

## CONTRACTUAL RELATIONSHIP BETWEEN PARTIES TO CREDIT CARD TRANSACTIONS

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### INTRODUCTION

To identify the relationship between the contracting parties in credit cards transaction will guide us in knowing the types of contract that exist among each other. The type of relationship between the contracting parties is one of the most important aspects of the credit card transaction. In view of the above, this paper will consider the nature of the relationship between the contracting parties to the credit card transaction i.e. the local issuer, the card holder and the merchant from both the Islamic and conventional points of view. In addition to that, it will examine the termination of the credit card contract between the card holder and the local issuer and its legal implications and consequences.

There are many types of credit cards with regard to the parties involved in their transactions. They include the following:

- i) **"Four-party credit card"** which consists of the international provider of the card, the local issuer, the card holder and the merchant;
- ii) **"Three-party credit card"** which consists of the local issuer, the card holder and the merchant;
- iii) **"Two-party credit card"**. Occasionally, the parties may be confined to only two i.e. the card holder and the merchant in the case of large department stores issuing cards that can only be used at their outlets.<sup>1</sup>

However, this paper will only cover the **"three-party card"**. For easy clarification, below is the short definition of the parties involved in the credit cards transactions.

**Card Issuer** means "the financial institution or business organization, or its duly authorized agent, which issues a credit card to their customers (credit card holder/debtor)".<sup>2</sup>

**Card Holder** is "any person to whom a credit card is issued or any persons who have agreed with the card issuer to pay obligations arising from the issuance of a credit card to another person".<sup>3</sup>

**Merchant** means "every person who is authorized by the card issuer or a participating party to furnish money, goods, services or anything else of value upon presentation, of a credit card by a card holder".<sup>4</sup>

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<sup>1</sup> Muhammad, A. U. *al-Jawanih al-Shar'iyah wa al-Masrafiyyah wa al-Muhasabiyyah Libitaqat al-I'timan*, Itrak, Cairo, Egypt, 1997, pp.27-28

<sup>2</sup> Irving J. Sloan, *The Law and Legislation of Credit Cards: Use and Misuse*, Oceana Publications Inc., London, 1987, P.104

<sup>3</sup> Ibid. p.21

<sup>4</sup> Ibid. p.104

Most credit cards usually require the above mentioned three parties in order to perfect the transaction. The contract between the card issuer and the card holder will however, be frozen or remain meaningless until the card holder starts using it. Therefore, using the card is an essential aspect of the contract. However, the question here is whether the agreement between the parties is considered as three different agreements or one? There are two conventional views regarding this issue which can be summarized as below.

According to the Consumer Act 1974 of the English law, the credit card agreement is not one but rather three different agreements. Firstly, it is an agreement between the debtor (card holder) and the creditor (card issuer), secondly, it is an agreement between debtor, creditor and merchant and thirdly, it is an agreement between the creditor and the merchant.<sup>5</sup>

All the three agreements should be looked at as three different agreements and, therefore, the conditions of each contract or agreement should be complied with in whole. This principle is further explained in *Re Charge Card Services Limited* (1986)<sup>6</sup> where Millett J. stated: upon the use of the card, three separate contracts came into operation:

- a) the contract of supply of the goods and/or services between the retailer (merchant) and the card holder;
- b) the contract between the retailer (merchant) and the card issuing company under which the retailer agrees to honour the card, and
- c) the contract between the card issuer and the card holder, under which the card holder agrees to reimburse the card issuer for the payments made or liabilities incurred by the card issuing company to the merchant as a result of the card holder's use of the credit card.

Therefore, there are, three separate contracts, each party being a party to two of the three contracting parties of the credit card transaction.<sup>7</sup>

Conversely, the American Law, considered the credit card agreement as one agreement consisting of three parties; that is, the card issuer, the card holder and the merchant. This was understood from the American Law where it considered the issuance of the card from the bank to the card holder as just an "offer of credit". That offer is only considered as accepted when the card holder uses it to pay for his purchase from the merchant.<sup>8</sup>

With regard to the classification of the relationship between the contracting parties from the Islamic law perspective, there are disagreements between the jurists as to whether the agreement between the parties is considered as one agreement or more. However, the preferable view is that the agreement between the parties is considered as three agreements. This is due to the difficulty of adaptation of the entire credit card scheme under one contract in Islamic law.<sup>9</sup>

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<sup>5</sup> Jones, S. A. *The Law Relating to Credit Cards*, BSP Professional Books, London, 1989, p.73

<sup>6</sup> (1986) 3 All ER, 289, (1986) 3 WLR 697

<sup>7</sup> Ibid, p.289 and p.697 respectively

<sup>8</sup> Ahmed, A. *The Legal Regim of Payment Cards, A Comparative Study Between American, British and Kuwait Law with Reference to Credit Cards*, A PhD Thesis in the Law Faculty, England, University of Exeter, 1990, p.356

<sup>9</sup> Abd al-Wahhab Abu Sulayman, *al-Bitaqat al-Bankiyyah al-Iqradiyyah wa sahb al-Mubashir min al-Rasid*, (Second edition), Dar al-Qalam, Damascus, 1424H/2003, p.133

## RELATIONSHIP AND RESPONSIBILITIES BETWEEN THE CARD ISSUER AND THE CARD HOLDER

Under this topic, we are first going to discuss the nature of the relationship that exist between the card issuer and the card holder, followed by the nature of the responsibilities of the two parties to one another in a credit card transaction.

