall be presented along with any other information that may be required by the Insurance Regulatory Authority of Uganda.

8.3 A takaful company shall comply with the following key principles on disclosure of information:

a. information should 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 should be sufficient to provide comprehensive, meaningful, and relevant information to the users;
c. adequate disclosures should 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 should allow comparisons over time and between takaful operators[23].

8.4 The presentation of primary financial statements of takaful businesses is similar to the presentation of primary financial statements of the conventional insurance business, except for the statement of financial position, statement of profit or loss, and comprehensive income as well as a statement of changes in equity. The presentation of statement of financial position, statement of profit or loss and comprehensive income, and statement of changes in equity of takaful business is prepared based on a columnar basis where a takaful operator is required to present three statements: one for the takaful fund, one for the takaful operator

[23] Compliance with IFRS Standards, including the disclosure of the accounting policies used by the entity, helps to achieve comparability. For example, users shall be informed of the accounting policies employed 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.

and one for the takaful company. Therefore, a Takaful company shall present the financial statements according to the following minimum components:

a) Statement of financial position;
b) Statement of comprehensive income;
c) Statement of changes in equity;
d) Statement of cash flows;
e) Family takaful fund's statement of financial position;
f) Family takaful fund's statement of comprehensive income;
g) General takaful fund's statement of financial position;
h) General takaful fund's statement of comprehensive income; and
i) Notes to the financial statements.

8.5 For placements of funds in an investment account with an Islamic banking institution, a takaful company 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 notes the nature of the underlying assets for the investment.

8.6 A takaful company shall disclose intercompany charges with a breakdown by type of services received and geographical distribution.

8.7 The notes to be disclosed in the annual financial statements of the takaful company shall include the following information:

a. takaful contract liabilities;
b. reinsurance/retakaful assets;
c. takaful receivables (including details of Outstanding Contributions and Wakalah Fee Receivables);
d. other receivables (including detailed information on Qard);
e. takaful payables;
f. impairment provisions (include details on Impairment Provisions for Outstanding Contributions, Wakalah Fee Receivables, and Qard);
g. total capital available showing separately Tier 1 Capital and Tier 2 Capital;
h. expense liabilities (The breakdown shall be consistent with that specified in Risk-Based Capital Framework for Takaful Operator);
i. gross and net earned contribution;
j. gross and net benefits and claims;
k. fees and commission income;
l. management expenses;

m. 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 director, distinguishing between the executive and non-executive directors, and Shariah Committee members;
n. commitments and contingencies with a breakdown by types and amount distinguishing between contingent liabilities and commitments;
o. 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
p. amount of Zakat payable and method of calculating it as approved by the takaful operator's Shariah Committee.

<u>Interim Reporting</u>

8.8 The explanatory notes to be disclosed in the interim financial report of the takaful company shall 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 annual financial statements (refer to paragraph 7.8). In addition, the takaful company shall disclose items that are material to the understanding of the interim financial report in accordance with IAS 34 Interim Financial Reporting.

9.0 TAXATION OF TAKAFUL AND RETAKAFUL BUSINESS

9.1 Income Tax

For tax purposes, the General Takaful and Re-Takaful arrangements shall determine their chargeable income in accordance with Part IV and the Fourth Schedule of the Income Tax Act.

In principle under the General Takaful and Re-Takaful arrangements:

- Contributions (premiums) received by a Takaful company from policyholders (Takaful members) are to be treated as part of the gross income. Similarly, contributions received by a Re- Takaful company from Takaful companies, as members of the Re- Takaful arrangement, are to be treated as part of gross income.

- The amount of any other income derived by the Takaful or Re- Takaful company during the year of income in carrying on such a business, including any commission, investment income e.t.c is treated as part of gross income.

- The amount of any reserve deducted in the previous year of income for unexpired risks adopted by the Takaful or Re-Takaful company during that year of income.

