

# Interest on Loans under Qatari Laws

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The main concern derives from the fact that interest is generally prohibited under the Islamic Shariah, which is embedded in many provisions of law in Qatar. For instance, Article 1 of the Qatari Constitution provides that Islam is the State's religion and the Islamic Shariah is the main source of its legislations. Article 1 of the Qatari Law No. 22 of 2004 (the "Civil Code") provides that in the absence of a text of law, the judge has to decide according to the requirements of the Islamic Shariah.

Applying interest and more generally, remunerating a lender which offers a loan to a borrower, is a concept that has commonly been considered as valid and enforceable around the world. However, in the State of Qatar, one needs to differentiate between the loans granted by licensed financial institutions and the loans that are granted by all other parties.

As a general rule, interest on loans other than loans granted by licensed financial institutions is not permitted in Qatar, pursuant to the provisions of the Civil Code.

Article 568 of the Civil Code provides that "If the loan contract included remuneration in excess of the lent monies under the contract, excluding the necessary guarantees securing the lender's right, the remuneration condition shall be void but the contract as whole shall remain valid."

According to the aforementioned Article of the Civil Code, assuming the absence of special banking laws and regulations, loans shall be interest free and the restitution of the principle amount (in the case of a loan of a sum of money) shall be the only obligation of the borrower under the loan.

However, Article 268 of the Civil Code provides that "If the obligation concerns an amount of money which the debtor fails to pay after being notified and the creditor proves that he has suffered damage as a result, the court may order the debtor to pay damages observing the principles of justice". The court may therefore decide that the borrower pays damages as a result of its failure to repay its due debt.

While interest on loans is generally prohibited under the Civil Code when the lender is not a licensed financial institution, the situation is completely different when the loan is granted by a local bank (or a branch of a foreign bank) licensed to conduct banking activities by the Qatar Central Bank ("QCB").

The QCB law No. 33 for 2006 ("QCB Law"), issued two years following the Civil Code, allows banks to apply interest in accordance with the regulations of the QCB.

Chapter two of the QCB Instructions to Banks ("QCB Instructions") also clearly states that licensed banks have the discretionary power to apply or not to apply interest. Therefore, set aside any issues relating to banking monopoly rules in Qatar, a foreign bank which does not have a branch licensed by the QCB to carry out banking activities in Qatar, may find that the interest which is applied on Qatari law governed loans may be invalidated by the local courts. In order to mitigate this risk, such foreign banks entering into transactions with Qatari borrowers are choosing a foreign law to govern their loan documentation and are submitting the disputes arising in connection with their loan to international arbitration or foreign courts.

Despite the QCB Law provisions and the QCB Instructions authorising the application of interest on loans,

the Qatari courts have a very conservative view in respect of interest and default interest application, even for when loans entered into by licensed banks in Qatar. Such conservative view and refusal to admit the right to apply interest and default interest for banks in Qatar, had caused some confusion in the banking sector's business for a few years until the Qatar Court of Cassation, in several rulings in cases brought before the court in 2010 , overruled the decisions of the Court of Appeal which did not uphold the agreement of the parties in respect of application of interest and default interest in a loan transaction between a licensed bank and its customer.

The Court of Cassation mentioned in its decision that loans granted by banks in Qatar were to be considered as commercial acts by nature and that Article 110 of the QCB Law, which states that "QCB has the right to apply interest or revenue to be determined by the QCB on scheduled credit facilities unless the agreement between the lending financial institutions with its customers states otherwise" clearly provided for the right of the bank to apply interest on loans granted to their customers.

The Court of Cassation also clarified that interest could either be "compensatory interest" or "default interest". According to the Court's definition, the compensatory interest applies in return of lending an amount of money to be used by the debtor for an agreed maturity, while default interest shall apply in case of failure by the debtor to pay the due amount of the loan on its due date. In this decision, "compensatory interests" refers to the contractual interest payments agreed between the bank and its customers. The Court of Cassation has also clarified that banks will have the right to claim default interest in addition to compensatory interests even if the agreement between the banks and their clients did not stipulate for the application of such default interest.

Following the decisions of the Court of Cassation, it has become clear that banks which are licensed by the QCB (whether they are local Qatari banks or branches of foreign banks) will be able to enforce the payment of interest and default interest due on their loans to their customers through the Qatari courts. .

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#### **Footnotes:**

- [1] Qatari Court of Cassation, decision of 28/12/2010, Case No 184/2010
- Qatari Court of Cassation, decision of 11/01/2011, Case No 208/2010
- Qatari Court of Cassation, decision of 11/01/2011, Case No 168/2010
- Qatari Court of Cassation, decision of 04/01/2011, Case No 207/2010