The nature of the relationship between the card issuer and the card holder from the conventional law perspective is that of a creditor-debtor relationship. The issuing bank is the creditor and the card holder is the debtor.<sup>10</sup> This principle has been expatiated by Sally Jones in her book *The Law Relating to Credit Cards* as she mentioned that in the typical credit card situation, there are three different contracts:

- a) the credit contract between the card issuer (creditor) and the account holder (the debtor);
- b) the supply contract between the merchant and the debtor; and
- c) the indemnity contract between the creditor and the merchant.<sup>11</sup>

From the Islamic law perspective, on the other hand, there are differences of opinion among the Muslim scholars about the nature of this relationship. Here is the summary of their views:

- a) the relationship between the card issuer and the card holder is a guarantee relationship (*kafalah*) whereby the card issuer agreed to guarantee the card holder for any purchase made via the credit card.<sup>12</sup>
- b) the relationship between the card issuer and the card holder is a transfer of debt (*hawalah*) relationship where the card holder (*muhiil*) has transferred the merchant (*muhiillahu*) to the card issuer (*muhal 'alaihi*) for collecting and receiving his rights from the card holder for the purchase or services rendered to him.<sup>13</sup>
- c) the relationship between the card issuer and card holder is a creditor-debtor relationship (*'aqd qard*) whereby the card-holder is allowed to buy and withdraw up to the limit-agreed upon, provided he does not pay interest in return for the loan because every condition (*shart*) that stipulates excess is forbidden and sinful (*haram*). However, issuing charges are allowed as they are paid in exchange for services and other related expenses.<sup>14</sup>

From the above explanation, it is clear that the card holder refers the merchant to the card issuer for the payment of price of the service/goods by transfer of debt. The card holder's pledge and liability to pay would thus be discharged in *Shari'ah*, and the card issuer would be obliged to pay the whole debt. This means that the relationship between the card holder and the card issuer from the card holder's point of view is that of an absolute transfer of debt

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<sup>10</sup> Diamond, *Commercial and Consumer Credit*, p.329

<sup>11</sup> Jones, *The Law Relating to Credit Cards*, p.73

<sup>12</sup> *Kafalah* is an Arabic term which means to add an obligation to an existing obligation in respect of a demand for something. Wazarat, A, *al-Mausitat al-Fiqhiyyah*, Dar al-Safat, Kuwait, 1416/1995, Vol.34, p.289

<sup>13</sup> Kamal, H. N. 1421H/2000. Twelfth Session, *Fiqh Academy of the Organisation of Islamic Conference*, Riyadh, Saudi Arabia. *Bitiqat al-I'timan*, p.463. Ali al-Qari, 1412H/1992, Seventh Session of the *Fiqh Academy of the Organisation of Islamic Conference*, Jeddah, Saudi Arabia, *Bitiqat al-I'timan*, p.389

<sup>14</sup> Ghuddah, A. S. 1412H/1992 Twelfth Session, *Fiqh Academy of the Organisation of Islamic Conference*, Riyadh, Saudi Arabia. *Bitiqat al-I'timan*, p.463

(*hawalah mutlaqah*) i.e. when someone transfers the debt owed by him to another, and the person who bears the obligation to pay the debt accepts to transfer the debt due to him. This is acceptable to the Hanafis<sup>15</sup> but not to other jurists on the basis of the *Hadith* which stated: "Whoever is asked to collect his debt from a third party who is capable of payment, he should do it".<sup>16</sup>

Therefore, this relationship of the card issuer, in its origin is that of guarantee, i.e. the card issuer is a guarantor of the card holder towards creditors whether merchants or other suppliers, and relationship between the card issuer and the merchant is that of security, even before incurring the debt, which is permissible according to the majority (*Jamhur*) except for the Shafi'is.<sup>17</sup> However, Shafi'is and some contemporary scholars, such as Wahbali al-Zuhayli, consider it as security for something that is not in existent yet and thus Islamically not tenable. This is due to the fact that guarantee, as they view it, is a mere contract of donation (*tabarru'*), whereas the card issuers aim at making profits from such contracts either by usurious interest in cases of late payments by the card holder, or from the merchant against marketing and brokerage which are not within the logic of guarantee or donation contracts in *Shari'ah*.<sup>18</sup>

Consequently, the card holder's relationship with the card issuer cannot be characterized as that of agency with commission (*wakalah 'ala 'ajr*), as the card holder does not give the card issuer a proxy within the legal and objective meaning of agency, and does not pay the card issuer for acting in the capacity of a commission agent. Nevertheless, the relationship within the meaning of agency when an Islamic Bank (card issuer) pays on behalf of his principal (the card holder) the amount required, if that amount is backed or covered with such credit as is sufficient to meet the payment. Similarly, al-Zuhayli is of the view that the relationship between the card holder and card issuer in Islamic *Fiqh* is that of transfer of debt as it is considered as a contract of donation-cum-contract of guarantee.<sup>19</sup>

## RESPONSIBILITIES OF THE CARD ISSUER AND CARD HOLDER TOWARDS EACH OTHER

It should be noted that, the existence of the creditor-debtor relationship between the card issuer and the card holder obliges the card issuer to lend the agreed sum to the card holder (debtor) under the terms conditions of the contract.