- The deductibility of expenses incurred by a Takaful company or a Re-Takaful company for management, marketing, claims admitted, allowable expenditures and losses, agency and commissions, and any provisions in respect thereof should be treated in the same way as such expenses were incurred by conventional insurance or a reinsurance company with the same level of activity.

9.2 Withholding Tax

With respect to withholding Tax, the tax implications will largely depend on whether the Takaful operator is withholding tax-exempt or not. It matters not whether a contributing member makes their contributions to the Fund through an intermediary or whether the contributions are directly made to the Takaful operator.

A takaful operator shall withhold tax on the gross amounts paid as premiums to a retakaful operator who is a non-resident person applying a rate prescribed under Part XI of the Third Schedule[24] exceptions as guided under s.118D (2) of the Income Tax Act

9.3 Value Added Tax (VAT)

Except for general takaful arrangements, the supply of health insurance services, life insurance services, micro-insurance services of a takaful fund as well as re-takaful services, is exempt from VAT[25].

9.4 Stamp Duty

Stamp duty shall be charged by a takaful operator on all general takaful arrangements applying the rates prescribed in Schedule 2 of the Stamp Duty Act, 2014. No stamp duty is charged on family (Life) Takaful arrangements.

[24] Income Tax Act, Cap.340 Sec 118D
[25] Value Added Tax Act, Cap.349 Second Schedule

10 APPENDICES

10.1 Illustration of Financial Statements

Applying IAS 1:51, ICPAU has determined that for purposes of reporting, financial information for takaful fund, takaful operator and takaful company shall be presented separately in columns. This shall ensure that financial statements provide relevant information that is useful to users in making economic decisions. It shall demonstrate that the takaful company is conducting its business in a Shariah-compliant manner by differentiating the rights and obligations between the takaful operator and the takaful fund.

10.1.1 Statement of Financial Position for takaful company

Statement of Financial Position	**Note**	**(A) Takaful Operator (Shareholder fund) SHS'000**	**(B) Family Takaful fund SHS'000**	**(C) General Takaful fund SHS'000**	**(A+B+C) Takaful Company (Combined) SHS'000**
Assets					
Cash and cash equivalents		xxx	xxx	xxx	xxx
Investment assets		xxx	xxx	xxx	xxx
Takaful contract assets		xxx	xxx	xxx	xxx
Retakaful contract assets		-	xxx	xxx	xxx
Current tax assets		xxx	-	-	xxx
Trade and other receivables		xxx	xxx	xxx	xxx
Takaful receivables		-	-	xxx	xxx
Retakaful assets		-	xxx	xxx	xxx
Deferred tax assets		xxx	-	xxx	xxx
Intangible assets		xxx	-	-	xxx
Property, plant, and equipment		xxx	-	-	xxx
Total assets		**xxx**	**xxx**	**xxx**	xxx
Equity, Liabilities, and Participants' Funds					
Equity					
Share capital		xxx	-	-	xxx

Reserves		xxx	-	-	xxx
Total equity		xxx	-	-	xxx
Liabilities and Participants' Funds					
Current tax liabilities		-	xxx	xxx	xxx
Other current liabilities		-	xxx	-	xxx
Investment contract liabilities					
Takaful contract liabilities		-	xxx	xxx	xxx
Retakaful contract liabilities		-	xxx	xxx	xxx
Provision for wakalah fees		xxx	-	-	xxx
Deferred income tax liabilities					
Participants' funds		-	xxx	xxx	xxx
Total liabilities and participants' funds		xxx	xxx	xxx	xxx
Total equity, liabilities, and participants' fund		**xxx**		**xxx**	

10.1.2 Statement of Profit or Loss

Statement of Profit of Loss	Note	(A) Takaful Operator (Shareholder fund) SHS'000	(B) Family Takaful fund SHS'000	(C) General Takaful fund SHS'000	(A+B+C) Company (Total) SHS'000
Takaful revenue			xxx	xxx	xxx
Takaful service expense			(xxx)	(xxx)	(xxx)
Net expenses from retakaful contracts held			(xxx)	(xxx)	(xxx)
Takaful service result			**xxx**	**xxx**	**xxx**
Income from investments			xxx	xxx	xxx
Net Investment Income			**xxx**	**xxx**	**xxx**
Finance expenses from takaful contracts issued			(xxx)	(xxx)	(xxx)

