DRAFT OF SHARIAH PARAMETERS:

*MURABAHAH PARAMETER*
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1. Overview: Challenge in Implementation of Shariah Rulings

1.1 In response to the need for a conducive, sound and stable Islamic financial environment, local and global Shariah governing bodies have formulated Shariah rulings and expressed Shariah opinions in the form of fatwas, resolutions and policies to be adopted by the Islamic financial industry.

1.2 An equivocal approach in formulating Shariah rulings for a particular product or financial service that has a wide implication across industry and across sovereignty calls for a more systematic Shariah ruling formulation. This is important if consistent Shariah opinions are to be adopted within or across sovereignty that allows comparison of Shariah rulings.

1.3 In implementing Shariah rulings, it is observed that the Islamic financial industry is faced with a number of challenges as follows:-

   a. lack of familiarity and ability to understand Islamic finance concepts;
   b. lack of published references on how to operationalise Shariah approved contracts from Shariah authorities; and
   c. lack of publicly available document on fatwa and Shariah resolutions as a source of reference.

1.4 It is also observed that implementation of Shariah rulings is limited to product approval and not comprehensive across product development and product life cycle comprising product idea generation, monitoring and supervision.
2. Shariah Parameters Initiative

2.1 Bank Negara Malaysia is developing a set of standard guidance document on application of Shariah contracts in Islamic finance operation, referred as Shariah Parameters. The initiative is based on the need to outline the essential features of Islamic financial product based on the underlying Shariah contracts that are endorsed by Shariah boards and adopted by the Islamic financial institutions.

2.2 The Shariah Parameters as standard guidance documents would provide a more comprehensive understanding of the principles and basis of adopting Shariah contracts for Islamic financial products, as well as enabling harmonization of the Islamic financial practices.

2.3 The development of Shariah Parameters is aimed at achieving the following objectives:-
   a. To clarify concepts, principles and conditions of Shariah contracts;
   b. To provide focus on features of Shariah contracts that form the basis of Islamic financial product;
   c. To provide basis for decisions on matters relating to conditions, mechanism and implementation of Shariah contracts;
   d. To facilitate Islamic finance professionals and practitioners to design and develop Islamic financial products; and
   e. To facilitate formulation of policies and guidelines on contracts adopted by Islamic financial service industry

2.4 The Shariah Parameters set out the Shariah requirements for the contracts of Murabahah, Istisna, Ijarah, Mudharabah, Musharakah and Wadiah. A concept paper on the parameters for each of these Shariah contracts will be issued for feedback and comment.
2.5 The concept paper on Shariah Parameters: *Murabahah* Contract set out the Shariah requirements for the application of *Murabahah* contract.

3. Shariah Parameter Methodology

3.1 In preparing the Shariah parameters, the following considerations have been made to institute a methodology to develop the parameters:

   a. Primary sources were given priority over secondary sources in determining the status of a feature or an issue;
   b. Fatwas were obtained to support the essential features of a particular contract; and
   c. Deductive and inductive approaches were adopted in formulating the parameters in the context of Islamic financial products and in meeting the needs of the Islamic financial services industry.

4. Notes to Users of Shariah Parameters

4.1 The Shariah parameter is subject to review from time to time by the Shariah Advisory Council of BNM (SAC). In this respect, relevant Islamic financial institutions are expected to observe the effective implementation date of the Shariah Parameters.

4.2 The parameters would assist users to understand the nature of the contract by understanding the definition, legitimacy as well as the purpose of the contract.

4.3 In the subsequent part, the essential features of the contract are clearly outlined to explain the practices in undertaking the contract. The features include among others the contracting parties, the subject matter, the price or rent where
relevant, profit distribution where relevant, delivery and payment of goods and services.

4.4 The parameters also highlight the operational issues relating to the contract to enable users to be aware of the implication of these issues on the product structure. It is important to note that certain issues involving legal matters, operations and risks were made based on resolutions made by majority opinion whilst other issues may have been based on a minority opinion of the scholars or Shariah boards. Where such issue is not deemed conclusive from the Shariah authority, users are expected to refer to the SAC for further guidance.

5. Applicability

5.1 This concept paper is applicable to:
   a. All Islamic banking institutions licensed under Islamic Banking Act 1983 (IBA);
   b. All banking institutions licensed under Banking and Financial Institution Act 1989 (BAFIA) which participate in Islamic banking scheme;
   c. Development financial institutions prescribed under Development Financial Institutions Act 2002 (DFIA) which provide Islamic financial services; and
   d. All takaful operators registered under Takaful Act 1984 (TA).
APPENDIX

SHARIAH PARAMETERS:
*MURABAHAH CONTRACT*
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1.0 BACKGROUND AND PREamble

Murabahah is a form of trust-sale that aims to finance acquisition of assets on short or long term basis. In a classical Murabahah practice, no financial intermediaries are involved and the customer would purchase an asset from the vendor on cost-plus mark-up basis. Payment were made either on a deferred or cash basis. The asset would have already been owned by the vendor and the purchase price is a mark-up price which is made known before the transaction. In modern Islamic financial practice, Murabahah sale established itself as a mode of asset financing with an agreed and known mark-up. Being the most prevalent financing mechanism in Islamic finance, Murabahah sale instrument has provided a Shariah compliant alternative to “interest-based lending” financing mechanisms. The Murabahah contract has also been applied for taking deposit and raising sukus.

