



Comparison of Fund Management Systems in Conventional Insurance and Sharia Insurance

Aicha Azdina Adly Fesya¹, Salsabilla Hamdi², Larasati Ritonga³, Zaldy Ichsan Febrian⁴, Ilham Soleh Tanjung⁵

¹International Open University Kanifing Gambia

^{2,3,4,5}State Islamic University of North Sumatra

E-mail: azdinaaicha19@gmail.com salsabillahamdi7@gmail.com

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Abstract

Insurance is a crucial instrument in the financial system, serving as a means of risk management. In Indonesia, insurance practices have developed into two main systems: conventional insurance and sharia insurance, which differ fundamentally, particularly in fund management. This article aims to compare fund management systems in conventional and sharia insurance, based on a review of previous research, laws and regulations, and relevant literature. The research method used is library research with a qualitative descriptive approach. The results indicate that fund management in conventional insurance is based on the principle of risk transfer, with a system of pooling premiums owned by the company, and investment management that potentially contains elements of *riba*, *gharar*, and *maisir*. Meanwhile, sharia insurance applies the principle of risk sharing through *tabarru'* and *tijarah* contracts, with the separation of participant funds from company funds, and investment management that must comply with sharia principles. Furthermore, differences in fund management are also reflected in the underwriting surplus mechanism and oversight by the Sharia Supervisory Board. Thus, it can be concluded that the fund management system in Islamic insurance has more transparent characteristics and is oriented towards the principles of justice and mutual assistance, in contrast to conventional insurance which is oriented towards company profits.

I. INTRODUCTION

The financial industry in Indonesia has shown significant growth, particularly in the insurance sector. Insurance plays a crucial role in protecting individuals and businesses against future risks. Through structured fund management mechanisms, insurance can provide financial security in the event of an unforeseen event. As public demand for risk protection products increases, the insurance system in Indonesia has evolved into two main forms: conventional insurance and sharia insurance.

Insurance (*verzekering* or insurance) is generally understood as a form of coverage. Professor R. Sukardono of Commercial Law explains that the term insurance originates from the word "*verzekeraar*," which refers to the insurer, the party responsible for the risk. Meanwhile, "*verzekerde*" is defined as the insured, the party who transfers the risk of their property or life to the insurer. On the other hand, Professor Wirjono Prodjodikoro uses the term "*asuransi*" as a loanword from the Dutch word

"*assurantie*," with the term "*penjamin*" for the insurer and "*terjamin*" for the insured. (Subagiyo, 2014)

Conventional insurance has long been known and used by the public, with a fund management system based on the principle of risk transfer from participants to the insurance company. In this system, premiums paid by participants become the property of the company, which is then managed and invested to generate profits. However, in practice, the conventional insurance system has often been criticized, particularly from an Islamic economic perspective, for allegedly containing elements of *usury* (*riba*), *gharar* (uncertainty), and *maisir* (gambling) in fund management and its contractual mechanisms.. (Jairin, 2021)

As an alternative, Islamic insurance exists to address the Muslim community's need for a risk protection system that complies with Sharia principles. Sharia insurance is based on the concept of mutual assistance (*ta'awun*) and risk sharing among participants, realized through the

tabarru' contract. In this system, funds collected from participants do not belong entirely to the company but are managed separately, separating participant funds from company funds. Fund management in Islamic insurance must also comply with Sharia provisions, including investment aspects that are free from *riba*, *gharar*, and *maisir*, and are supervised by the Sharia Supervisory Board. (Afandi, 2022)

The aim of this research is to examine the conventional and sharia insurance fund management systems from the perspective of regulations and operational principles.

II. RESEARCH METHODS

This study employed a qualitative research method with a library research approach. The data sources used were secondary data obtained from previous research, insurance-related laws and regulations, and relevant books and scientific literature. Data were collected through a search and review of these sources, then analyzed descriptively to compare fund management systems in conventional and sharia insurance, in accordance with the research objectives.

