THE APPLICATION OF MICRO TAKAFUL MODEL ISLAMIC MICRO INSURANCE MODEL AS A TOOL FOR THE GROWTH OF SMALL AND MEDIUM ENTERPRISES, SME'S IN NIGERIA

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ABSTRACT

Takaful. Islamic insurance is one of the engine blocks of Islamic finance. Islamic economics, Islamic banking/finance and Sukuk i.e. Islamic capital market instrument are other economic engines. Takaful plays a significant role in the growth and development of economic activities The role of Islamic insurance in the growth and development of economic activities cannot be overemphasized, takaful industry in an economy have long ago been recognized as one of the aids for economic growth, Therefore Nigeria as a nation cannot pause tapping the benefit of Takaful especially in its crusade for small and medium enterprises growth and development. This paper explores the models of Takaful for small and medium enterprises growth, an exploratory method of study was adopted, and the paper is largely based on documented research of related literature. From these studies, deductive method of reasoning was used to logically construe the application of Takaful models as a tool for the growth of small and medium enterprises in Nigeria. Finally based on the reviewed works, appropriate takaful models for the growth of small and medium enterprise in Nigeria was drowned, comprising participant's contribution, donations from philanthropies, government interest-free loans, saving and investment returns from interest-free financial institutions.

Key words: Takaful, Micro Takaful, Economic Growth and SME'S.

INTRODUCTION

Islamic finance becomes among the most acceptable worldview in the 21st century (Islamic Finance Report Malaysia, 2014). Islamic Insurance contributed in the world economic growth and development and became the only shock absorber of the economic meltdown in the 21st century. Global Reinsurance co. Report, (2015) Takaful as an engine block of Islamic finance, Islamic economics, Islamic banking/finance and Islamic capital market instrument i.e. Sukuk are other economic engines. The role of Islamic insurance in the growth and development of economic activities cannot be over emphasize, takaful industry in an economy have long ago been recognised as one of the aids for economic growth (Ayub 2014) therefore it is crucial for Nigeria as a nation to tap the benefit of takaful in its crusade for small and medium scale enterprises growth and development. Beck and Bhatti (2007)

Evidence of a positive causal relationship between insurance penetration and economic growth have been identified, the partner-agent model facilitates the pooling of risks between the formal and informal sectors, enhancing access, quality of basic financial services, availability of credit and mobilization of savings. Insurance and risk management facilitate sustainable growth and productivity, especially for small and medium scale enterprises. Beck (2010). Hasim (2014) despite its essential role, efficiency, fairness and equity, Islamic finance, still 2.7 billion People (70% of the adult population) in emerging economies still have no access to basic Islamic financial services. To this, Micro Takaful services are also imperative for the success of small and medium scale enterprises constituting mostly the adult class not in Nigeria only, where access or financial inclusion strategies still faces drawbacks both at governmental and individual levels. Whereby people are exposed to all sorts of risks in their daily life expected and unexpected, and these risks damage one’s life, properties, and business ventures.

Most often, these risks affect and leave the lives of individuals in the societies so devastating, shattering, vulnerable and helpless. Matsawali (2012). During the 21st century global financial crisis, many micro enterprises were affected, (Muhammad, 2010) stated that SMEs were affected to a larger degree since many SMEs operators were involved in trading and supplying products or services to other businesses during the subprime financial crises. These operators were mostly low-income earners, and the crises compelled them to have some form of risk protection, hence, the need for micro Takaful to aid in the critical business situation. Micro Takaful protects against insurable risks. This idea is supported by Turkestan, (2008), who contended that micro insurance protects assets and lives against insurable risks of the target population, such as micro entrepreneurs and low-income people in relation to cost, terms, coverage, and delivery mechanisms.

Akhter, and Khan, (2009), further elaborated that the protection against risks such as losses and natural perils is important in order to achieve sustainable development of living, it also provides a sense of security for living and prevents poor communities from falling into abject poverty. Bhatti, (2010), stated that the existence of micro finance and micro Takaful is considered as poverty alleviation strategies to empower people and exit them from poverty and retain financial ground. Micro Takaful, therefore, protect SME’S aiding their basic needs, especially average, low and poor SME’s who cannot afford the specific sum required by the takaful companies and provide a way of pooling resources among themselves against unforeseen specified risk, in a sharia (Islamic law) compliant manner. The weight of micro enterprises is the crucial outlook for employment opportunities of a nation, especially developing country like Nigeria with abundant unemployed teeming youth.

