

What is so special about Islamic credit cards?

Islamic credit cards operate under different structures in different countries, unlike conventional credit cards. **James Massey** explains why.

A credit card is useful for a number of reasons, not just for buying things when you don't have the money available, such as mail order, telephone orders or internet payments that require the additional security of CVW numbers, but also for transactions such as hotel booking or car hire, which require the ability to take additional charges above the initial amount.

For retail Islamic banks to meet customer needs and provide a full service, there is a need for them to provide Islamic "credit cards". A conventional credit card is not permissible, even if the user is certain that he will pay the bank within the time limit, as the user enters into a contract with the bank and is obliged to pay interest if he delays payment.

So how can we define an Islamic credit card?

Firstly, the card must meet the Shari'ah requirements on lending, which vary from region to region. Effectively, this means it must avoid the three essential prohibitions in Islamic finance: Riba, Gharar and Maysir.

The concept of interest, or Riba as it is known, is clearly proscribed in the Qur'an and the Hadith. So an Islamic credit card cannot apply interest to payments even if the user is late in paying.

Gharar, or uncertainty, is somewhat open to interpretation, but Islamic cards should not involve a charging scheme where the monthly repayment or service charges are variable based on a number of factors.

Maysir or gambling is also prohibited, so apart from preventing access to sites such as online gambling, Islamic cards need some other form of insurance cover.

Secondly, an Islamic credit card must work through accepted international payment schemes, such as MasterCard or Visa, and provide facilities that are not available on debit cards such as

CVW numbers for "card not present" transactions and hold amounts. Also, the merchant charges and issuer's fees should not be withheld, which means the acquirer will have to manage the arrears on their books and will be liable to IPS and intra scheme settlements.

Thirdly, an Islamic card should not encourage behaviour that is considered Haraam. The category of Haraam includes all manner of forbidden behaviours, and transactions of an inappropriate nature must be declined immediately by a Shari'ah compliant processing system.

So how can Islamic banks be compliant with the local Shari'ah rules?

Apart from excluding certain types of transactions, there are a number of schemes that are used. A transaction could be executed only by use of the customer's own funds, i.e. providing the money against a savings account to exclude the risk of the per cent accruals. The main problem with these products is that they are not credit cards at all; for all practical purposes, they are debit or charge cards. The customer is getting a short-term loan, which is guaranteed against his account, and it is debited fully at the end of the credit period.

Another way is to base the card on 'Ujra' or service charge. In this case, an annual service charge is levied depending on the credit size. The card works in a similar way to conventional credit cards, however, with no interest charged. It only charges an annual fee, which is payable in quarterly instalments.

Some Malaysian banks offer Islamic credit products including credit cards on the basis of 'Bai' Allnah' contracts, which work on the basis of two back-to-back 'akad' agreements. The first is the bank's agreement to sell an item to the



customer at a pre-agreed price, with the second agreement covering the customer selling back to the bank at a lower price. The difference is the bank's profit on the transaction.

Such products do not pass the test of strict Islamic compliance as practiced in the Gulf and are often criticised for camouflaging interest payments. Plus, they cannot really deal with items such as cash withdrawals, the purchase of services or consumables, as there is no asset for the bank to buy back.

There are also schemes based on the principal of Murabaha, where the bank purchases the required asset or product and the asset is then resold at a higher price to the customer. By paying this higher price through instalments, the customer effectively gets credit without paying interest.

These also have problems with intangibles such as services, cash withdrawals and consumables. To manage these sorts of transactions, a scheme based on Tawarruq is required. The customer with a cash requirement buys an item on a deferred installment payment basis and the customer then immediately resells the item for cash to another part of the bank.

Disclaimer: The writer is general manager, MEA, at BPC Banking Technologies