Considering a credit card agreement, the card issuer obliges to issue a card to the card holder on production of which the card-holder may have goods, services or cash. Normally, this is not expressly provided for in the agreement, but implied based on the common understanding of the parties. It would appear that it is not common for the card issuer to be under any obligation to issue a card and he may reject any application for card with or without giving reasons. However, once the

<sup>15</sup> Al-Zuhayli, *Bitiqat al-I'timan*, P.12. see also Abu Sulayman, *Bitiqat al-Bankiyyah* P.136. this is also the views of some scholars such as Shaikh Hasan al-Jawahiri, *Bitiqat al-I'timan* a paper presented at the Fifteenth Session, *Fiqh* Academy of the Organisation of Islamic Conference, Muscat, Oman, 6<sup>th</sup>-11<sup>th</sup> March, 2004. P.8

<sup>16</sup> Al-Kasani, A. B. *Bada'i' al-Sana'i' fi Tarih al-Shara'i'*, Dar al-Kitab al-'Arabi, Beirut, 1402H/1982, Vol.6, P.16

<sup>17</sup> Musnad, Ibn Hanbal, Vol.3 Hadith no.9974, 'Alam al-Kutub, Beirut, 1998, P.618

<sup>18</sup> Al-Zuhayli, *al-Bitaqat al-I'timan*, P.14

<sup>19</sup> Ibid.

card is issued, it is usual for the card issuer to retain ownership of the card and to provide for its return and repossession at any time. Besides that, the card issuer usually has the right to terminate the agreement at any point of time.<sup>20</sup>

It should also be noted that, the card issuer's offer to lend money is treated as a continuing offer to the card holder to borrow up to the specified credit limit. This offer can always be revoked, until it is accepted. Under the terms of the agreement, acceptance will be deemed to be given, in the case of a transaction with a merchant for an amount less than the ceiling limit; otherwise, acceptance will be an actual authorization by the issuer of the particular transaction. From the time the particular transaction is concluded, the card issuer cannot revoke his offer to lend money. The card issuer does not promise the card holder that all merchants displaying the relevant logo will accept credit cards as payment, though it may be a breach of the merchant's agreement with the card issuer for him to refuse to accept a credit card in payment. In fact, there is very little that the card issuer promises to do under a credit card agreement. However, the card issuer is in the business of providing credit and although he might not be under any obligation to extend credit, he will only make a profit if he does so.

Alternatively, the agreement also puts certain responsibilities on the card holder which he has to bear all the time. In addition to that, payment by the card holder of the amount agreed by the parties under the terms of their contract is usually the card holder's main obligation under the agreement. Therefore, payment in accordance with the terms of the agreement will generally result in a discharge of the agreement by proper performance. Therefore, failures to pay will usually constitute a breach of the agreement which may in certain circumstances, justify the card issuer to terminate the agreement.<sup>21</sup>

Consequently, the card holder is also under responsibility to inform the card issuer immediately in the event of loss or theft of the card with the specific method agreed in their agreement. Failure to do so will make him liable for all purchases charged through the use of the card. It should be understood that, as soon as when the card issuer has been informed of the loss or theft of the card by the card holder, responsibility of unauthorized use of the card will be transferred from the card holder to the card issuer whose responsibility will be to inform the merchant of the loss or theft of the card by inserting the card number into the lost or stolen cards list which is routinely sent to the merchant. Upon receiving the said list, including the number of a particular card the merchant should control that number in order to prevent any unauthorized transaction with that card or else he will be liable for the charges encountered.<sup>22</sup>

In other words, the responsibility will be borne by the person who causes harm to others by his mistake or negligence. If the mistake is not caused by any of the parties, then the card issuer will bear the responsibility as one of the industry's risks.<sup>23</sup>

Advisably, the card holder should wisely use the card in accordance with the agreement. Therefore, he should take a reasonable precaution to protect the card from being lost or stolen. But the question that arises is whether the card holder should be responsible for any other use of the card other than his own? To answer this question, there are three situations to be considered:

a) Liability on the card for transactions entered into by the card holder himself,

<sup>20</sup> Jones, *The Law Relating to Credit Cards*, Pp.198-199

<sup>21</sup> Ibid. pp.198-199

<sup>22</sup> Sloan, *The Law and Legislation of Credit Cards: Use and Misuse*, P.15

<sup>23</sup> Ibid.

