580575 - What are the permissible alternatives to a penalty in the case of delayed payment of a loan?

the question

What are the permissible alternatives to a penalty in the case where a customer delays payment of a loan?

Summary of answer

It is prohibited to stipulate a penalty in the event of any delay in paying back a loan, or a debt resulting from a sale to be paid for at a later date, or any other kind of debt. It is permissible to stipulate that all instalments will become due immediately, or the timescale for payment will be reduced, if the debtor delays payment.

Detailed answer

Praise be to Allah.

I.

It is prohibited to stipulate a penalty in the event of any delay in paying back a loan, or a debt resulting from a sale to be paid for at a later date, or rent, and so on, because stipulating that something be paid in addition to the debt is riba (usury).

The Sahabah gave rulings that giving a gift in return for a loan when the loan is still owed and has not yet been repaid is riba, so how about stipulating that a gift or something extra be given?

The Muslims are unanimously agreed that stipulating that something extra be given when giving a loan is riba.

Al-Buhari narrated in his *Sahih* (3814) that Abu Burdah said: I came to Madinah and I met

`Abdullah ibn Salam (may Allah be pleased with him). He said to me: You live in a land where riba is prevalent. If someone owes you something and he sends you a gift of a load of straw, or a load of barley, or a load of alfalfa, do not accept it, for it is riba.

Alfalfa is a plant that is eaten by livestock.

Al-Qurtubi (may Allah have mercy on him) said in his *Tafsir* (3/241): The Muslims are unanimously agreed, based on what is narrated from their Prophet (blessings and peace of Allah be upon him), that stipulating that something extra be given when lending is riba, even if it is a handful of animal feed, as Ibn Mas`ud said, or it is a single grain. End quote.

What was said about loans may also be said about all other kinds of debt.

It says in a statement of the Islamic Fiqh Council regarding sales to be paid for in instalments:

3.If someone who bought on credit is late in paying an instalment on the appointed day, it is not permissible to force him to pay more than he owes on the basis of a prior stipulation or otherwise, because that is riba and is prohibited.

End quote from *Majallat al-Majma`* (issue no. 6, vol. 1, p. 193).

And it says in a statement of the Council regarding credit cards: It is not permissible to issue an unloaded credit card or to use such a card if there is a stipulation that interest will be charged, even if the applicant is determined to pay within the grace period when no interest is charged.

End quote from *Qararat wa Tawsiyat Majma` al-Fiqh al-Islami*, p. 187.

Please see question no. 177994.

II.

One of the permissible alternatives to protect oneself from the risk of delay in payments is to stipulate that there should be collateral or a guarantor, and to agree that the lender will sell the collateral in order to pay off the debt, or will ask the guarantor to pay off the debt, if the debtor

defaults on the debt.

It says in *Al-Ma`ayir ash-Shar`iyyah li Hay'at al-Muhasabah*, p. 115: The financial institution may stipulate permissible ways of guaranteeing payment in murabahah (profit-sharing) contracts, for the one who requested the purchase. That includes the financial institution seeking a guarantor, or keeping the customer's investment money as collateral, or giving as collateral any valuable movable property or real estate, or the item of the contract being official collateral, without allowing him to take ownership of it (until the debt is paid), or after he takes ownership, and releasing the collateral gradually, according to how much he has paid of its price.

III.

Another permissible alternative is stipulating that all instalment payments become due immediately, or the interval between payments is to be reduced, if the borrower delays payment.

So it is permissible to say that all instalments will become due if there is any delay in payment, and the borrower should be required to pay all that he owes in one payment in that case.

And it is permissible to say that if there is any delay in payment, the period for instalment payments will be reduced from two years to one year, and the monthly instalment will be doubled, for example.

That is because the time for repayment is the right of both parties, so it is permissible for them to agree to cancel it [and pay off the entire price immediately], or to reduce the time for repayment.

It says in a statement of the Islamic Fiqh Council regarding sales to be paid for in instalments:

5.It is permissible, according to Islamic teachings, for the one who sells items to be paid for in instalments to stipulate that all instalments will become due before the agreed-upon time if there is any delay in payment of one or more instalments, so long as the debtor accepted this stipulation when drawing up the contract. End quote.

And it says in *Al-Ma`ayir ash-Shar`iyyah*, p. 215: It is permissible for the financial institution to

stipulate that the customer must pay all instalments before they are due, if he refuses or delays paying any one instalment for no good reason. End quote.

And it says (p. 213): The evidence for it being permissible to stipulate that all instalments must be paid before they are due in the event of any delay is the words of the Prophet (blessings and peace of Allah be upon him): “The Muslims are bound by their conditions.” Moreover, the purchaser agreed to the deferred payment schedule, and he has the right to cancel it [and pay what he owes immediately] or to waive his consent in the event of any delay in payment. End quote.

IV.

Another acceptable alternative is stipulating that the deal will be annulled if the debtor defaults on repayment or delays deliberately.

So the alternatives to stipulating a penalty in the event of delay are many, as follows:

1. Stipulating that something be given as collateral.
2. Stipulating that there should be a guarantor.
3. Stipulating that all instalments will become due immediately, or the time scale will be reduced, if the debtor delays payment of an instalment.
4. Stipulating that the contract will be annulled if there is any default on payment or deliberate delay.

And Allah knows best.