The development of Murabahah from a sale-based transaction to a financial instrument has raised a number of issues in the local and international markets practice. The benefit of the parameter is to provide a more comprehensive and complete understanding of the nature and features of Murabahah contract as guidance to all finance practitioners, finance professionals, academicians, scholars and regulators. Detailed references to specific Shariah fatwas, opinions and standards would facilitate Scholars in Islamic finance to expound further the systematic development of Islamic financial products that adopt the Murabahah contract.
2.0 PURPOSE AND SCOPE

The purpose of this Shariah contract parameter for *Murabahah* is to provide reference on the nature and features of the contract to the Islamic financial services industry. This parameter is endorsed by the Shariah Advisory Council of Bank Negara, Malaysia on [>DATE<]. Specific definition and guidelines on the basis of legitimacy in adopting the *Murabahah* contract are described to facilitate the understanding of the Shariah contract requirements. The features identified in this parameter shall serve to assist the Islamic financial services industry to identify, understand, apply and distinguish the contract from other contracts prevalent in the industry.

The features identified and described in this parameter are extracted from the text of fatwas opined by Shariah boards or committees of financial authorities and financial institutions. For each of the fatwa on a particular conditionality, activity, situation or context relating to the contract, the underlying concept and principle is deduced and stated to guide the application of the *Murabahah* contract.

If a feature of a contract practised is not specified in this parameter and the Islamic financial institutions use an alternative opinion, such feature would require further deliberation by the Shariah Advisory Council of Bank Negara Malaysia to decide on its status.

This parameter also takes into consideration relevant mechanisms and contracts such as *Wa’d, Wakalah, Kafalah* and *Rahn* where relevant. These are identified and proposed as secondary features mentioned in this parameter.

The scope of the parameter is confined to the *Murabahah* contract as endorsed by the Shariah Advisory Council of Bank Negara Malaysia adopted by the Islamic
financial institutions under the purview of Bank Negara Malaysia in the Islamic financial services industry.

3.0 DEFINITION

Murabahah comes from the word ribh which means increase. Technically, Murabahah is the mark-up disclosed to the purchaser as per the seller’s purchase price for a trust-sale of a certain specified asset, excluding monetary assets including debt. Murabahah sale may be contracted either in the form of cash or deferred payment.

In the Islamic financial services industry, Murabahah is adopted in a transaction known as Murabahah to the Purchase Orderer (MPO) whereby three parties are involved, namely the Islamic Financial Institution (IFI), the supplier and the purchase orderer (customer). The Murabahah credit sale of a specified asset by an IFI to the purchase orderer (customer) is at a disclosed mark-up price based on the IFI’s cost of financing the purchase.

For the purpose of this parameter, the technical definition of Murabahah is Murabahah to the Purchase Orderer. In order to avoid ambiguity, this Murabahah parameter is meant only for the purpose of financing acquisition of assets. Murabahah contract which is meant for cash financing known as Tawarruq is not within the scope of this parameter. This definition also excludes monetary assets including debt.
Essential pillars of a sale contract, which are: legal capacity of contracting parties, offer and acceptance, lawful and existing subject matter and price known with certainty, apply to Murabahah to the Purchase Orderer.

From an operational perspective, MPO involves four significant stages which are: customer order with Wa’d or promise to purchase, acquisition at known and agreed cost, sale at mark-up and deferred payment with security. However, various other applications of MPO may be formalized based on the specified technical definition of MPO.

Illustration 3.1: Murabahah Financing

A purchase orderer applies to an IFI for car financing under a Murabahah sale contract. The IFI does not essentially have the car but will, upon the promise of the purchase orderer to purchase the car on a mark-up basis, purchase the car from a third party, i.e. the supplier. The IFI purchases the car from the supplier, then, sells it to the purchase orderer on a deferred payment basis. The difference between the purchase price paid by the IFI to the supplier and the sale price that the IFI is selling to the purchase orderer is a mark-up for the IFI. For example, the financier purchases the car from the supplier at RM100,000 and sells on credit to the purchase orderer at RM120,000 payable in 5 years. While the seller earns trading profit, the financier earns the financing profit through a mark-up sale.
4.0 LEGITIMACY OF MURABAHAH CONTRACT

The legality of Murabahah is deduced from the Quran, the Sunnah of the Prophet Muhammad (SAW), the consensus of the Muslim jurists and Qiyas (analogy).

4.1 THE QURAN

The Quran generally allows the sale contract. Among others, the Quran says to the effect that “... Allah permitted trade and prohibited usury”. (2:282)

4.2 THE SUNNAH OF THE PROPHET MUHAMMAD (SAW)

There is no direct juristic authority from the Sunnah of the Prophet (SAW) on the legitimacy of Murabahah sale. It is deemed permissible based on the general permissibility of sale in Islamic law. The Prophet Muhammad (SAW) is reported to have said: “The best earning is what man earns with his own hands and from a permissible trade”. (Narrated by Hakim)

4.3 THE IJMA’ OF THE MUSLIM JURISTS

It is noted that people have inherited these transactions (Murabahah) for ages without any objection and that would constitute consensus (Ijma’) on permissibility of Murabahah.
4.4 ANALOGY (QIYAS)

Since the Prophet Muhammad (SAW) has approved the Tawliyah sale (sale based on cost price), the sale on mark-up will be equally permissible on the basis of analogy on the Tawliyah sale. The determination of cost and making it known to the buyer are common in both the Tawliyah and Murabahah sale.