III. RESULTS AND DISCUSSION

A. Basic Concepts and Principles of Conventional Insurance

The definition of insurance varies widely and has been put forward by many economists and insurance experts. One definition states that insurance is a form of collective effort in society consisting of a group of individuals who collect funds through a contribution payment system to mitigate or eliminate economic losses that may be experienced by the group's members. Thus, insurance can also be understood as an effort to reduce risk. The primary function of insurance is to provide compensation for economic losses arising from disasters or accidents. Formally, insurance can be defined as a system in which insured participants, for certain considerations, promise to pay contributions, in exchange for guaranteed compensation or assistance if they experience losses related to the loss of economic value during their membership period.

Simply put, insurance can be defined as a reserve fund set aside by a group of people to deal with unforeseen events. If one member experiences a loss, the burden of that loss is shared by all members of the group. Therefore,

the primary purpose of insurance is to provide protection against various risks that can threaten human life and activities. In practice, this threat of loss is what drives humans to create various protection mechanisms to avoid it.

According to Article 246 of the Republic of Indonesia Commercial Code (KUHD), insurance or coverage is an agreement in which the insurer binds himself to the insured by receiving a premium, to provide compensation for loss, damage, or loss of expected profits, which may be experienced due to an uncertain event.

Based on this definition, insurance has four main elements, namely:

- a. The insured party is obliged to pay premiums to the insurer, either at once or in installments.
- b. The insurer is obliged to pay compensation to the insured if an uncertain event occurs.
- c. There are events that cannot be predicted beforehand.
- d. There are interests that could cause losses if the event occurs.

Conventional insurance is a type of insurance that is run based on the principle of risk transfer. In this system, the insured pays a premium to the insurance company as the insurer, and in return the insurance company bears certain financial risks according to the provisions of the policy. This concept is in line with the provisions of Article 246 of the Commercial Code (KUHD) of the Republic of Indonesia, insurance is defined as: "Insurance or coverage is an agreement by which an insurer binds himself to the insured by accepting a premium, to provide compensation to him for a loss, damage or loss of expected profits, which he may suffer due to an uncertain event." (Japatani Siregar, 2023)

Historically, conventional insurance has been known since the Babylonian era, around 4,000–3,000 BC, through the Treaty of Hammurabi. Its development continued in 1668 AD with the founding of Lloyds of London in a London coffee house, which became a pioneer of modern insurance. In Indonesia, insurance was introduced during the Dutch colonial period, along with the development of the plantation and trade sectors managed by the Dutch.

Conventional insurance has a legal basis derived from human thought, philosophy, and culture, and operates under positive law. However, because it is not based on divine law, its practice often contains elements of uncertainty. From a sharia perspective, conventional insurance contracts are considered to contain elements of gharar, usury, and maysir due to the lack of clarity regarding the payment amount, the benefits to be received, and the duration of the payment and coverage. (Mukhsinun, 2019)

B. Basic Concepts and Principles of Islamic Insurance

In the Encyclopedia of Islamic Law, insurance is defined as an agreement between two parties, in which the first party is obligated to pay a premium, while the second party is obligated to provide assistance in the event of a specific event, as agreed upon. From a muamalah perspective, sharia insurance is understood as a mechanism for mutual risk sharing between individuals. Each party assumes the responsibility for the other party's risk, which is implemented based on the principle of mutual assistance in good deeds by pooling funds to cover the risk.

The National Sharia Council explains that Islamic insurance (ta'min, takaful, or tadhâmun) is an effort to protect and help each other among a group of people or parties through the management of funds in the form of asset investments and/or tabarru' funds, to face certain risks with contracts in accordance with sharia principles. This concept is based on Surah Al-Ma'idah verse 2 of the Quran, which emphasizes the command to help each other in virtue and piety, and the prohibition of helping each other in sinful and transgressive acts. (Sulaeman, 2023)

In line with this principle, the National Sharia Council of the Indonesian Ulema Council (DSN-MUI) through Fatwa No. 21/DSN-MUI/X/2001 Article 1 paragraph (1) stipulates that sharia insurance is an effort to protect and help each other among a number of people or parties through investments in the form of assets and/or tabarru' to face certain risks with sharia-compliant contracts. (Kurniawan, 2023)

The concept of takaful, which forms the basis of Islamic insurance, is also reinforced by a hadith of the Prophet Muhammad (peace be

upon him), narrated by Bukhari and Muslim, which states that the relationship between believers is like a building that strengthens each other. Another hadith also describes believers as one body, where if one part feels pain, the whole body feels it. This principle of mutual assistance in good deeds was later accommodated in Indonesian positive law through legislation.