- b) Liability on the card for unauthorized transactions entered into by the agent and
- c) Liability on the card for transactions entered into by an unauthorized user.<sup>24</sup>

### **Card holder's liability for his use of the card**

It should be noted that, most agreements include the condition that the card holder is liable for all amounts entered on the account between him and the card issuer. Because it is usual for the card issuer to keep the accounting records, the card holder solely rely on the card issuer's efficiency and accuracy and the card holder trusts the particular card issuer to keep proper accounts. Even so, the card holder would be well advised to keep all vouchers relating to credit card transactions and to check each statement as it appears. If the card holder is keeping a close check on the statement of account, it might at least alert him to the possibility of unauthorized items appearing on the vouchers.

Therefore, the agreement may impose a more onerous payment obligation on the card holder. For example, he might be required to indemnify the issuer for any loss suffered by the latter arising from the use of the card or account.<sup>25</sup>

The card holder's payment obligations are, therefore, dependent on the provisions of the agreement and in the case of a credit card transaction. These obligations are usually very general. Limitations on the extent of the card holder's liability are provided for both in common law in the agency's case and under the British Consumer Credit Act 1974.

Each liability that is imposed on the card holder by virtue of the agreement will arise either as a result of the card holder's use of the card by himself or by another person using the card as an agent of the card holder. A person will be liable for the acts of another as his agent if that person is acting on the card holder's directives within his actual or apparent authority. Usually the merchant should not have to bother himself with the question of whether the authorized holder of a credit card is the principal or the agent; in fact, as a general rule, the card does not differentiate between the account holder and the card user. Consequently, there are two situations when a card holder will, prima facie be liable for the use by another of his credit facility.<sup>26</sup>

- (a) where there is a common law agency, where the agent has either express, implied or apparent authority to act on behalf of the principal; and
- (b) where there is a deemed agency, i.e. deemed by statute.

If the card holder (principal) so wish, he may either make a person an authorized user of a card on the principal's account or give authority to another to use the principal's own card. Here, an authorized user would be regarded as having the principal's authority in respect of obligations on the credit agreement. However, currently it is not usually possible for a person to use a credit card in another's name because of the requirement of a signature, but the signature is not essential to liability and even if it is, the card holder may have authorized the agent to sign as the holder. This situation is analogous to that in *Greenwood v. Marlins Bank*<sup>27</sup> where a husband was estopped from denying the bank's authority to debit his account for cheques signed in his name by his wife when she knew that she was forging his signature. In either the case of the authorized user or the person

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<sup>24</sup> Jones, *The Law Relating to Credit Cards*, P.177

<sup>25</sup> Ibid. Pp.177-180

<sup>26</sup> Ibid.

<sup>27</sup> (1933) AC 51

authorized to use the principal's own card, the user would have the principal's authority to use the card and the principal would be estopped as against the card issuer from claiming that the use was unauthorized.<sup>28</sup>

### **Card holder's liability for use of his card by his agent**

Section 83(1), of the British Consumer Credit Act of 1974 lays down the basic rule that a card holder under a regulated consumer credit agreement shall not be liable to the card issuer for any loss arising from the use of the credit facility by another person not acting, or treated as acting, as the card holder's agent. Therefore, a card holder will not be liable and cannot be made liable for any use made of the credit card facility by any third party. However, if the third party is acting, or can be treated as acting, as the card holder's agent; the card holder can be fully liable. If a card holder gives his card and Personal Identification Number (PIN) to a third party with instructions to use it in an (ATM), this would probably be a case of agency. The third party, when he draws money from the ATM would be doing so as agent for the card holder. Difficulties may be encountered in deciding when that agency has expired and whether the third party is "to be treated as acting" as the card holder's agent. It is probable that this is a reference to ostensible authority or agency by estoppel. It would be a question of fact in any given case whether a card holder could be stopped from denying that the third party was his agent, or that, because of the third party's position, it would be thought by those who dealt with him that he did have the authority of the card holder.<sup>29</sup>

### **Card holder's liability for the use of card by unauthorized person**

Unauthorized use of a credit card has been defined by American Truth in Lending Act of 1968 (TILA) as: "use by person other than the card holder who does not have actual, implied or apparent authority for such use, and from which the card holder receives no benefit."<sup>30</sup>

Under TILA, the card holder is liable for its unauthorized use only if the card is an accepted card, and only to the extent of \$50.00. This applies to all credit card holders including corporations as well as individuals, and that cannot be applied in a situation where a card holder voluntarily and knowingly allows another person to use his credit card and that other person subsequently misuses the card. Furthermore, the issuer must give adequate notice to the card holder of the potential liability, and must provide the card holder with a self-addressed prestamped notification to be mailed by the card holder in the event of the loss or theft of the credit card, and the unauthorized use of the credit card must occur before the card holder has notified the issuer that an unauthorized use of the credit card has occurred or may occur as the result of loss, theft or otherwise. The card issuer is also required to provide a method whereby the user of such a card can be identified as the person authorized to use it. For the purposes of determining whether the card issuer has been properly notified, a card holder notifies the card issuer by taking such steps as may be reasonably required in the ordinary course of business to provide the issuer with the pertinent information whether or not the issuer received such information.<sup>31</sup>

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<sup>28</sup> Jones, *The Law Relating to Credit Cards*, Pp.177-180

<sup>29</sup>Peter E. Sayer, *Credit Card and the Law: An Introduction*, Fourmat Publishing, London,1988, P.104