5.0 FEATURES OF MURABAHAH CONTRACT

Murabahah is a contract that comprises several principal features namely price of Murabahah sale, asset of Murabahah sale, duty of full disclosure and Wa’d (promise to buy).

5.1 PRICE OF MURABAHAH SALE

5.1.1 The basis of Murabahah sale price shall be determined based on the acquisition cost with a disclosed added mark-up amount or percentage to be determined upon concluding the Murabahah contract.

5.1.2 The mark-up shall be determined based on a mutual agreement between the IFI and the purchase orderer.

5.1.3 The mark-up, either in a form of value or percentage of agreed cost shall be determined and specified at the conclusion of the Murabahah contract prior to the day of the delivery. Any benchmark adopted is specified to determine the mark-up at the conclusion of contract.
5.1.4 The determination of the mark-up may either be based on an agreed percentage of agreed cost or specified amount for a known and agreed currency.

5.1.5 The agreed mark-up that is determined shall not be subjected to price variation or affected by currency fluctuation as payment due is pre-determined at agreed currency.

5.1.6 Any mutually agreed benchmark including conventional financial benchmark such as Base Lending Rate (BLR) may be used to determine the mark-up in the Murabahah contract.

**Illustration 5.1: BLR Used As Benchmark For Determining Murabahah Mark-up**

An IFI operating in a dual banking system where conventional banking offer similar financial services to the same pool of customers. The BLR of the industry is quoted at 3%. The IFI assesses the expectations of investment and non-investment account holders which is found to be 3.5% in lieu of BLR. In this respect, the pricing of Murabahah financing may take into consideration the BLR as the base rate as a form of competitive price determination.

5.1.7 In an agreement where several Murabahah contracts are separately concluded and executed, each Murabahah contract mark-up may be priced differently.
5.1.8 If several commodities in several Murabahah contracts are sold to the same purchase orderer, the total purchase price plus the total mark-up may be stated in one clause in the Master agreement, provided that the details of each asset’s purchase price and mark-up must be appended to each sale contract.

5.1.9 At the time of concluding a Murabahah contract, both the IFI and the purchase orderer may mutually agree to vary the financing tenure and adjust the mark-up that was initially promised in the Wa’d undertaking.
5.1.10 The acquisition cost, which forms the cost portion of the Murabahah purchase price may include direct expenses which refer to costs incurred to enable the acquisition of goods by the IFI and delivery of the goods to the customer. This includes expenses such as for transportation, storage, assembling, taxes, insurance or takaful or any valid expenses established by customary practice. Any indirect expenses shall not be included in the acquisition cost.

5.1.11 Whenever a purchase order involves a transaction requiring the issuance of a Letter of Credit (LC), the IFI may include the commission for issuing the LC as part of the total cost.

5.1.12 Upon acquisition of an asset and until its transfer to the purchase orderer, the IFI is liable for the asset, and may insure the asset acquired before transferring it to the purchase orderer. The takaful contribution paid by the IFI may be added to the cost of purchase or acquisition, provided that it should not be higher than the asset’s initial value.

Illustration 5.3: Variation In The Original Murabahah Terms

A customer’s order to purchase equipment estimated at RM 50,000 for a financing period of 5 years is specified and promised to an IFI. IFI agreed to finance the order at 10% mark-up as per the order. Upon acquisition, the price of purchase is RM 60,000 and both the customer and IFI renegotiate the term and mutually agree that IFI will finance through Murabahah at 10% for a period of 6 years to enable the customer to meet regular instalment payments of RM 11,000 per year.
5.1.13 Any additional direct expenses not specified in the agreement relating to a *Murabahah* contract incurred post conclusion of the *Murabahah* contract shall be borne by the customer provided that such a clause to that effect is already incorporated in the contract. These additional charges, however, shall not be taken into consideration in determining the *Murabahah* sale mark-up.

**Illustration 5.4: Additional Cost Of The *Murabahah* Contract**

An IFI has fulfilled its contractual obligations with a purchase orderer by purchasing empty containers. However, the purchase orderer failed to claim his assets on the stipulated delivery date, causing the IFI to incur more port expenses. Empty containers located inside the port have a grace period of 10 days, after which charges of USD 1,000 per day will be levied. The aforementioned charges are to be borne by the purchase orderer after being notified of the arrival of his shipment. These extra charges should not be part of the cost price.

5.1.14 Any purchase of asset on credit by an IFI may be sold to the purchase orderer provided that the terms of credit sale are made known to the purchase orderer in order to decide on the mutually agreed purchase price and mark-up.

5.1.15 In the case of non-disclosure of this credit term, the contract is voidable at the option of the purchase orderer to return the asset to the IFI at cost (*khiyar al-Radd*).