The provisions regarding sharia insurance are legally regulated in Law Number 40 of 2014 concerning Insurance. Article 1, Chapter I, Number 2, states that sharia insurance is a collection of agreements that include agreements between sharia insurance companies and policyholders, as well as agreements between policyholders, for the purpose of managing contributions based on sharia principles for mutual assistance and protection. This protection is provided through the provision of compensation for losses, damages, costs, lost profits, or legal liability to third parties due to uncertain events, as well as through payments based on the death or survival of the participant with predetermined benefits or based on the results of fund management. (Fauzi, 2019)

C. Fund Management System in Conventional Insurance

Fund management in conventional insurance is based on the principle of risk transfer, where all participant risk is transferred to the insurance company. The premiums paid by the client become the property of the company and are fully managed by the insurer. The amount of benefits received by participants cannot be guaranteed from the outset because they depend on the occurrence of certain events within the policy term, thus containing an element of uncertainty (gharar). (Prahendratno, 2023)

In practice, conventional insurance companies' profits are largely determined by the ratio of premiums collected to claims paid. This mechanism creates a speculative element (maisyr), particularly in life insurance, as the returns to both participants and the company depend on the life or death of the insured. Furthermore, collected premium funds are generally invested in interest-based instruments, making conventional insurance fund management inherently riba (usury).

Conventional insurance fund management is also not under the supervision of a Sharia Supervisory Board, so its operations and investments are strictly subject to positive law and internal company policies. If no claims are filed by the policy's expiration or the insured withdraws, the premiums paid are not refunded and become the insurance company's profit. (Sipa, 2023)

D. Fund Management System in Sharia Insurance

Sharia insurance operates based on the principles of shared responsibility, mutual assistance, and mutual protection among participants. The insurance company manages participants' contribution funds, develops them through halal means, and distributes compensation to participants affected by disasters in accordance with the terms of the contract. Funds used in Sharia insurance come from *tabarru'* funds, charitable funds collected for the common good. (Lestari, 2020)

The use of contracts is the main element that distinguishes Islamic insurance from conventional insurance. The contracts in Islamic insurance are designed to avoid the elements of *gharar* and *maysir*, which scholars have questioned in conventional insurance practices. Therefore, Islamic insurance applies a risk management concept that complies with Islamic law.

Sharia insurance employs the concept of risk sharing, where the risk is not transferred to the company but is borne collectively by the participants. The Sharia insurance company acts solely as a claims and fund manager (operator), not as a risk insurer. Claims paid to participants are derived from the participants' own pooled funds, so there is no transfer of ownership of the funds to the company. Contributions paid by participants do not constitute a transfer of funds but remain the property of the participants as owners of the capital. All participants are bound by a contract to assist each other (*ta'awun*) through a *tabarru'* fund mechanism in accordance with sharia principles. (Fauziyah, 2025).

E. Advantages and Disadvantages of Conventional and Sharia Insurance Fund Management Systems

The fund management system is a fundamental aspect of insurance company

operations because it directly relates to the company's sustainability, participant protection, and fairness in benefit distribution. Both conventional and Islamic insurance have their own characteristics in managing participant funds, which ultimately give rise to their respective strengths and weaknesses.

In conventional insurance, the funds paid by participants in the form of premiums become the sole property of the insurance company. The company has full authority to manage, invest, and utilize these funds for operational purposes and business development. This system adheres to the principle of risk transfer, which transfers risk from participants to the insurance company. The primary advantage of a conventional insurance fund management system lies in investment flexibility and the large scale of fund management. Conventional insurance companies can invest premium funds in various financial instruments without Sharia-compliant restrictions, potentially generating higher returns and maintaining company liquidity.