<sup>30</sup> Sloan, *The Law and Legislation of Credit Cards*, P.20

<sup>31</sup> Sayer, *Credit Card and the Law*, Pp.18-19

In any action by the card issuer to enforce liability for the use of a credit card, the burden of proof is on the issuer to show that the use was authorized, or that the conditions of liability for the unauthorized use have been met. Finally, these provisions do not impose on a card holder for the unauthorized use of a credit card beyond his liability for such use under other applicable laws or under any agreement with the issuer.<sup>32</sup>

## **RELATIONSHIP AND RESPONSIBILITIES BETWEEN THE CARD ISSUER AND THE MERCHANT**

First and foremost, we explain the relation between the card issuer and the merchant then followed by their responsibilities to one another within the transaction. The relationship between the merchant and the issuer from the conventional law point of view is generally "a purely business arrangement with both parties acting independently and for their own interests."<sup>33</sup>

. However, it would appear that the relationship between the merchant and the card issuer is that of creditor (merchant) and debtor (card issuer). The merchant is a person who was entitled to expect payment at the time of the transaction with the card holder but who has agreed to postpone payment. Moreover, the merchant pays for this privilege by providing the issuer with time to pay. Hence, it could be said that the merchant does not provide credit either, partly because he has agreed to accept the substitute method of payment as satisfying the debt. Therefore there is no debt and there can be no deferment of debt necessary to the concept of credit and partly because the terms of the merchant's contract with the creditor differ from those between the merchant and debtor. Whilst the merchant is entitled under the contract with the debtor to immediate payment, under the contract with the creditor he is only entitled to payment after complying with certain conditions, e.g. returning the sales voucher etc. In these circumstances, the debt is not even due until these conditions are complied with and, therefore, there can be no deferment. Of course, if credit was provided under a contract by the merchant to the issuer, this would not be credit under a credit card agreement but a quite separate type of agreement and it would be regulated by the Consumer Credit Act 1974 because the issuer, who would be the debtor in such an agreement, is likely to be a company.<sup>34</sup>

Sometimes, a merchant could be the card issuer's agent and vice versa but that will depend on the terms of their agreement. If there is an agency between the parties where the merchant is the card issuer's agent, any transaction entered into with a card holder by the merchant in his capacity as agent would be a transaction which only the issuer and card holder would be parties effectively making this a two-party agreement. Similarly, if card issuer were the merchant's agent, any credit agreement entered into with a card holder by the card issuer in his capacity as agent would effectively be made between the merchant and the card holder.<sup>35</sup>

With regard to this relationship from the Islamic law perspective, on the other hand, there are differences of opinion among the Muslim scholars as to which transaction under Islamic law would be the fitting basis of this relationship. While some scholars considered it as an agency relationship (*wakalah*) others see it as transfer of debt (*hawalah*), yet another group are of the view that it is brokerage

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<sup>32</sup> Ibid.

<sup>33</sup> Jones, *The Law Relating to Credit Cards*, p.279

<sup>34</sup> Sayer, *Credit Cards and the Law*, Pp.78-79

<sup>35</sup> Ibid. P.279



(*samsarah*) relationship and so on.<sup>36</sup>

However, it is submitted that this relationship is actually a mere commercial relationship, based on agency with commission (*wakalah 'ala 'ajr*), where the card issuer is considered as an agent of the merchant in collecting payments of the goods and services provided for the card holder and crediting them to the merchant's account. The card issuer is also an agent of the merchant for withdrawing from the merchant's account any sums owing for returned goods, and this is what is clear from the relationship. Jurists have permitted agency by agreement with or without commission.<sup>37</sup>

The card issuer would be entitled to a commission from the merchant in exchange for sending customers or clients (card holders) to him, for promoting the merchant's products and services, and for collecting their payments. This commission charged by the card issuer on the merchant is in the form of deductions from the prices of the sold products, and is not an unearned increment, excess or interest. Thus, there is no usury (*ribah*), involved. It is also not taken from a discounting (*da'wa ta 'ajjal*) perspective, i.e. to discount the debt for early payment' to be made because the payment/settlement by the guarantor bank of the card is prompt (immediate or instantaneous), as and when the proper and valid selling vouchers are surrendered or handed over.<sup>38</sup>

## RESPONSIBILITIES OF THE ISSUER AND THE MERCHANT TOWARDS ONE ANOTHER

The agreement between the merchant and card issuer is governed by the general principles of the law of contract. However, the contract between the card issuer and the merchant is likely to be in writing and it may be on the card issuer's standard terms. The main areas for negotiation between the card issuer and the merchant are the commission or discount, the ceiling limit for authorization of transaction and whether or not the merchant can enter into a transaction when a card is not produced.<sup>39</sup>

Under the merchant's agreement with the card issuer, the latter is required to maintain a record of all the transactions between him and the merchant and to pay accordingly. The merchant agrees to pay a charge for his participation in the scheme and deduct a percentage as agreed from the face value of all sales vouchers. The merchant also agrees to honour all the conditions of the agreement and the card issuer's current operating terms which may vary from time to time. The merchant is obliged to display the relevant credit card logo in a place visible to the public and any other promotional literature distributed from time to time.<sup>40</sup>