5.1.16 Any discount on cost of acquisition obtained upon purchase by IFI shall be accorded to the purchase orderer with a proportionate reduction in mark-up amount at agreed rate.
Illustration 5.5: Discount Benefit To Purchase Orderer

A supplier offers a 10% trade discount to its purchasers for any purchase of RM 50,000 and above. The IFI, based on the promise by the purchase orderer, purchases an asset worth RM 50,000 from the supplier. The client, being the purchase orderer, subsequently purchases the asset from the IFI at RM 50,000 with a mark-up of 20% via a Murabahah contract. Although there is no contractual relationship between the supplier and the purchase orderer, the latter, and not the IFI, should be the beneficiary of this discount. Without the discount, the Murabahah sale price payable by the client is (1.2 X 50,000) RM60,000. However with the 10% discount, the Murabahah sale price payable by the client is (1.2 X 45,000) RM 54,000.

5.1.17 Any asset purchased in foreign currency by an IFI may be sold to the purchase orderer in any currency agreed with the purchase orderer at a cost price, equivalent to the exchange value of the foreign currency initially paid by the IFI on the day of purchase.

Illustration 5.6: The Effect of Currency Volatility On Murabahah Transactions

On the order of its client, the IFI purchases a car from France in USD for an amount of USD50,000 to finance the client for Murabahah car financing at an agreed mark-up of 10% in Malaysian currency. On the purchase day, the exchange rate of 1USD was RM3.50, but on the day of the sale of the car to the purchase orderer, the Dollar has depreciated to RM3.20. In principle, this depreciation has no effect on the Murabahah sale contract, and the payment should be made according to the rate prevailing on the day the IFI purchased the asset from the supplier. The Murabahah selling price payable by the client is (1.1 X 50,000 X 3.5) RM 192,500.
5.1.18 Alternatively, the two parties may also negotiate on whether the Takaful contribution should constitute part of the cost and hence, may be charged separately.

**Illustration 5.7: Inclusion Of Takaful Charges For Murabahah Financing**

An IFI finances a customer for the purchase of a property valued at RM250,000 at a mark-up of 10% per annum for a period of 10 years. The *Murabahah* selling price is RM500,000 if straight line method is used. The customer is also required to insure the property against fire as well as to take up a Mortgage Reducing Term Takaful (MRTT). Both parties agreed that the takaful contribution shall be paid separately by the customer to the takaful operator via the IFI. The contribution paid to the takaful operator for fire insurance and MRTT shall be additional costs borne by the customer in addition to the selling price.

5.1.19 The IFI may reward a purchase orderer who honours the terms of the *Murabahah* contract by opting to waive part of the price.

5.1.20 The IFI and the purchase orderer may agree to make settlement in a currency which is different from the currency specified in the contract at the prevailing exchange rate on the day of payment.

5.1.21 Rescheduling of debt in another currency is not permissible. However, full settlement of outstanding debt in another currency is permissible and it shall be executed based on the exchange rate of the settlement date.
Illustration 5.8: Settlement of Murabahah in Another Currency

A purchase orderer currently owes an IFI a sum of Euro 70,000 for a house financed under Murabahah sale two years ago. Given the fact that the purchase orderer’s income is paid in US dollar, and being mindful of exchange rate risk exposure, the purchase orderer requested the IFI to fully settle his debt in USD instead of Euro. The exchange rate of 1 Euro during the time of concluding the contract was USD1.10, but at the time of the proposed full settlement of the debt, the rate rose to USD1.20. The amount to be settled in USD is converted at USD1.20 per 1 Euro which is USD84,000. There is no riba implicated in the arrangement as the debt is fully settled.

5.2 MODES OF PAYMENT

5.2.1 The IFI shall make payment directly to the supplier and not through the purchase orderer except when the latter is appointed as an agent of the IFI.

5.2.2 The IFI may consider, at the time of pre-payment or early settlement, waiving part of the outstanding payment in form of a discount to the purchase orderer for settlement before the maturity date.

5.2.3 Alternatively, both the IFI and the purchase orderer may insert a pre-agreed clause in the contract for such a discount or rebate in the case of early settlement.
5.2.4 The payment of the Murabahah may be rescheduled to suit the financial position of the purchase orderer or for any other reasons but no additional amount to the selling price due to extension of time or market condition is permissible.

5.2.5 The IFI may charge the purchase orderer a fee for processing the purchase orderer’s Hawalah application to transfer the debts to another customer as a form of settlement.
5.3 **DISCLOSURE OF PURCHASE PRICE (TRUSTEESHIP)**

5.3.1 The purchase cost of the asset payable by the IFI to the seller shall be disclosed to the purchase orderer before concluding the *Murabahah* contract. The cost shall include the purchase price and expenses related to the acquisition of the assets or goods.

5.3.2 The failure of the IFI to properly disclose the purchase price as cost to determine the mark-up to the purchase orderer shall render the *Murabahah* contract null and void *ab initio*.

**Illustration 5.10: Intentional Misrepresentation of Purchase Price**

An IFI agreed to provide *Murabahah* financing of RM 150,000 for a vehicle at a disclosed cost of purchase of RM 100,000 and mark-up of RM 50,000. Additional information obtained by customer from supplier indicated that the cost of vehicle is RM 90,000. The *Murabahah* contract is null and void due to the failure of disclosing actual cost of purchase.

5.3.3 In the event where the purchase orderer is appointed as the agent of the IFI based on a *Wakalah* contract, where several quotations are given by the purchase orderer for the IFI to consider, the IFI shall clearly specify to the purchase orderer the quotation which the IFI has chosen.
5.3.4 The IFI shall disclose to the purchase orderer the mark-up to be added to the purchase price. The mark-up could either be a fixed amount or a percentage of the purchase price.