However, the conventional insurance fund management system also has several weaknesses. Participants do not have rights to any surplus funds earned by the company, as the premium funds already belong to the company. Furthermore, from an Islamic economic perspective, conventional insurance fund management contains elements of *riba* (usury), *gharar* (gharar), and *maysir* (gambling), particularly in the investment mechanisms and insurance agreements. This leads to the conventional system being deemed inconsistent with the principles of justice and transparency for Muslim participants. (Dharmawan, 2025)

Unlike conventional insurance, Sharia insurance implements a fund management system based on the principles of mutual assistance and risk sharing. Funds paid by participants do not belong entirely to the company but are classified as *tabarru'* funds, which are used to assist other participants experiencing disaster. The Sharia insurance company only acts as a fund manager (operator) and receives compensation in the form of *ujrah* (cost of capital) according to the agreed contract. The main advantage of this system lies in the principles of justice and equality, where participants have a more equal

position and are entitled to an underwriting surplus if there is excess funds after deducting claims and technical reserves. (Azizi, 2025)

Furthermore, fund management in Islamic insurance is overseen by the Sharia Supervisory Board (DPS) to ensure all investment and operational activities comply with Sharia principles. Participants' funds can only be invested in instruments that are halal and free from usury. This provides a sense of spiritual security for Muslim participants and increases trust in the Islamic insurance system. (Panisa, 2025)

Despite its advantages in terms of principles and ethics, the Islamic insurance fund management system also faces several weaknesses. The relatively smaller scale of the Islamic insurance industry compared to conventional insurance limits operational efficiency and investment diversification. Furthermore, the complexity of contracts and the separation of participant and company funds require a stricter administration system, potentially increasing management costs. Public literacy regarding the concept of Islamic insurance fund management is also relatively low, impacting the growth and optimization of managed funds. (Chong, 2024)

Thus, it can be concluded that conventional insurance fund management systems excel in terms of flexibility and economies of scale, but have weaknesses from a fairness and Sharia compliance perspective. Conversely, Sharia insurance offers a fairer, more transparent, and more Islamic-compliant fund management system, although it still faces challenges in terms of efficiency and industry development. These differences demonstrate that the choice of insurance system is strongly influenced by the economic needs and values held by participants.

IV. CONCLUSION AND SUGGESTIONS

A. Conclusion

Based on the results of the studies and discussions conducted, it can be concluded that the fund management systems in conventional insurance and sharia insurance have fundamental differences in terms of principles, mechanisms, and management orientation. Conventional insurance applies the principle of risk transfer, whereby premiums paid by participants become the property of the insurance company and are managed entirely

for the company's benefit, including investment activities. This system offers advantages in terms of fund management flexibility and economies of scale. However, from a sharia perspective, it contains elements of usury, gharar, and maysir (risk of risk) and tends to be oriented towards company profits.

In contrast, Islamic insurance applies the principle of risk sharing based on the concept of mutual assistance (ta'awun) through the tabarru' fund mechanism. Fund management is carried out separately between participant and company funds, and is supervised by a Sharia Supervisory Board to ensure compliance with Sharia principles. This system emphasizes fairness, transparency, and mutuality among participants, while granting them the right to share in the underwriting surplus in accordance with applicable regulations. However, Islamic insurance still faces challenges such as limited business scale, operational efficiency, and low public literacy levels.

Thus, it can be concluded that conventional insurance and Sharia insurance each have their own characteristics and advantages in fund management. The choice of insurance system is not solely determined by economic considerations but also influenced by the values, principles, and needs of participants, particularly in the context of compliance with Sharia principles.

B. Suggestion

Recommendations Based on the results of this study, it is recommended that insurance companies, both conventional and sharia, increase transparency in fund management and provide clear and easy-to-understand information to participants regarding contribution, investment, and claim mechanisms. Specifically for the sharia insurance industry, efforts are needed to strengthen public literacy and education to increase understanding of the concept of sharia-based fund management. Furthermore, regulators are expected to continue refining policies and supervision to support the growth of a healthy, fair, and sustainable insurance industry. For future researchers, it is recommended to conduct empirical studies using quantitative data to obtain a more comprehensive picture of the performance and

effectiveness of fund management systems in conventional and sharia insurance.

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