FCI

Facilitating Open Account – Receivables Finance

Exploring Cross-Border Opportunities in Islamic Factoring

FCI ISLAMIC
INTERNATIONAL FACTORING

What is **Islamic International Factoring?**

International factoring is the process of purchasing an invoice from an exporter in one country and collecting it later from the buyer/ importer located in another country. The exporter generally receives payment up front from the factor and the source of repayment comes from the proceeds paid by the buyer/importer at the due date of the invoice. Factoring may include a set of trade related services such as: protection against bad debts; collection of receivables; financing and receivables ledger administration. Islamic International Factoring is an International Factoring transaction where at least one factor is an Islamic Financial Institution (IFI).

THE HISTORY

"Islamic banking has the potential to foster greater financial intermediation and inclusion, especially among Muslim populations, over 24% of the global population, that may be under-served by conventional banks, and to facilitate lending in support of small and medium-sized enterprises", says the IMF.

Since Shariah allows trade with people from other religions, it is important that countries adapt their regulatory, supervisory, and consumer protection frameworks to address the unique risks in Islamic finance, and take steps to develop Shariah-compliant financial markets & monetary instruments and strengthen the international architecture for growing cross-border operations.

FCI established a working group with guidance from the Legal Committee, members in UAE and ITFC. The working group researched and prepared a contract to facilitate Islamic International Factoring transactions. The Supplemental Agreement for Islamic International Factoring has been reviewed and revised by Islamic scholars, and during the 50th Annual Meeting, it was approved by the FCI Council in 2018.

> *Islamic International factoring will be a new and fruitful horizon for both Islamic and conventional financial institution members of FCI, creating ever higher trade finance volumes.*
>
> - Yüce Uyanik | FCI Legal Committee

Similarities between "Murabaha" & Factoring

The below similarities make Factoring an acceptable instrument under Shariah law:

- Factors can approve particular orders and sales contracts.
- The factor is the sole owner of the receivable and all rights of the supplier are transferred to the factor.
- The factor has an obligation to pay the purchase price of the receivable to the supplier on any agreed date.
- The receivable is related to a bona fide sale of goods or rendered service.

Key Principles of Islamic finance

The main principles of Islamic finance are:

- Interest (riba) is prohibited in all financial transactions.
- Extreme uncertainty (gharar) is prohibited on the subject contract of the transactions.
- Traded goods, services and activities must be acceptable (halal) to Shariah principles, and unlawful (haram) earnings and expenditures are prohibited.
- The obligations of trust (amanah) and covenants (uqud) must be adhered to, while fraud of giving less than due in measure and weight and unjust enrichment are prohibited (good faith in contracting).

Deviations from the GRIF

The Supplemental Agreement for Islamic International Factoring has only three important deviations from the GRIF:

- As interest is prohibited in Islam, late payments by the Export or Import Factors are subject to a 'late payment amount' to be agreed on by the parties, not to 'interest'.
- As the trade of some goods and services are prohibited in Islam, the product or service related to the receivable must be approved by the other party before the first assignment by the Export Factor.
- Transactions with the prohibition of the assignment are not acceptable.

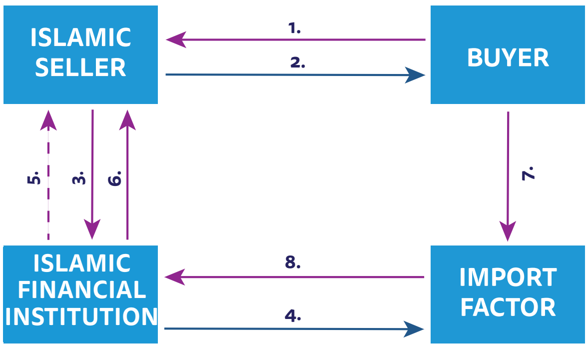
Since there is no reference to financing between the export and import factors in the GRIF, and the import factor is responsible for the payment of full amount of the purchase price of the approved receivable without any discount/ interest, all the other terms and conditions of the GRIF are applicable in an Islamic International Factoring transaction in terms of a 'wakalah/ tamleek' (assignment). It should also be noted that there is no restriction in Islam to prevent trade between Islamic and conventional financial Institutions. Therefore this new opportunity is open to all FCI members.

How does it work?

Islamic International Factoring works on the basis of tamleek, exactly like the assignment in usual international Factoring, with the only difference of signing the Supplemental Agreement to cover the deviations mentioned earlier. If the Export Factor is an Islamic financial Institution, the Import Factor may sometimes receive an order approval request instead of a credit line depending on which Islamic financial instrument is used as a basis for Factoring.

ISLAMIC EXPORT FACTOR

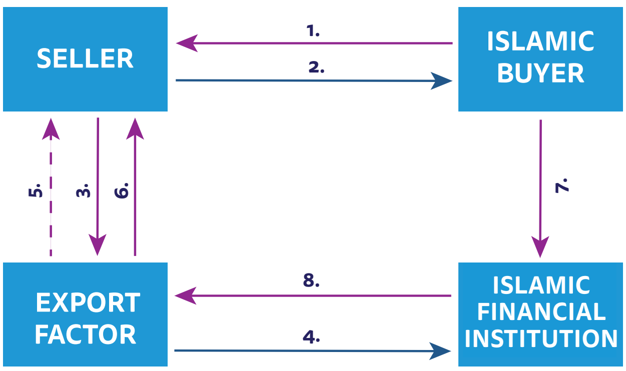
An Islamic International Factoring transaction with an Islamic Export Factor and conventional Import Factor. Whatever the Islamic financial transaction is used as a basis for Islamic Factoring, the Receivable is assigned to the Import Factor under the GRIF and Supplemental Agreement for Islamic International Factoring. For the Import Factor there is no more differences in their action than the deviations listed earlier.



1. Order
2. Delivery of goods and invoice
3. Assignment/sale
4. Assignment under GRIF + Supplemental Agreement
5. Optional Financing under an appropriate Islamic Finance method
6. Payment to the Seller
7. Payment of the Buyer
8. Payment - Commission

ISLAMIC IMPORT FACTOR

The flow of transactions is not different for an Islamic Import Factor. A conventional Export Factor assigns its receivables to the Islamic Import Factor under the GRIF and Supplemental Agreement for Islamic International Factoring on the basis of their conventional Factoring agreement with the supplier. The only restriction for the Export Factor may be the related goods or services that must be agreed on at the time of approval.



1. Order
2. Delivery of goods and invoice
3. Assignment
4. Assignment under GRIF + Supplemental Agreement
5. Optional Financing under a conventional method
6. Payment to the Seller
7. Payment of the Buyer
8. Payment - Commission

Find out more about the benefits of Islamic International Factoring, and how we can help you expand your business into new markets:
www.fci.nl

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