Bank study (1978) points out the advantages of micro enterprises as increasing aggregate output, efficient use of capital and labor, initiating indigenous enterprise, improving management skills, resulting in economic balance, and fairness in income distribution. With the numerous advantages, micro enterprises are faced with problems associated with low wages, the high price of finance, and use of primitive technology in Nigeria.

Furthermore, limited input and output markets and inadequate infrastructure facilities hinder the growth of small enterprises in most developing nations (Khan 2007). Smaller firms usually do not have access to funds from traditional financial institutions (Berger and Udell 1998). The application of micro takaful is a panacea to the worrisome financial and material risk faced by SME’s in Nigeria, which this study is showcasing.

This paper consist of an introduction, Methodology, legal Basis of Takaful, Silent features of insurance and Takaful Concept, Why Micro-Takaful and Objective, Micro Insurance and Micro Takaful, Small and Medium Enterprises, Proposed Micro Takaful Model and Conclusion respectively.

METHODOLOGY

This paper explores the models of Takaful for small and medium enterprises growth in Nigeria. The paper is largely based on documented research of related studies to source its literature. From these studies, a deductive method of reasoning was used to logically construe the application of micro takaful models as a tool for the growth of small and medium enterprises in Nigeria. Finally, based on the relevant literature, appropriate micro takaful model for the growth of small and medium enterprises in Nigeria was drowned.

LEGAL BASIS OF TAKAFUL

Takaful scheme has evolved from the teachings of Islam, i.e., on the basis of the *Quran* (Divine Law) and the Sunnah (Traditions of Prophet Muhammad S.A.W.). (*The Quran* 5:2) *"*Help ye one another in righteousness and piety, but help ye not one another in sin and rancor." Another verse narrated: You will plant for seven years consecutively; and what you harvest leave in its spikes, except a little from which you will eat. (Q. 12:47). Then will come after that seven difficult years which will consume what you saved for them, except a little from which you will store. (Q. 12:48). This shows how Islam promotes the act of taking precautionary measures against any risks. The above verse described how Prophet Yusuf (*Allaihi-Salam)* filled the grain silos from the surplus of seven years of a good harvest as a protection to ensure the availability of continuous food supply during the seven years of drought, which originates insurance.

Prophet Muhammad (P.B.U.H) said: "The believers, in their affection, mercy, and sympathy to each other, are like the body, if one of its organs suffer and complains, the entire body responds with insomnia and fever" *(Muslim).*also in a separate Hadith narrated by Abu *Hurayrah,* the Prophet (S.A.W) said, *"Whoever removes a worldly grief from a Muslim, Allah will take away one of his grief's in the hereafter, whoever alleviates the needy, Allah will alleviate from him in both the world and Hereafter"*

Yosef. (1996) Cited some reasons influencing the design and offerings of takaful business. First, Muslims felt the need to practice Islam and apply its rules and regulations in total. Second, Muslims desire a financial system that can create a truly Islamic economy for the sake of the *ummah*. Third, with the establishment of the Islamic banking system, an inherent need arose for takaful or Islamic insurance to complement its services and offerings. It was the historical evidence that led Muslim jurists to acknowledge that the basis of shared responsibility in the system of „*Aqilah,"* laid the foundation of mutual insurance, and in general conclude that insurance in Islam must be based on the principles of mutuality and cooperation. Practicing Islamic insurance in Muslim's life is therefore part of the objectives of life and fulfilment of righteousness to attain success in this world and the hereafter. According to Muhammad (2007), Islam does not like the concept of the "pious person" as distinct from the "worldly person." It enjoins a system of devotions/worship as well as guides on the economy, political affairs, and international relations. Regarding this integrated approach, the Holy Qur'an says:

