

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

MURABAHA/MURABAHA TO
THE PURCHASER

Definition of Murabaha:

- **Literary Meaning:** Sale on profit. Technically a contract of sale between a buyer and a seller in which a seller purchases the goods needed by a buyer and sells the goods to the buyer on a cost-plus basis. Both the profit (mark-up) and the time of payment (usually in installments) are specified in an initial contract.
- In other words it is a particular kind of Sale where the Seller discloses its cost and profit charged thereon.
- The price in this sale can be both on spot and deferred.

Murabaha to the purchase orderer:

- Murabaha refers to a contract in which a financial institution purchases good upon the request of a client who makes payment that covers cost and agreed-upon profit margin for the financial institution

Scope of MURABAHA:

- As it is a kind of sale, there must be a seller and buyer and some thing that is bought and sold. The Bank is the Seller and the Client is Buyer.
- It cannot be used as a substitute for running finance facility, which provides case for fulfilling various needs of the Client

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- It is a fixed price Sale and normally is done for short term.
- The transaction can be used in order to meet the working capital requirements of the Client.

Procedure prior to the contract of Murabaha

The customer's expression of his wish to acquire an item through the institution

- It is permissible for the institution to purchase the item only in response to its customer's wish, as long as this practice is compatible with the Shari'a precepts for the contract of sale.
- It is permissible for the customer to request the institution to purchase the item from a particular source of supply.
- However, the institution is entitled to decline to carry out the transaction if the customer refuses offers from other sources of supply that are more suitable for the institution.

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- The customer's wish to acquire the item does not constitute a promise or commitment except when it has been expressed in due form.
- It is permissible to prepare a single set of documentation to include both the customer's stated wish that the institution should buy the item from the supplier and a promise to buy the item from the institution, which the customer signs.
- It is permissible for the customer to prepare such a document, or it may be a standard application form prepared by the institution to be signed by the customer.

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- The customer may obtain statement of prices from the supplier whether they are addressed to the customer by name, or with no reference to any named customer.
- In the latter case, the statement is considered as an invitation to negotiate, and not as an offer of sale.
- It is preferable that the invoice should be addressed to the institution so as to constitute an offer of sale from the supplier effective up to the end of a specified period.
- Once acceptance comes from the institution, that automatically concludes the contract of sale by the two parties.

The position of the institution in respect to the application of the customer for Murabaha to the purchase orderer

- When there is acceptance by the customer of an offer from the supplier that is either addressed to him personally, or that has no addressee, then it is not permissible for the institution to carry out Murabaha to the purchase orderer.
- It is essential to exclude any prior contractual relationship between the customer who is the purchase orderer and the original supplier of the item ordered, if any, regarding the supply of the item.
- It is not permissible to transfer a contract that has been executed between the customer and the supplier of the ordered item to the institution.

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- The institution must ensure that the party from whom the item is bought is a third party, and not the customer or his agent.
- It is permitted for the institution to purchase the item from a party who has a blood or marital relationship with the customer.
- It is preferable that the institution's application procedures for Murabaha to the purchase orderer be designed to avoid such a practice.
- It is not permitted for the institution and the customer to agree to form a Musharaka in a project or a specified deal together with a promise from one of them to buy the other's Musharaka participation by means of Murabaha on either spot or deferred payment terms.

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- However, it is permissible for one partner to promise to purchase the other's Musharaka participation at market selling price or at a price to be agreed upon at the time of sale provided a new contract is drawn up. This sale may be on spot or on deferred payment terms.
- It is not permitted to carry out a Murabaha on deferred payment terms where the asset involved is gold or silver or currencies.
- It is also impermissible to issue negotiable instruments where the underlying asset consists of Murabaha receivables or other receivables.

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- It is not permitted to conclude a Murabaha contract on a commodity that was the subject matter of a previous Murabaha contract with the same customer, i.e. to refinance the transaction.

The Promise from the customer

- It is not permissible that the document of promise to buy (signed by the customer) should include a bilateral promise which is binding on both parties (the institution and the customer).
- The customer's promise to purchase, and the related contractual framework, are not integral to a Murabaha transaction.
- If the institution has other opportunities to sell the item, then it may not need such a promise or contractual framework.

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- A bilateral promise between the customer and the institution is permissible only if there is an option to cancel the promise which may be exercised either by both promisors or by either one of them.
- It is permissible for the institution and the customer, after the latter has given a promise but before the execution of the Murabaha, to agree to revise the terms of the promise whether with respect to the deferment of payment, the mark-up or other terms.
- The terms of the promise cannot be revised unless both parties agree to revise the promise, as the right to do so cannot be given exclusively to one of them.