5.3.5 Any defect caused by *force majeure* in the asset purchased for the purchase orderer which is discovered by the IFI or the purchase orderer shall be communicated to the other contracting party. Both the IFI and the purchase orderer may either mutually agree to adjust the terms of the contract or rescind it.

5.3.6 IFI may levy a service charge for additional services rendered by IFI as requested by the purchase orderer such as to conduct a feasibility study on business needs.

### 5.4 ASSET

5.4.1 Assets such as traded goods, production materials, property, equipment and fixtures, and, other intangible and non-monetary assets, are eligible assets for sale provided these are not specifically

Illustration 5.11: Disclosure of Purchase Price

A purchase orderer requested an IFI to finance a purchase of specified equipment. The purchase orderer who has specialized knowledge of the equipment was required by the IFI to provide several quotations of such equipment by different suppliers to ascertain a fair value of cost of purchase. Based on established industry standards of the equipment, the IFI agreed to purchase the specified equipment based on one of the few given quotations. The quotation thus becomes the purchase cost in the *Murabahah* sale to the purchase orderer. This selected quotation shall be disclosed to the purchase orderer.
prohibited in the *Quran* and *Sunnah* such as usurious items, liquor and flesh of swine.

5.4.2 Assets to be purchased for *Murabahah* sale shall be assets which are valid and can be considered for an enforceable sale. For example, a purchase of a *Waqf* property is not acceptable in a *Murabahah* sale as *Waqf* properties are restricted from being sold.

**Illustration 5.12: Invalid Assets for Murabahah Transaction**

A customer requested an IFI to finance purchase of an unoccupied property. Upon communication with the potential seller, it was found that the property was registered in the name of foundation and is designated as *Waqf* property. Since *Waqf* property is meant for the society and not subject to commercial sale, financing for the identified property is not permissible and not valid from Shariah principle.

5.4.3 Asset meant to be sold to the purchase orderer on *Murabahah* basis shall be legally and/or beneficially owned by the IFI prior to the *Murabahah* sale to the customer.

5.4.4 Physical possession or constructive possession by the seller of an asset is required for the asset to qualify for a *Murabahah* contract. Constructive possession shall be proven via existence of physical evidence of effective transfer or receipts such as warehouse receipt, etc.
Illustration 5.13: Constructive Possession of Murabahah Asset by IFI

An IFI received a customer’s application for financing to purchase goods worth RM 150,000 to be delivered to customer’s warehouse with a purchase undertaking. Based on the promise, the IFI disbursed payment to the supplier upon receipt of third party warehouse certificate as evidence of constructive possession that the goods have been received. The IFI then executes the Murabahah sale at a mark-up price of RM 200,000 to the customer, payable in three months time. The customer immediately accepts delivery since the goods are available in the customer’s warehouse as specified.

In cases where the goods are delivered to a different warehouse and the title is impliedly transferred to IFI upon disbursement, the Murabahah sale cannot be concluded as the goods are not delivered to the customer’s warehouse. In this case additional transportation costs shall be borne by IFI to conclude the sale and ensure delivery as specified in the customer’s order.

5.4.5 Transfer of ownership from the IFI to the purchase orderer shall take place upon execution of the Murabahah contract and this could be manifested by way of abandoning the right of ownership (takhliyah) by the IFI or enabling the purchase orderer to make full use of the asset, assuming full liability (tamkin).

5.4.6 The Murabahah sale shall exclude any sale of currencies and debt for a deferred payment.

5.4.7 Shares may be made as asset of a Murabahah transaction.

Illustration 5.14: Purchase of Shares as a Murabahah Transaction

An entrepreneur, seeking funding to purchase certain Shariah compliant stocks, draws up a Murabahah contract with an IFI to purchase for him shares at RM10 per share. After buying the shares, the IFI sells them to the entrepreneur at a marked-up price of RM12 per share.
5.4.8 Intellectual properties such as trademarks, brands and copyright, also qualify as asset of *Murabahah* transaction.

**Illustration 5.15: Purchase of Goodwill as a *Murabahah* Transaction**

A customer seeks financing from an IFI to purchase a brand name of a distributor known as “Fitforall” valued at RM500,000 that will enable the customer to be part of the retail chain to sell the goods under the brand name. The brand provides product quality assurance to existing and potential brand loyal customers, as well as an established international distribution network. The IFI may purchase the brand name and sell it to the customer at a marked-up price of RM750,000 to be paid over a period of 5 years.

5.4.9 Usufructs such as air tickets qualify as assets to be purchased and sold on *Murabahah* basis.

5.4.10 Indirect expenses of IFI such as staff wages, labour charges, customs fees and storage charges which are not part of cost of purchase, do not qualify as *Murabahah* assets.

**Illustration 5.16: Indirect Expenses Not a Valid Object For *Murabahah***

A customer seeks IFI financing to pay for the professional fees and technicians’ wages for a contract of service that has been awarded to the customer. The customer has valued the fees and wages at RM600,000 as the financing amount and is prepared to pay a marked-up price of RM660,000 for the one year contract. Work done by the professionals and technicians may not be transferred as the object of sale and hence, the proposed *Murabahah* financing is not valid. *Murabahah* for cash financing is relevant to finance this requirement.
5.4.11 Services rendered as part of the subject matter of *Murabahah* may qualify as assets.