'It is not righteousness that ye turn your faces towards East or West, but it is righteousness to Believe in Allah and the Last Day, and the Angels, and the Book and the Messengers; to spend of your substance, out of love for Him, for your kin, for orphans, for the needy, for the wayfarer, for those who ask, and for the ransom of slaves; to be steadfast in

prayer, and practise regular charity, to fulfil the contracts which we have made; and to be firm and patient, in pain (or suffering) and adversity, and throughout all periods of panic. Such are the people of truth, God fearing. (2: 177)''

SILENT FEATURES OF CONVENTIONAL INSURANCE AND CONCEPT OF TAKAFUL

According to Muhammad (1985), three elements in conventional insurance do not conform to the requirements of the *Shari'ah* law:

(i) ***Al-Gharar***: (Speculations). This refers to 'unknown' or 'uncertain' factors in a conventional insurance contract. In conventional insurance, policyholders are not informed on how profits are distributed and in what the funds are invested in. In a Takaful operation, this is based on the *Mudharabah* concept, the distribution of the benefits to the operators and the participants are outlined in the contract. Lack of clarity in the transaction, some hidden terms, and conditions of contract called invisible hands and ambiguity in business affairs result in the business catastrophe which also insured and protects only one party and denied the other is a distinguishing factor between micro-takaful with conventional micro finance

(ii) ***Al-Maisir***: (Gambling). This is the 'gambling' element and is said to derive from 'Gharar' element. In conventional insurance, the policyholder stands to lose all the premiums paid if the risk does not occur. On the other hand, he stands to get more should a misfortune happen while paying a small amount premium. In Takaful, even though the risk does not occur, the participant is entitled to get back the contributions that he has paid. Should the risk occur, he will be paid from his premium fund plus the pool of funds from the 'donation' of other participants? The gambling concept is forbidden it involves transactions by chance, cost less earnings and dubious reward, micro-takaful promotes earnings in activity, reward in participation and extension of helping hands to grow a human society.

(iii) ***Riba***: (Interest). This refers to the interest factor present in the investment activities of conventional insurance companies. The policy loan in conventional life insurance is, in fact, a *Riba* based transaction. Islam prohibits any investment in non-Halal products. Also, it is an increase above the quantum of the principle lent demanded by the creditor upon the debtor weather the finance borrowed incur gain or loss. In micro-takaful the participant's funds are used as benevolent and a gesture to one another with no compensation or payback reward, what they are after is mutuality among them and the hereafter reward.

Abdul Rahman, Yosef, and Abu Bakar (2008) asserted that Takaful is acceptable in Islam by risk-sharing under the *Taawun* principle through the creation of the *Tabarru* (donation) fund. The Arabic text, "Takaful" is derived from the word "*Kafala*" which means to guarantee and protect. In Islamic interpretation, *Takaful* is a pact among a group of members or participants that agree to always give mutual assistance to one another (Takaful Brunei Darussalam, 2011). Micro Takaful (micro insurance) is defined as the protection of assets and lives against insurable risks of the target population, such as the micro entrepreneurs and low-income groups.

WHY MICRO-TAKAFUL AND OBJECTIVE

During the 21st global financial crisis, many micro enterprises were affected. Muhammad (2010) stated that SMEs were affected to a larger degree since many SMEs operators were involved in trading and supplying products or services to other businesses during the subprime financial crisis. These operators were mostly low-income earners, and the crises compelled them to have some form of risk protection. Hence, the need for micro Takaful. Micro Takaful protects against insurable risks. This idea is supported by (Turkestan and Ahadi, 2008) who contended that micro insurance protects assets and lives against insurable risks of the target population, such as micro entrepreneurs and low-income people about cost, terms, coverage, and delivery mechanisms.

Akhter et al. (2009) further elaborated that the protection against risks such as losses and natural perils is necessary to achieve sustainable development of living. It also provides a sense of security for life and prevents poor communities from falling into abject poverty. Bhatty, (2010) stated that the existence of micro finance and micro Takaful is considered as poverty alleviation strategies, poverty reduction mechanism and retain financial ground among SME's. This illustrates the importance of micro Takaful as a risk mitigation technique to solve business operation problems. Thus, the need for micro *Takaful* products and services for risk protection.