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- It is permissible for the institution to purchase the item from a supplier on a “sale or return” basis, i.e., with the option to return it within a specified period.
- If the customer then does not purchase the item, the institution is able to return it to the supplier within the specified period on the basis of conditional option that is established in Shari'a.
- The option between the institution and the supplier does not expire by the mere presentation of item to the customer, but it expires by virtue of the actual sale to the customer.

Commissions and expenses

- It is not permissible for the institution to receive a commitment fee from the customer.
- It is not permissible for the institution to receive a fee for providing a credit facility.
- The expenses of preparing the documents of the contract between the institutions and the customer are to be divided between the two parties, provided they do not agree that the expenses are to be borne by one of the parties.

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- If the Murabaha to the purchase orderer is carried out by means of syndicated financing, the institution which acts as the arranger of the syndicate is entitled to claim an arrangement fee to be paid by the participants in the syndicate.
- It is permissible for the institution to take a fee for a feasibility study that it undertakes, if the study is based on the request by the customer and is for his benefit, and he agreed to pay the fee from the outset.

Guarantees related to the commencement of the transaction

- It is permissible for the institution to obtain from the customer a guarantee regarding the good performance by the supplier of his contractual obligations towards the institution in his personal capacity and not in his capacity as purchase orderer or an agent of the institution.
- Hence, if the Murabaha contract is not executed his guarantee would still be valid. This guarantee is required only in cases where the customer has suggested a particular source of supply for the item that is the subject matter of the Murabaha contract.

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- As a consequence of this guarantee, the customer will be obliged to make good any damage suffered by the institution due to failure of the supplier to provide good performance of his contractual obligations.
- These obligations concern meeting the specification of the item to be supplied and the exercise of diligence in executing the contract, non-observance of which results in the loss of the institution's time and efforts or property, or in a legal dispute and damage claims.
- It is not permitted to impose on a customer who is the purchase orderer a guarantee regarding hazards that may affect the item such as damage and destruction during period of shipment or storage.

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- It is permissible for the institution, in the case of a binding promise by the customer, to take a sum of money as *hamish jiddiyyah* (i.e. a security deposit).
- *This is to be paid by the customer at the request of the institution, both as an indication of the financial capacity of the customer and to ensure the compensation of any damage to the institution arising from a breach by the customer of his binding promise.*
- *Having taken his hamish jiddiyyah, the institution need not to demand compensation for damage as this may be charged against the hamish jiddiyyah.*

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- The *hamish jiddiyyah* is considered not as *urbon* i.e. earnest money.
- *The amount of money deposited by the customer as security for his commitment can be either held as trust in the custody of the institution, in which case the latter cannot invest it, or it may be held, if the customer permits the institution to invest it, as an investment trust on the basis of Mudaraba between the customer and the institution.*
- In the case of the customer's breach of his binding promise, the institution is not permitted to retain *hamish jiddiyyah* as such.

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- Instead, the institution's rights are limited to deducting the amount of the actual damage incurred from *hamish jiddiyyah* as a result of the breach.
- The actual damage to the institution may not include the loss of its mark-up in the Murabaha transaction, that is, its opportunity loss
- When the customer has fulfilled his promise and executed the contract of Murabaha to the purchase orderer, the institution must refund *hamish jiddiyyah* to the customer.
- The institution is not entitled to use any amount of *hamish jiddiyyah* except in the case of breach of promise as laid down in item.

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- It is permissible for the institution to agree with the customer that the amount of *hamish jiddiyyah* will be deducted from the price payable by the customer pursuant to the contract of Murabaha to the purchase orderer.
- It is permissible for the institution to take urbon (earnest money) after concluding the Murabaha sale with the customer.
- This may not be done during the contractual stage at which the customer has given his promise to purchase.

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- It is preferable that the institution return to the customer the amount that remains after deducting the actual damage incurred from the *urbon* as a result of the breach, namely the difference between the cost of the item to the institution and its selling price to a third party.

Acquisition of title to, and possession of the asset by the institution or its agent

The acquisition of the asset or good by the institution prior to its sale by means of Murabaha to the purchase orderer

- The institution is prohibited from selling any item in a Murabaha transaction before having acquired the item.
- Hence, it is not valid for the institution to conclude a Murabaha sale with the customer before concluding the purchase from the supplier of the item of the subject matter of the Murabaha, and before actual or constructive possession of the item as a result of the supplier giving control over the item or presenting documents that represent possession.
- It is permitted that the contract between the institution and the supplier be completed by means of a meeting of the two parties to discuss the details, at which point the contract may be executed.