The merchant is required to accept all valid and current credit cards issued by the card issuer which are properly presented by the card holders and is not able to impose any minimum financial limit on use of the card nor to require the card holder to pay more than an equivalent cash transaction. The merchant must agree

<sup>36</sup> See the discussions of scholars of the *Fiqh* Academy of the Organization of Islamic Conference on the contractual relationship between the issuer (creditor) and the merchant at the seventh session held in Jeddah, Saudi Arabia, pp.652-682

<sup>37</sup> Al-Zuhayli, "*Bitaqat al-I'timan*" P.14

<sup>38</sup> Abu Sulayman, *al-Bitaqat al-Bankiyyah*, P.218

<sup>39</sup> Jones, *The Law Relating to Credit Cards*, P270

<sup>40</sup> Ibid, P271

to abide by the card issuer's ceiling limit imposed on that outlet. The issuer usually reserves the right to vary the ceiling limit even to nil and this can be done at any time. The merchant agrees only to use the card issuer's vouchers for purchases and refunds and to use the equipment supplied by the card issuer. The merchant is obliged to submit all sales vouchers to the card issuer within a specific period, usually five working days, and if presenting sales vouchers to the issuer, the merchant warrant that

- (i) all statements of fact contained therein are true,
- (ii) that the merchant has supplied the goods or services as specified in the voucher and at the price stated which is a price not greater than the merchant's normal price for those goods or services, and
- (iii) that no other sales voucher has been or will be issued on the same day in respect of the same goods or services.<sup>41</sup>

The merchant must agree to authorize his bank to debit his account in respect of any sums owing to the card issuer and latter agrees to credit the merchant's account with the face value less the discount of all valid vouchers duly presented. The merchant undertakes to notify the card issuer of any change of bankers.<sup>42</sup>

A voucher will usually be invalid if

- (a) the transaction is illegal or of no legal effect,
- (b) the signature on the voucher is incompatible with that on the card,
- (c) the customer's sale voucher is different in any respect from that presented to the bank for payment,
- (d) the card has expired, is out of date or not yet valid,
- (e) the card is void on the company's list,
- (f) the merchant's normal price is higher than the price charged,
- (g) where authorization has not been obtained in circumstances where authorization is required,
- (h) if deviation is made by the merchant in any way from the terms of the agreement or from the card issuer's current operating instructions,
- (i) where for any reason the voucher is incomplete,
- (j) failure of the merchant to present the vouchers to the card issuer within the prescribed time period,
- (k) if petition has been presented for the merchant's liquidation or the merchant has become insolvent or a receiver has been appointed by the court,
- (l) where the card issuer has exercised his rights under the agreement, e.g. in case of breach of agreement by the merchant or where the card issuer is of the opinion that the merchant's financial condition may affect the merchant's ability or willingness to comply with all the terms of the agreement in the contract.<sup>43</sup>

When the card issuer has no liability to pay out on any invalid vouchers, even though a voucher is invalid the card issuer reserves the right to pay out on that voucher without prejudice to his legal rights. Moreover, the card issuer may subsequently treat the voucher as invalid. Similarly, the card issuer is not obliged to notify the merchant whether a specific voucher is valid or invalid in their face value. Nevertheless, it is normal for each merchant to agree to indemnify

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<sup>41</sup> Ibid.

<sup>42</sup> Ibid, P271

<sup>43</sup> Ibid. P.272.

the card issuer in respect of any claim, loss or liability incurred by the card issuer arising from or relating to any transaction between the merchant and the card holder. And in case of any dispute between the merchant and the card issuer, the merchant shall prove to the satisfaction of the card issuer that the transaction was authorized by the card holder. Usually, there is a clause permitting the card issuer to vary the terms of the agreement and the operating instructions generally and to vary the commission charge and specifically the ceiling limit.

In a final note, the card issuer has a right of termination, and this is not necessarily limited to cases of breach by the merchant. In fact, it is abnormal for the merchant to have an express right to repudiate the agreement but it would follow that he would have a right to terminate under usual contractual principles if the card issuer were in breach of a condition of the contract.<sup>44</sup>

### **RELATIONSHIP AND RESPONSIBILITIES BETWEEN THE CARD HOLDER AND THE MERCHANT**

It should be noted that, the relationship between the card holder and the merchant is going to be explained first then followed by their responsibilities towards one another in the credit card transactions. The card holder and the merchant's relationship is that of a contract of sale of goods, but the contract is a threefold contract under which the card issuer is responsible for the payment to the merchant in accordance with the terms of the contracts between them and the card holder is not under personal obligation to the merchant for the price of the goods.<sup>45</sup> The nature of this contract is in accordance with the conventional point of view.

In the case of Islamic law perspective, the relationship between the card holder and merchant could be a buying as well as selling relationship of goods and services, or leasing relationship, in hotels, for example, or else, where the card holder refers the merchant to the card issuer to claim payment from him for the purchase of goods and services..<sup>46</sup>

### **RESPONSIBILITIES OF THE CARD HOLDER AND THE MERCHANT TOWARDS ONE ANOTHER**

It should be note that, there are some questions arising from the contractual relationship between the card holder and the merchant of which the most important one is whether or not the merchant is obliged to accept a credit card for payment. Similarly, is the card holder liable to pay the price of the sold goods to the merchant in the event of the insolvency of the card issuer?