Micro Takaful is derived from the overall concept of Takaful to meet the basic needs of the average, low and Poor's who cannot afford the specific sum required by the takaful companies; it is a pool of resources by the average, low and poor income earners to protect themselves against unforeseen specified risk. This is to enable them to solve their basic needs of education, health, shelter, and food, etc., in the Shari'a (Islamic law) compliant manner for both Muslims and non-Muslims.

The objective and basis for takaful organizations remain that of the micro takaful since it has to fulfill all shari'a obligations of forbidden *gharar*, *maysir* and *riba* also participants in micro Takaful has to agree in helping one another with their contributions at the occurrence of defined catastrophe stated in the deed agreement. Bello (2015) Takaful in general and micro takaful, in particular, cannot go beyond the objectives of the shari'a in which it is built from, which includes, protection of Religion, Life, Progeny, Property, Intellect, and Honour. Also micro takaful compliments the aim of Islamic finance of equity, justice, and fairness in societal dealings.

MICRO INSURANCE AND MICRO TAKAFUL

Micro insurance is a subset of financial tools from the microfinance. It was not a standalone discipline but within micro finance and later developed into a field of study. Ingram and McCord (2011) 'micro' means a small unit than the total in the larger community. Micro insurance is not a new form of insurance facility but a special one indeed. As such it is defined as either life micro insurance or non-life micro insurance policies that provide protection to the poor and against specific risks in exchange for a regular payment of premium calculated proportional to the likelihood and cost of the relative risk. Hisam (2014).

The pool is to reimburse those members of the micro insurance scheme who suffer losses from a predefined set of perils. Micro insurance aims at protecting the poor and low-income earners. There is an element of a social protection system, similar to social insurance schemes. A study by (Ramm and Ankolekar, 2014) addresses the potential and roles of micro insurance within a broader social protection framework in a country, by identifying it as an idea of protecting the poor and the low-income earners from abject poverty; this work tends to argument some models to solidify the gesture to small and medium enterprises owners.

A micro insurance that complies with *shari'a* principles is called micro takaful. The mechanism provides *shari'a*-based protection to the poor, average, low-income earners and under-privileged individuals at an affordable rate (Akhtar, 2006). Micro insurance (micro takaful) is a type of insurance (takaful) geared towards protecting the poor, average, low-income earners and vulnerable people in the society. The low-income earners can benefit from Takaful products through their sources of income, contributions, and donations among themselves to guide future occurrence of hazards inherent in their businesses, through any of the models, more importantly, the Micro-Takaful.

SMALL AND MEDIUM ENTERPRISES

In a practical sense, economic goals cannot be achievable without the immense contribution of SMEs. It must be emphasized that it is while attending to small matters that bigger things are created from (Sule, 1986). Small and medium enterprises (SMEs) play important roles in the economic growth and sustainable development of any economy (Ariyo, 2005). SMEs may look small by name and nature, but they set the foundation for economic growth for nations. The potential benefits of SMEs to any economy include a contribution to the economy regarding the output of goods and services; creation of jobs at relatively low capital cost; provision of a vehicle for reducing income disparities; development of a pool of skilled and semiskilled workers as a basis for future industrial expansion, among others. Taranga, (2011). This SME'S imperative demands a squarely continues management of the organization to create proper understanding among the practitioners in the field of business and the operators of small enterprises in driving a sustainable finance mode for risk mitigation, which is the mind of this note.

According to NCI, (2003), a small-scale industry is an enterprise with total cost (including working capital but excluding cost of land) above N1.5m, with a labour size of between 11 and 100 workers, while the medium-scale industry has a total cost (including working capital but excluding cost of land) above N50 million but not exceeding N200million, with a labour size of between 101 and 300 workers. On the other hand, the revised operational guidelines of SMEEIS, (2005) defines a small and medium industries as an enterprise with a maximum assets base of five hundred million nairas (N500m)(excluding land and working capital), and with no lower or upper limit of staff. The size and magnitude of SME'S in the micro-takaful organization does not hinder its management, what is keenly is the managing policy and the guiding principles to ensure adherence to the Islamic code of conduct which stipulates not the magnitude but the managerial affairs, whether hundreds or thousands in composition what matters is the binding rule and selves agreement.