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- Likewise, the Murabaha is considered as void if the contract with the supplier is void, as in this case the institution would not have complete title to the item.
- It is permitted that the contract between the institution and the supplier be completed by means of a meeting of the two parties to discuss the details, at which point the contract may be executed.
- Likewise, it is permitted that the contract be completed through exchanging the notices of offer and acceptance, either in written form or correspondence by any form of modern communication customarily practiced according to known principles.

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- The original principle is that the institution itself purchases the item directly from the supplier.
- However, it is permissible for the institution to carry out the purchase by authorizing an agent, other than the purchase orderer, to make purchase; and the customer (the purchase orderer) should not be appointed to act as an agent except in a situation of dire need.
- Furthermore, the agent must not sell the item to himself. Rather, the institution must first acquire title of the item and then sell it to the agent.

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- In the later case, it is obligatory to adopt procedures which would ensure that the following conditions are observed:
 - a. The institution itself must pay the supplier
 - b. The institution should obtain from the supplier the documents that confirm that a sale has taken place.
- It is obligatory to separate the two liabilities of risk attaching to the purchased item, namely the liability of the institution and the liability of the customer as agent of the institution.

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- This is achieved by having an interval in time between the performance of the agency contract and the execution of the contract of Murabaha to the purchase orderer, as indicated in the customer's notice of performance of the agency contract to acquire the item and offer to purchase the item by means of Murabaha, followed by the institution's notice of its acceptance of the customers' offer to purchase and the execution of the Murabaha sale contract.
- The original principle is that all the documents and contracts concerned with the execution of the sale of the item must be in the name of the institution and not in that of the customer, even if the latter acts as the institution's agent in acquiring the item.

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- It is permissible, at the time when the institution appoints someone as its agent for the acquisition of the item, that the two parties agree to authorize the agent to carry out the acquisition of the item as agent, without disclosing the existence of the agency agreement.
- In this case, the agent will act as principal in dealing with other parties, and will undertake the purchase directly in his name but on behalf of the institution as principal. However, it is preferable that the agent's role be disclosed.

The institution's taking possession of the asset or good, prior to its sale by Murabaha to the purchase orderer

- It is obligatory that the institution's actual or constructive possession of the item be ascertained before its sale to the customer on the basis of Murabaha to the purchase orderer.
- The condition that possession of the item must be taken by the institution (before its onward sale to the customer) has a specific purpose:
 - that the institution must assume the risk of the item it intends to sell. This means that the item must move from the responsibility of the supplier to the responsibility of the institution.

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- Similarly, it is obligatory that the point when the risk of the item is passed on by the institution to the customer be clearly identified, with reference to the stages in which the item is transferred from one party to another.
- The forms of taking delivery or possession of items differ according to their nature and different trade customs.
- Taking possession may be actual in the case of the physical delivery or transportation to the acquirer or its agent, but may also take place constructively by placing of the item at the acquirer's disposal so as to enable him to deal with it at his will, even though no physical delivery has taken place.

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- Taking possession of an item of real property may also take place by means of the property being vacated and its being placed at the acquirer's disposal; if the latter is not able to have disposal of the purchased item, then the vacation of the property is not considered as conveying possession.
- In the case of moveable assets, possession will take place in accordance with the nature of asset.
- The receipt of bill of lading by the institution or its agent, when purchasing goods on the international market, is considered as constructive possession. The same would apply to the institution's receipt of certificates of storage issued by warehouses following appropriate and reliable formalities.

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- The original principle is that the institution itself must receive the item from the premises of the supplier or from a location that is specified in the delivery conditions.
- The responsibility for the risk attached to the item is transferred to the institution upon its taking possession of the item.
- However, it is permissible for the institution to authorize another party to take delivery of the item on its behalf.
- Providing insurance cover for the item sold by Murabaha is the responsibility of the institution at the stage of its acquiring ownership.

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- The institution undertakes this responsibility in its capacity as the owner of the item & also bears all the consequential risks.
- The insurance indemnity, if the need for a claim arises before ownership is transferred to the customer, belongs to the institution exclusively and not to the customer.
- The institution is entitled to calculate expenses as part of the purchasing cost that may be subsequently built into the price of *Murabaha* deal.

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- Agency in carrying out the procedures of obtaining insurance cover for the item at the stage of the institution's acquisition of ownership of the asset is permitted.
- However, it is obligatory that the institution should bear the cost of insurance.