**Illustration 5.17: Cost of Services Rendered as Part of *Murabahah* Sales**

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<td>A customer seeks IFI financing to acquire and install machinery valued at RM 1.2 million. The supplier of factory plant and machinery provides the components to be assembled at the customer’s factory site. Assembly and customization services cost an additional RM 300,000. With the given cost structure and a mark-up of RM 500,000, IFI <em>Murabahah</em> selling price is RM 2 million for a three year financing period for the components, assembly and customization of the plant and machinery to be installed at the customer’s site.</td>
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5.4.12 *Murabahah* sale shall not take effect between the same contracting parties on the same asset. The revolving facility using *Murabahah* contract may involve separate contracts on different assets between the same contracting parties.

**Illustration 5.18: Murabahah Revolving Facility**

A master *Murabahah* agreement to provide RM 500,000 working capital financing facility at a mark-up of 10% per annum for a period of 2 years was agreed between IFI and its customer in January 2007. The following transactions were effected in the first year as follows:

a. *Murabahah* financing of RM 250,000 worth of office equipment at RM 25,000 mark-up was transacted in February 2007 to be paid 12 months later.

b. *Murabahah* financing of RM 150,000 worth of office supplies at RM 15,000 mark-up was transacted in April 2007 to be paid 12 months later.

c. Payment of RM 262,500 was made to settle the *Murabahah* financing of RM250,000 (transaction a) with 50% rebate on mark-up. The payment was received six months earlier in August 2007.
d. **Murabahah** financing of RM 350,000 worth of fixtures at RM 17,500 mark-up was transacted in September 2007 to be paid in 6 months.

In April 2008 full payment was received for financing in April 2007 (transaction b) but there was a request for the transaction in September 2007 (transaction d) to be rescheduled. Thus the fixtures were bought and sold again at the same mark-up to the customer. This transaction to reschedule the financing does not comply with Shariah.

The purchase and resale of the fixtures to the customer to reschedule the financing is prohibited as it involves the same asset, even though the working capital financing facility is still available in the second year.

5.4.13 The liability for loss or damage of asset acquired for the purchase orderer while in the possession of IFI shall be borne by the IFI.

5.4.14 Any asset purchased by the IFI for **Murabahah** financing to the customer shall be specified and differentiated from similar or other goods in the same shipment. This is to ensure effective delivery of specified goods.

5.4.15 **Murabahah** to purchase orderer sale by the IFI to the customer shall not be valid if IFI purchases an asset from the customer and subsequently sells the same asset to the customer. The contract shall also be invalid if asset purchased by customer from vendor is subsequently purchased by IFI and sold to the customer based on MPO.

5.4.16 The IFI shall not sign the **Murabahah** contract with the purchase orderer prior to the purchase of assets or goods to be acquired.

5.4.17 In **Murabahah** to Purchase Orderer, the vendor from whom the IFI purchases the asset shall be a non-related party to the customer.
5.4.18 The IFI shall be deemed to have ownership right on assets to be sold based on MPO upon receipt of documents attesting to the ownership transfer to IFI which include, among others, shipment and storage certificates.

5.4.19 The purchase orderer may request the IFI to purchase the assets intended for the Murabahah financing from a specific market place or a supplier. However, the IFI may decline this request for whatever reason deemed reasonable by the IFI.

5.4.20 The purchase orderer would apply to the IFI, an order to purchase an asset with identified specifications. The purchase orderer may provide the IFI with information pertaining to the asset specifications in terms of price, availability and market location. However, the IFI reserves the right to conduct its own assessment on the asset ordered to be purchased.

5.4.21 Assets purchased by the IFI according to the purchase orderer’s requirements may be delivered to the purchase orderer prior to the conclusion of the Murabahah contract.

5.4.22 Loss or damage of goods in the possession of the purchase orderer prior to the conclusion of the Murabahah contract due to negligence of the purchase orderer shall be borne by the purchase orderer.

5.4.23 The purchase orderer has a recourse to the supplier through the IFI for any defect of asset or good delivered to the purchase orderer based on the defect option (khiyar al-‘Ayb). The IFI may seek
indemnification for the loss in value due to the defect from the takaful company which arranged the takaful coverage for the assets or goods.

**Illustration 5.19: Defective Asset Not Valid as the Object of Murabahah**

A purchase orderer requests for an IFI to finance the purchase of a completed residential property identified by the purchase orderer under a Murabahah contract. After processing the application, it was found that the property was certified not fit for occupancy by building authorities due to structural defect. The object of sale is found to be of non-merchantable quality and hence would not qualify for IFI Murabahah financing to the customer until and unless rectification to the property is carried out by vendor to obtain the fitness certificate.

5.4.24 Alternatively, the IFI may incorporate in the contract to exempt itself from any defect in the asset. The IFI may, upon agreement by the purchase orderer, assign the right of recourse from the vendor for the defect, to the purchase orderer.

5.4.25 The IFI shall reject a Murabahah application by the purchase orderer who has already established a contractual relationship with the supplier aimed at acquiring cash rather than trading the goods under transaction.
5.5 **ENHANCED FEATURES OF THE CONTRACT**

5.5.1 **WA’D (PROMISE) BY THE PURCHASE ORDERER TO PURCHASE THE ASSET ON MURABAHAH BASIS**

5.5.1.1 The *Wa’d* (promise) by the purchase orderer to purchase the asset from the IFI upon the latter’s acquisition of the asset shall be binding on the purchase orderer.