The contradictions in the definition of SMEs as given by NCI, (2003) and SMEEIS (2005) point to the different interpretations of what SMEs are at various schemes. Hence, their approaches to the funding of SMEs are affected. In addition to this, however, the small business' contribution to macroeconomic development is inhibited by the fact that they have no, or only overpriced, access to financial institutions and other services (Schneider, 2002).

More so the accessibility to funds and the cost of rising have remained issues limiting the in-capitalisation requirement leading to the premature collapse of SMEs (Mambula, 2002). Funding has, therefore, continues to be one of the key managerial problems that keep confronting business enterprises in Nigeria today. An adequate source of fund for SME'S is a catalyst for their growth and development in which this work intends to identify other means of fund generation for small enterprises in Nigeria, but using some Islamic resource acquisition manners. The two fundamental financing concepts of SMEs, the formal and informal forms of funding, have been identified by scholars and practitioners (Galina's, 1998).

Also in Aruwa, (2004) the findings were that, among the most popular of the formal sources of financing, the commercial banks and development banks remain the official sources of finance for enterprises. The informal sources, which comprise borrowing from friends and relatives, and cooperative credits, have also been identified as potential sources of financing SMEs. The problem of SME financing has received a tremendous research efforts from researchers. Some notable works in this respect include Arnold, (1998). Anic and Paus, (1998), Inang and Ukpong, (2002) and Aruwa, (2004). In their findings, four problems in financing SMEs have become recurrent: the cost of capital; risk; the inappropriate terms on bank loans; and the shortage of equity capital. They are the suggestion that government should come to the rescue of SMEs. This call was seemingly answered when Small and Medium Enterprises Equity Investment Scheme (SMEEIS) came on board in 2001. SMEEIS is a banker's committee financing initiative that started in 2001 to finance SMEs in the form of equity participation. Some of the works concerning funding for SMEs were done before SMEEIS came into existence while some were in the early operational years of SMEEIS, which some of the researchers felt was premature to assess the initiative objectively.

Presently, it is over fifteen years since the inception of the scheme, which is a reasonable period to critically evaluate its performance. SMEEIS is the current sector driven economic policy thrust of government involving banks. It is an equity financing initiated by the federal government aimed at formalizing SMEs source of funding. (Terungwa, 2011). This background paves the way for re-structuring SME'S development to ensure continues and robust growth of microfinance and takaful activities for economic development in a nation like Nigeria and other similar developing countries. The recent development by the present government of Buhari in re-introducing Nigerian development Bank mainly for the growth of SME's in the country is a giant step towards the development of SME's; the bank was initiated to provide soft and affordable funds for small and medium enterprises. This still does not concur with the Micro-Takaful objective of mutuality among participants. This paper finds it imperative to design a model that will sweet and compliment another effort to ensure the growth of SMEs through enhancing their sources of funds. The proposed Micro Takaful model is a risk mitigation formula and funds generation via contributions and donations through capital formation and risk management.

Takaful models commonly used

The types of models commonly used by takaful operators namely Al- mudarabah model (profit sharing) and Alwakalah (agent) (Rabiah, 2010). However, all the models pursue the same goal of sharing individual risks collectively to reduce the risk exposure of each participant against a specified loss. There are two standard models applied, namely the *mudarabah* model and the *wakalah* model. Another model prevalent in practice is the combination of these two models. Bisani, (2011)

