

1822 - Letters of credit

the question

One of the practices which is well-known in the financial field nowadays is when a businessman wants to import a product, for example, he asks the bank for a letter of credit for a certain amount, either in his own account or from the bank itself, and the bank takes some form of payment for providing this letter of credit. What is the ruling on this?

Detailed answer

Praise be to Allaah, Lord of the Worlds.

Firstly: Letters of credit may be of different types, initial or final. Either type of letter of credit may or may not be covered by the balance in the businessman's account. If it is not covered, then the issuer bears joint liability with the applicant with regard to current and future obligations. This is essentially what is known in Islamic fiqh as *damaan* (liability) or *kafaalah* (sponsorship or surety).

If the letter of credit is covered, then the relationship between the one who is requesting it and the provider (the bank) is that of an agency. Acting as an agent is valid whether or not a fee is paid, so long as the agent relationship serves the interest of the one for whom it is done (in this case the third party from whom the good are being purchased).

Kafaalah (sponsorship) is a voluntary agreement whose purpose is goodwill. The *fuqaha'* have stated that it is not permissible to accept a fee in return for it, because in that case when the sponsor (*kafeel*) receives a sum of money when the credit is paid, it becomes like a loan which brought some benefit to the lender, which is not allowed in Islam [because it is like *riba* or interest - Translator].

Islam Question & Answer

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On this basis, the following is clear:

Firstly: that it is not permissible to charge a fee for issuing a letter of credit – which usually takes into account the amount of money and length of time involved – whether the credit is covered or not.

Secondly: charging administration fees for preparing either type of letter of credit is permissible, so long as the amount charged does not exceed what is usual, whether the letter of credit is wholly or partly covered. In evaluating the administration fee for issuing a letter of credit, it should be taken into account what is actually involved in doing so. And Allaah knows best.