In respect of the first question, the normal sense of contract for the sale of goods or services is that the card holder makes the offer to the merchant to purchase the goods and it is left to the merchant to accept that offer or not. If he decided to accept, his acceptance must be unconditional before it is effective to conclude the deal. The merchant's display of a credit card logo in his shop is merely an indication of the his willingness to accept payment in that form, but it does not itself amount to an offer to contract on those terms. Normally, the offer that the card holder makes

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<sup>44</sup> Jones, *The Law Relating to Credit Cards*, P273

<sup>45</sup> Aubrey L. Diamond, *Commercial and Consumer Credit: An Introduction*, Butterworths, London, 1982, P.329

<sup>46</sup> Abu Sulayman, *al-Bitaqat al-Bankiyyah*, P247. See also al-Zuhayli, *Bitaqat al-I'timan*, P.15

when he intends to pay by credit card is identical to the offer he makes when intending to pay by cash.<sup>47</sup>

As soon as the card holder started displaying his credit card at the time of the offer, the merchant will assume that his intention is to pay by use of that card. However, it is submitted that it is not necessary for the merchant to know in advance that the card holder intends to use the card. In case the merchant has accepted the card holder's offer to buy goods, the contract is made and the card holder's tender of a credit card as payment cannot be refused or if it is refused, will amount to a breach of contract either on the basis that the contract includes an implied term that the merchant is willing to accept payment by credit card or there is a collateral contract whereby the merchant has agreed to accept payment by credit card. Payment by card is equal to payment by cash and the merchant is entitled to expect payment in cash and, therefore, payment by credit card is adequate.<sup>48</sup>

This conclusion is somewhat surprising as the merchant, in fact, ultimately receives less from that transaction than he would if payment were in cash. The merchant is reimbursed for the transaction by the card issuer but at a discounted rate which the card issuer regards as his commission. This is the price the merchant pays to give his customer the option to pay by cash or by credit card. The merchant hopes that his display of willingness to take credit cards will increase his turnover such that the commission charged is set off against increased profits.<sup>49</sup>

The second issue to be addressed is whether payment by credit cards is absolute or conditional? The answer to this question can be seen in the case of *Re Charge Card Services Limited* (1986)<sup>50</sup> where it was held by the Court of Appeal that payment by means of a credit or charge card is not conditional but absolute. It is a complete payment by the card holder who is not liable to pay the merchant (garage) if the card is not honoured. Thus, it is the merchant who runs the risk that the card issuer may become insolvent.<sup>51</sup>

## **TERMINATION OF CONTRACT BETWEEN THE CARD ISSUER AND THE CARD HOLDER AND ITS LEGAL EFFECTS**

There are normally two ways to terminate the contract between the card issuer and the card holder:

- a) Fulfillment of all clauses of the agreement and honouring all the obligations by the parties within the period of the contract. That is the normal termination for contracts and agreements.
- b) Breach of a contract by either party.<sup>52</sup>

Furthermore, there are cases of ending an agreement because of death or default. Here are the procedures for their termination.

### **1. Death**

Practically all credit card agreements are not assignable to the card holder and are personal. The facility can be used by the card holder alone. When the card holder

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<sup>47</sup> Jones, *The Law Relating to Credit Cards*, P260

<sup>48</sup> Aboubacar Salihou Kante, *Credit Cards from the Islamic Legal Perspective*, Ilmiah Publishers, Kuala Lumpur, 2006, p.45

<sup>49</sup> Ibid.

<sup>50</sup> (1986) 3 All E.R 289, (1986) 3 WLR 697

<sup>51</sup> Paul, D. *Sale of Goods and Consumer Credit*, (Fifth Edition), Sweet & Maxwell, London, 1996, P.270

<sup>52</sup> Abu Sulayman, *al-Bitaqad al-Bankiyyah*, p.114

dies, it might be thought that this would automatically bring the agreement to an end and allow the card issuer to claim the outstanding balance from the estate of the deceased card holder. This cannot be done without an order of the court.

In the absence of such an order, all the card issuer can do is to send out statements which demand the minimum repayment from the estate of the deceased. The card issuer may also demand, return of the deceased's card and freeze the account, because the card issuer is not prevented from treating the right to draw any credit as restricted or deferred and taking such steps as may be necessary to make the restriction or deferment effective.<sup>53</sup>

## **2. Default**

If the card holder commits a breach of contract and the card issuer wishes to terminate the agreement and demand full repayment, a special procedure must be adhered to. Under normal circumstances, the card issuer would include a provision in the card holder's agreement which states that any breach will give the card issuer a right to terminate forthwith. This is normally done to avoid complex arguments over whether a breach of a particular clause gives the card issuer the right to terminate. However, the position is somewhat altered by the Consumer Credit Act 1974.<sup>54</sup>

Under section 87 of this Act, before an issuer can become entitled by reason of a breach by the card holder to

- (a) terminate the agreement; or
- (b) demand earlier payment of any sum; or
- (c) treat any right conferred upon the card holder as terminated, restricted or deferred;
- (d) enforce any security, a default notice must be served upon the card holder.