***Mudarabah* model**

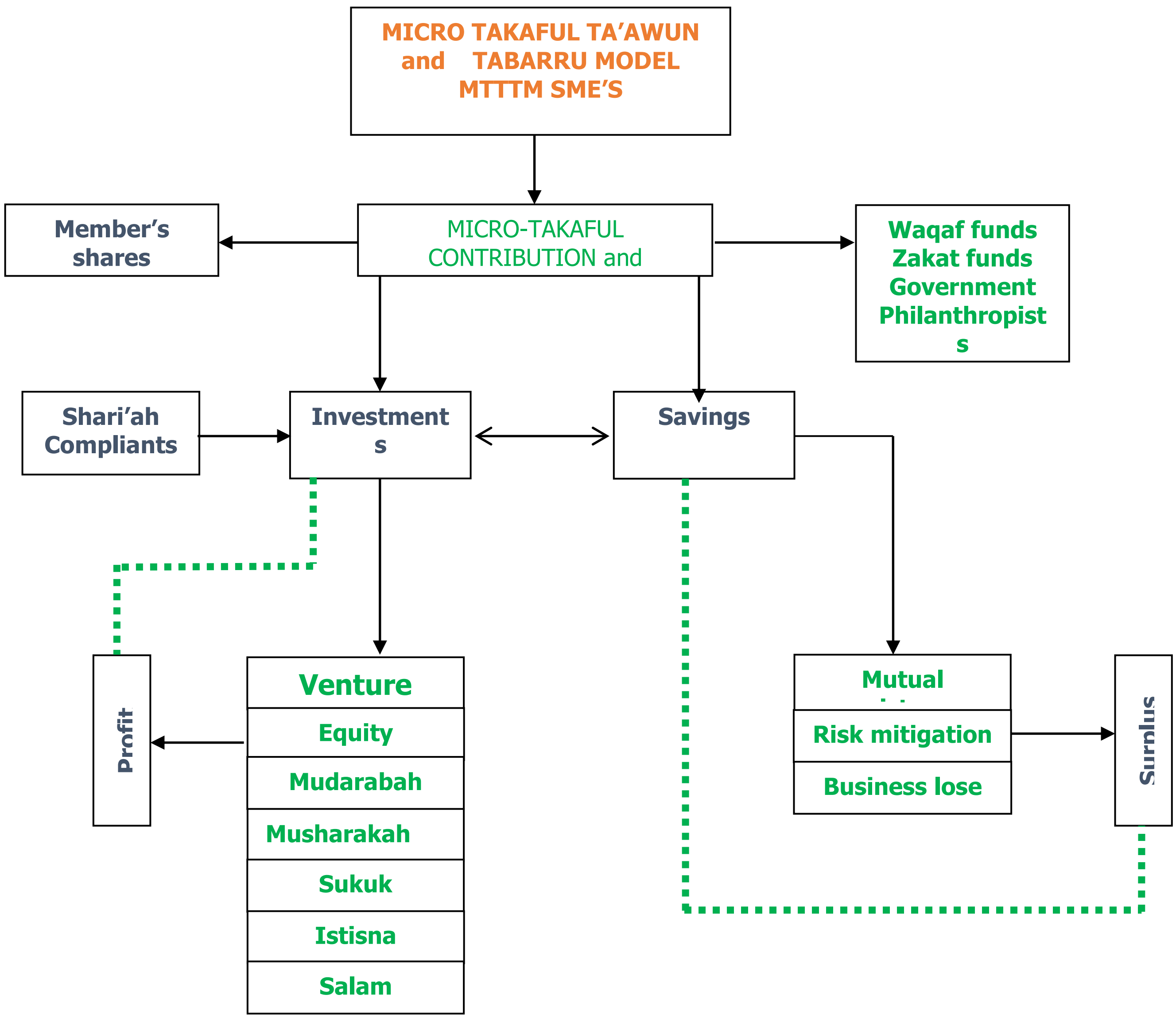
The *mudarabah* model is the profit-sharing model, is based on a principal-manager agreement. It was introduced in the Malaysian market in 1984. ***Waqf* model** the *waqf* model, also frequently referred to as *wakalah waqf* model was developed and is practiced in Pakistan. It shows some resemblances to the combined model. Bisani (2011)

The main difference towards the previous models is that, in this business model, the PTF constitutes a separate legal entity in the form of a *waqf*. As a consequence, the risk Fund belongs neither to the operator nor the participants. The ownership rights of the *takaful* funds are transferred from the TPs to the *waqf*. The relationship between the TP and the participants is established via the *waqf* entity. Bisani, (2011).