Finance income from retakaful contracts held			xxx	xxx	xxx
Net takaful finance expenses			**xxx**	**xxx**	**xxx**
Net takaful and investment results			**xxx**	**xxx**	**xxx**
Operating revenue		xxx	-	-	xxx
Wakalah fee income		xxx	-	-	xxx
Surplus sharing from family takaful fund		xxx	-	-	xxx
Realised gains/(losses)		(xxx)	xxx	-	xxx
Fair value gains/(losses)		xxx	(xxx)	xxx	(xxx)
Other operating expenses		(xxx)	(xxx)	(xxx)	(xxx)
Profit before tax		xxx	xxx	xxx	xxx
Tax expense		xxx	xxx	xxx	xxx
Profit for the year		xxx	xxx	xxx	xxx

10.2 Accounting entries for Qard

For takaful contracts that generate surpluses, there will be no Qard triggered and consequently, no accounting would be required for either the takaful fund or the takaful operator. IAS 8:10-12 guides on accounting treatment for a transaction in absence of an IFRS that specifically applies to that transaction. Applying that guidance, a takaful company shall classify Qard as a payable of the takaful fund and a receivable of the takaful operator. The table below summarizes the accounting treatment that would be required:

S/N	DETAILS
1.	In the event that the takaful fund has a deficiency, the Insurance Regulatory Authority of Uganda[26] requires the takaful operator to meet the resulting deficit. However, the takaful operator would only be a lender of last resort if and only if none of the following sources of funds is available: a. Future expected liquidity surpluses from contracts currently generating liquidity deficits; b. Accumulated reserves from past surplus contracts; and c. Current/future surpluses from other takaful contracts.

[26] Regulation 37 (3) of the draft Takaful Regulations, 2019

<table>
<tr><td></td><td>If a takaful fund suffers a deficit in absence of any of the above sources, the takaful fund would expect to receive Qard from the takaful operator and would include the expected Qard cash inflows and outflows in its fulfilment cash flows applying IFRS 17 Insurance Contracts.</td></tr>
<tr><td>2.</td><td>When Qard is actually received by the takaful fund from the takaful operator:

(i) The expected Qard inflows of the takaful fund would be decreased to reflect the receipt. The takaful fund would recognise a payable (liability) with the following entries:

DR Cash XXX
CR Qard payable (Liability) XXX
[Narration: being Qard received from takaful operator (shareholders' fund) to rectify deficit]

(ii) The takaful operator would recognize a Qard receivable (asset) in the statement of financial position with the following entries:

DR Qard receivable (asset) XXX
CR Cash XXX
[Narration: Being Qard extended to Takaful Fund to rectify deficit]</td></tr>
<tr><td></td><td>In the takaful company's books (consolidated books of the takaful operator and takaful fund)

DR Assets (Qard + Cash) XXX
CR Liabilities XXX

(Narration: being double-counted assets and overstated liabilities)</td></tr>
<tr><td></td><td>DR Liabilities XXX
CR Qard XXX

(Narration: being the elimination of double-counted assets and overstated liabilities)</td></tr>
</table>

Note

a. Applying IFRS 17:24, the takaful fund could achieve a more faithful presentation by determining Qard cash flows at an aggregated level and then allocating the effect of those cash flows to all the affected groups on a rational basis.
b. ICPAU considers that compliance with IFRS 17 may require the following information to be included in the notes:

- The cumulative nominal amount of Qard advanced to the takaful fund and is included in the fulfilment cash flows;

- The effect and cause of changes in the amounts from period to period; and
- The expected repayment period of Qard.

Such information could be provided below the reconciliation fulfilment cash flows required by IFRS 17:101.