5.5.1.2 The *Wa’d* shall be separately executed prior to the execution of *Murabahah* contract.

5.5.1.3 During the purchase requisition, the purchase order application shall contain the promise which must be duly signed by the purchase orderer.

5.5.1.4 The purchase orderer who promised to purchase and to take delivery of asset but refused to enter into the *Murabahah* transaction upon purchase made by the IFI as per agreed terms shall be held liable for breach of *Wa’d* and shall compensate for related actual costs incurred by the IFI for the disposal of the asset to a third party and the shortfall in the disposal price compared to the purchase price.
5.5.1.5 The purchase orderer at the stage of Wa’d may act as a Kafil to the IFI to guarantee the safe delivery of the asset by the supplier to the IFI. Any loss incurred due to late delivery of the asset to the IFI shall be borne by the purchase orderer as the Kafil. The purchase orderer may also be held liable for damages if the asset supplied by the supplier is found to have violated the agreed specifications. Damage or defects that arise after the delivery of the asset to the purchase orderer shall not be covered under this guarantee arrangement.

5.5.1.6 During the Wa’d stage, a Murabahah sale price may be determined based on a benchmark such as BLR as specified by clause 5.1.6 to determine the mark-up.

5.5.1.7 Amendment to the terms of the binding promise shall not be permitted without the consent of the other party.

5.5.1.8 During the Wa’d stage prior to executing the Murabahah contract, the IFI and the purchase orderer may mutually agree to modify the
terms for example the maturity date of payment or a new mark-up as well as to change from *Murabahah* contract to other financial transactions.

5.5.1.9 At the time of *Murabahah* contract execution, details of the transaction shall be incorporated and documented eventhough these specifications were already stipulated during the *Wa’d* stage.

5.5.2 EVENT OF DEFAULT AND RECOVERY OF *MURABAHAH* FINANCING

5.5.2.1 The customer shall ensure timely and prompt payment of *Murabahah* financing as per payment schedule agreed with the IFI.

5.5.2.2 The outstanding liability after the demise of the customer may be waived by the IFI. In the cases where there is no waiver, the IFI may claim the remaining instalments from the heirs of the purchase orderer under a court order or on a mutual agreement basis unless stated otherwise in the contract.

5.5.2.3 IFI may include a clause in the *Murabahah* contract, stipulating a “compensation for late payment” as determined by the relevant authorities, which is claimable by the IFI from the customer as income or include a clause stipulating penalty which shall be channelled to charity. The IFI may also require the customer to prove claim of non-delinquent insolvency in order to be exempted from penalty.
5.5.2.4 If the customer defaults, the IFI may purchase the same asset or a part thereof from the customer in default on cash basis. The proceeds of which, may be used to settle the outstanding debt on the basis of set-off (Muqasah). Upon acquisition of the asset by the IFI, the asset may be leased to the purchase orderer on the basis of lease with an option to purchase (Ijarah Muntahia Bi Al-Tamlik).

5.5.2.5 A customer in default may be granted an extension to settle his debts, provided no additional charges on the financing amount are imposed. IFI may recover the outstanding debt from the securities provided by the purchase orderer. For the purpose of rescheduling the outstanding debt, the IFI may demand additional securities from the purchase orderer.

5.5.2.6 The IFI may impose the customer in default to bear all costs accrued to recover the payment defaulted, including the costs of judicial proceedings and legal fees which the IFI would have incurred to recover the outstanding payment.

5.5.2.7 The contract of Murabahah may contain a clause, binding the customer to settle all outstanding obligations before the maturity date if he defaults on any instalment.

5.5.2.8 The IFI may grant the customer in default a grace period to settle the debt after sending notices of reminders before commencement of debt recovery measures. However, any increase in the selling price due to rescheduling of the contract or due to inability to pay on time is not permissible.
5.5.3 **AGENCY IN MURABAHAH**

5.5.3.1 The IFI may appoint the purchase orderer as its agent (Wakil) to purchase the asset from the vendor on behalf of the IFI.

**Illustration 5.21: Purchase Orderer Buying on Behalf of Seller**

An international company requests an IFI to finance the import of raw materials from Finland. Due to the inability of the IFI to conduct a market survey for the best quotations, the IFI appointed the same company to conduct the market survey and purchase the asset on its behalf. This arrangement requires two separate contracts. Firstly, the IFI signs a *Wakalah* contract with the company so that the latter would act as an agent for the IFI. Subsequently, the IFI would enter into a *Murabahah* contract with the company. Both contracts are separate as the parties involved are acting in different capacities.

5.5.3.2 The appointment of the purchase orderer as an agent by the IFI based on a *Wakalah* contract to acquire the asset from the supplier shall be in a separate contract from the *Murabahah* contract.

5.5.3.3 The purchase orderer as a purchasing agent of the IFI shall not waive the effective transfer of assets or goods from the IFI to the purchase orderer. The IFI which appoints purchase orderer as purchasing agent shall not waive its liability on the purchased asset. Such waiver may lead to money lending or cash financing.