The need to serve the notice and go through the procedure does not prevent the card issuer from treating the right to draw upon any credit as restricted or deferred and taking such steps as may be necessary to make the restriction or deferment effective. If a card holder had exceeded his credit limit or breached the agreement in some other ways, the card issuer would not be precluded from immediate freezing of the account and demanding the return of the card. It seems that if the card issuer has the right and wishes to terminate for some reasons other than the card holder's breach, he need not serve a default notice.<sup>55</sup> Section 88 of the Credit Consumer Act of 1974 deals with the content and effects of the default notice.

The notice must specify:

- (a) The nature of the alleged breach;
- (b) If the breach is capable of remedy, what action is required to remedy it and the date before which that action is to be taken?
- (c) If the breach is not capable of remedy, the sum (if any) required to be paid as compensation for the breach and the date before which is to be paid.

Under section 88(2) the same Act, the card issuer must give the card holder at least seven days after the date of the service of the notice to take whatever action is required. It appears that this means seven clear days excluding the day on which the notice was served and the day on which the card issuer proposes to take further specified steps.<sup>56</sup>

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<sup>53</sup> Sayer, *Credit Cards and the Law*, pp.127-128

<sup>54</sup> Ibid, p.128

<sup>55</sup> Ibid.

<sup>56</sup> Ibid, p.129

The question which must be asked is "what breaches the card holder are capable of remedy and what are not?" One would need to look objectively at all the facts. If the card holder is just late with repayments, it is suggested that this is a breach which is capable of remedy. However, if the card holder has given his card to another for purposes of fraud, it could be argued that the breach goes to the very basis or root of the relationship and cannot be remedied. Probably, the test to be applied would be whether the card holder's act has irrevocably destroyed the relationship between himself and the card issuer. Probably, most breaches will be capable of remedy.<sup>57</sup>

### **Legal Effects of Termination of the Contract**

If any of the contracting parties exercises his right to revoke the contract and terminate it, this will put the card holder in the full debt which he has to the card issuer during the use of the credit card. In case of his failure of repayment, the card issuer will have the right to sue him as the card holder is responsible for the use of the card.<sup>58</sup>

### **CONCLUSION**

This seminar paper showed that there are various types of relationships between the parties to credit cards transactions and their contractual obligations towards one another. The relationship between the contracting parties is one of the most important aspects of the credit card transactions. That is why this article highlights all the nature of the relationship between the contracting parties, particularly the local card issuer, the card holder and the merchant from both Islamic and conventional point of view. The paper also manages to examine the termination of the credit card contract between the card holder and the local issuer and its legal consequences.

Even though credit card transactions varies the number of parties involed in their transactions, this paper only cover the "three-party card" transaction i.e., the card issuer, the card holder and the merchant.

Conventionally, the relationship between the card issuer and the card holder is that of creditor and debtor. The issuing bank is the creditor while the card holder is the debtor.<sup>59</sup> There is supply contract between the merchant and the card holder (debtor) and thereis indemnity contract between the card issuer (creditor) and the merchant.<sup>60</sup>

From the Islamic point of view, there are differences of opinion among the Muslim scholars as o the nature of their relationship. According to Hanafi school, the relationship between the card holder and the card issuer from the card holder's point of view is that of an absolute transfer of debt (*hawalah mutlaqah*).<sup>61</sup>

The *Jamhur* are of the opinion that the relationship between the card issuer in its origin is tha of guarantee, i.e. the card issuer is the guarantor of the card holder towards creditor whether merchants or other suppliers and the relationship

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<sup>57</sup> Ibid, P.130

<sup>58</sup> Ibid.

<sup>59</sup> Diamond, *Commercial Law and Consumer Credit*. P.329

<sup>60</sup> Jones, *The Law Relating to Credit Cards*. P.73

<sup>61</sup> Ala' al-Din Abi Bakr al-Kasani. *Bada'I al-Sana'I fi Tartif al-Shariah*. Vol. 6. 1982 p.16

between the card issuer and the merchant is that of security, even before incurring the debt, which permissible in Islam.<sup>62</sup>

The writer is of the opinion that, the card holder's relationship with the card issuer cannot be characterized as that of agency with commission (*wakalah ala 'ajr*), as the card holder does not give the card issuer a proxy within the legal and objective meaning of agency, and does not pay the card issuer for acting in the capacity of a commission agent. However, the relationship comes within the meaning of agency when an Islamic Bank pays on behalf of his principal (the card holder) the amount required, if that amount is backed or covered with such credit as is sufficient to meet the payment. Therefore, the correct position should be the relationship between the card holder and the card issuer in Islamic *fiqh* is that of transfer of debt as it is considered as a contract of donation-cum-contract of guarantee.

Finally, various adaptations may be used to legalize the use credit cards provided that the formula in question does not fall under the prohibited legal rulings.

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<sup>62</sup> Al-Zuhayli, *Bitaqat al-I'timaan*, p.14