***Wakalah* model** the *wakalah* model is based on a principal-agent arrangement. In an agency contract, rights or businesses are delegated to an agent who acts on behalf of someone else. He is in charge of contributing his knowledge, skills and abilities in order to fulfill his duties. The development of the *wakalah* model started in Sudan and the Middle East, where it is also still widely used. Bhatti (2011)

Combined model, the combined model, also referred to as *wakalah mudarabah* model represents the most prevalent business model in takaful. As the name suggests, this model combines the *wakalah* model for underwriting with the *mudarabah* model for investment. This *takaful* model is also accredited and recommended as standard practice by the AAOIFI (Accounting and Auditing Organisation for Islamic Financial Institutions). Bisani, and Imran (2011).

PROPOSED MICRO TAKAFUL MODEL AS A TOOL FOR THE GROWTH OF SMEs IN NIGERIA



Proposed Micro Takaful Model

SMEs capital is assumed inadequate and small. However, the basic needs surrounding the owners are much bigger than the business itself (Khan, 2011) the surrounding basic needs lying on the enterprise which cripples the growth and expansion of the businesses are mostly physical and insurable. Such requirements include Educational, Health, Marriages, and Naming Ceremonies, festivities, Shelter, Mobility and Funeral burial which engulf the SMEs capital. Imran (2012) The need to ensure these basic needs for the growth of SMEs is imperative which will in return increase economic activities and capital growth of the SMEs. This model tends to sketch how contribution from participants is invested, and donations received channeled to mitigate participant's basic needs.

The operational model of microtakaful is similar to takaful scheme as *mudarabah*/*wakala* takaful model but can be structured on some models without altering the concept of *mudarabah* and *wakala* takaful. The proposed micro takaful model is a combination of Takaful *Ta'awun* and *Tabarru* models, i.e., It is an integrated model to invest participant's contribution and using donations from the government, *zakat* funds, *waqf* funds, sadaqats funds, donor organizations and NGOs for the reduction or meeting participants' basic needs and the mitigating business loses. The Proposed model for Micro-takaful, is based on participant's contributions and donations received by the TPs i.e. Takaful participants using *Mudarabah*, *Waqaf* and *Wakala* model in Takaful contract, the participants pay contribution and receive donations, these funds spelled into two accounts, *shari'a* complaints investments accounts or financing services such as venture capitalist, equity, *mudaraba* financing account, *musharaka* financing account, salam financing, *istisna* financing, ijara etc and Participant's Account (PA) for the purpose of savings only, the two accounts were created to diversify income from contributions and donations. Any deficit from any account if incurred, surplus from other accounts can be used to fund the deficit.

The micro Takaful operator gets his charges base on the agreed terms from owners' of the micro-takaful, and returns are shared accordingly. This diversified takaful approach is grounded to cover the two accounts and manage them concurrently by the takaful operator. This concurs with (Zainal, 2013) proving that Charitable Trust Fund received in a cooperative can be managed with the intention that it will be preserved over time notwithstanding that it may be temporarily used by the participants' to meet temporary deficits due to fluctuating claims experience. In this context, the participants' fund is the Cooperative Common pool, When the Cooperative Common Pool fund runs a deficit, the Charitable Trust Fund provides *qard hassan* (benevolent loan) to the Cooperative Common Pool fund to cover the deficit. The *qard hassan* will be repaid when the pool returns to profitability with no extra charge.

CONCLUSION

The overwhelmed acceptability of Islamic financial services in the 21st century leads to derivation of Micro Takaful from Takaful (Islamic insurance), is a great opportunity for institutions both governmental and non-governmental to tap this ground and secure an enabling environment for the low income earners especially the small and medium enterprises by coming up with strategic models such as the micro takaful model for the growth and development of SMEs. This paper is a helping hand towards a boast to the Takaful sector in Nigeria where Islamic financial services are in hatching stage, the paper proposes a Takaful Mudarabah/Waqaf model i.e. Investment/Donation micro Islamic insurance facility based on shari'a law and principles, as a strategy for curtailing the cankerworms that prevent the growth of SMEs in Nigeria. The work provides a platform for the SMEs to ensure basic needs of Education, Health, Shelter, Mobility, Funeral Burial and festivities hindering speed growth of SMEs in Nigeria.

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