5.5.3.4 As a purchasing agent of the IFI, the purchase orderer may obtain quotation on asset price in the name of the IFI.
5.5.3.5 As a purchasing agent of the IFI, the purchase orderer may obtain quotations from the supplier under his name subject to acceptance from the IFI.

5.5.3.6 The IFI may appoint the supplier as its selling agent to conclude the Murabahah contract with the purchase orderer.

5.5.3.7 The supplier may be appointed as the agent of the purchase orderer to purchase the goods on Murabahah basis from the IFI. This agency contract is a separate contract independent from the sale contract of the supplier to sell and deliver the assets to IFI.

5.5.3.8 The promisor cum purchase orderer may be the sole authorized agent to purchase or import a particular asset from the vendor or exporter. Notwithstanding clause 5.4.17, the relationship between the promisor and vendor and the fair value of purchase price must be made known to the IFI.

5.5.3.9 The name of purchase orderer who is appointed as an agent of the IFI to conclude the Murabahah contract may be disclosed in all documents.

5.5.4 GUARANTEE / SECURITY

5.5.4.1 The IFI may require guarantees in two stages of MPO arrangement. The first is guarantee at the stage of Wa’d from the purchase orderer and the second is guarantee at the stage of Murabahah contract from the customer. The guarantee at the Wa’d stage is to ensure actual purchase of the asset by the purchase orderer from...
the IFI while the guarantee at the Murabahah contract stage is to ensure full payment of the selling price at the date of maturity. These guarantees may include a third party guarantee, a pledge of any asset or real or moveable property, or a pledge of the asset of the Murabahah contract, cheques or promissory notes, or any security measure deemed legal and lawful.

5.5.4.2 At the stage of acquisition from the vendor, the IFI shall not require the purchase orderer to subscribe to a takaful policy on the asset of Murabahah so that IFI could secure the full payment which will be due on the purchase orderer.

5.5.4.3 A third party guarantor shall be of good financial standing and is capable of making good the instalments defaulted by the purchase orderer.

5.5.4.4 Securities of non-Shariah approved companies such as shares of conventional banks pledged as collateral for Murabahah transaction shall be avoided.

5.5.4.5 If collateral consists of a mixture of principal amount and interest amount, only the principal amount is allowed to be taken by the IFI in the case of customer default.

5.5.4.6 The guarantee for payment of customer’s outstanding liability to IFI for purchase of assets or goods under Murabahah contract shall not take effect until the actual Murabahah contract is duly executed.
5.5.4.7 Upon declaration by the court that the customer is insolvent or bankrupt, all outstanding amount due from Murabahah contract is claimable from the guarantee, collateral or other securities to settle the debt.

5.5.5 SECURITY ARRANGEMENT

5.5.5.1 The IFI, as a financier, may impose on the purchase orderer an amount of money as security deposit (hamish al-Jiddiyah) to compensate against losses incurred in the event the purchase orderer breaches the promise or Wa’d.

5.5.5.2 Any balance of the security deposit shall be returned to the purchase orderer if the deposit is not utilized to mitigate loss (if any) suffered by IFI upon satisfying the conditions for the purpose of placing the deposit.

5.5.5.3 This security deposit may be treated as part of the payment of the agreed selling price under the Murabahah contract and hence, not refundable.

**Illustration 5.22: Refund of Purchase Orderer’s Deposit**

A customer promises to purchase and places 10% of cost of purchase as a deposit with an IFI to finance the purchase of RM 50,000 worth of textiles. The financing is based on Murabahah at a mark-up selling price of RM 75,000 for a 6 month financing period. Upon receipt of goods by the customer the outstanding amount payable to the IFI is RM 70,000 (less RM 5,000 security deposit).

On the other hand, in the case where goods are purchased but the customer does not take delivery, the IFI incurs disposal costs of RM 2,000 and is able to dispose off the goods at RM 49,000. The loss on disposal and the disposal costs...
5.5.5.4 Any form of deposit such as Wadi’ah deposited by the purchase orderer with the IFI may be used as a pledge to fulfil the liabilities of the purchase orderer under the Murabahah contract. In the event of default, the IFI may use the Wadi’ah to redeem the payment based on a set-off mechanism.

5.5.5.5 If the purchase orderer has defaulted in payment of the Murabahah contract, a portion or all of the property charged as collateral may be disposed, or cheques deposited by the purchase orderer may be cashed at an equivalent value to compensate for the total outstanding amount.

5.5.5.6 To safeguard the interest of the IFI, the IFI may defer the registration of the asset in the name of the purchase orderer until full settlement of selling price. However, this practice does not and shall not deprive the purchase orderer’s right of ownership to the asset.

5.5.6 DISSOLUTION/TERMINATION OF THE CONTRACT

5.5.6.1 Upon settlement of the outstanding debt owed to the IFI by the purchase orderer without any encumbrances, the Murabahah contract is dissolved.
5.5.6.2 The IFI and the purchase orderer may mutually agree to dissolve the contract at any point in time prior to maturity date unless stated otherwise in the relevant documents of the Murabahah contract.

5.5.6.3 The IFI may take a down-payment from the purchase orderer (‘urbun) after signing the contract. This payment may be used to compensate the actual losses incurred by the IFI should the purchase orderer were to terminate the contract.

6.0 EFFECTIVE IMPLEMENTATION DATE