Conclusion of a *Murabaha* contract

- It is not permitted for the institution to consider that the contract of *Murabaha* to the purchase orderer is automatically concluded by its mere taking possession of the asset.
- Likewise, the institution may not force a customer who is the purchase orderer to take delivery of the asset and pay the *Murabaha* selling price, if the customer refuses to conclude the *Murabaha* transaction.
- The institution is entitled to receive compensation for any actual damage it has incurred as a result of the customer's breach of a binding promise.

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- The compensation consists of the customer reimbursing the institution for any loss due to a difference between the price received by the institution in selling the asset to a third party & the original cost price paid by the institution to the supplier.
- When the institution has purchased an asset for a deferred price, with the intention that it will be sold on a Murabaha basis, then the institution is obliged to disclose to the customer that the asset is purchased by the institution on deferred payment basis.
- The institution has the obligation to disclose to the customer, when concluding the contract of sale, the details of any expenses that it would include in determining the selling price.

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- The institution is also entitled to include any expenses relating to the item if this is acceptable to the customer.
- However, if the institution failed to disclose any expenses, it is not entitled to include them unless they are customarily considered as normal expenses, such as transportation expenses, storage expenses, fees for letters of credit and insurance premiums.
- The institution is not entitled to include in the base cost of the item, for the purpose of calculating the Murabaha price, any amounts other than the direct expenses that are paid to a third party.

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- It is not permissible for the institution to add the cost of the item payments made to its own staff for their work, & the like.
- If the institution has, even after the drawing up of the Murabaha contract, received a discount for the same item that was sold on Murabaha basis from the supplier of the item, then the customer should benefit from that discount by a reduction of the total Murabaha selling price in proportion to the discount.
- It is an obligation that both the price of the item and the institution's profit on the Murabaha to the purchase orderer transaction be fixed and known to both parties on the signature of the contract sale.

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- It is not permitted under any circumstances to subject the determination of the price or the profit to unknown variations or variations that are determinable in the future, such as by concluding the sale and making the profit dependent on the rate of LIBOR that will prevail in the future.
- There is no objection to referring to any other known indicators during the promise stage as a comfort indicator to determine the rate of profit, provided that the determination of the institution's profit at the time of concluding the Murabaha to the purchase orderer is based on a certain percentage of the cost and is not tied up with LIBOR or a time factor.

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- The institution's profit mark-up is Murabaha to the purchase orderer must be known, and the mere mention of the total selling price is not sufficient.
- It is permissible that the profit be determined based on a lump sum amount or a certain percentage of the cost price only or of the cost price plus the expenses.
- This determination is completed by the agreement and mutual consent of the two parties.

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- It is permissible to agree on the payment of the price of the item under Murabaha to the purchase orderer either by short or long term installments, and the selling price of the asset becomes a debt that the customer is obliged to pay at the time agreed upon.
- It is not permitted subsequently to demand any extra payment either in consideration of extra time given for payment or for delay in payment that may be for a reason or no reason.

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- It is permissible for the institution to stipulate in the contract of Murabaha to the purchase orderer a condition that the institution is free from responsibility for all or some of the defects of the asset; this is known as *Bai' al-Bara'ah* (sale on 'as is' basis).
- In the case of stipulating such a condition, it is preferable that the institution should assign to the customer the right of recourse to the supplier to obtain compensation for any defects that are established, which would otherwise be recoverable by the institution from the supplier.

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- If the institution did not stipulate its exemption from pre-existing hidden defects whose effects appear after the conclusion of the contract, then it is responsible for pre-existing hidden defects excluding any new defects (recent defects).
- The institution is entitled to include, as a condition of the contract, that in case of the customer's refusal, after the execution of the Murabaha contract, to take delivery of the asset at the prescribed time, the institution could revoke the contract or sell the asset to a third party on behalf of the customer and for his account.

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- The institution could then recover from the selling price the amount due to it from the customer under the contract, and would have recourse to the customer for the balance if that price were not sufficient to cover the amount due to the customer.

Guarantees and treatment of *Murabaha* receivables

- It is permissible for the institution to stipulate to the customer that installments may become due before their originally agreed due dates in case of the customer's refusal to perform or delay in paying any installment without any good reason.
- This may take place in one of the following ways:
 - a) The installments automatically become due as a result of a mere delay in a payment.
 - b) The installments become due after a delay in payment exceeding a specified time period.
 - c) The installments become due after the sending of a reminder notice by the institution to the seller giving a specified time period for payment.

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- The institute is entitled, in these circumstances, to waive a portion of its dues.
- The institution should ask the customer to provide lawful security in the contract of Murabaha to the purchase orderer.
- Among other things, the institution may receive a third party guarantee or the pledge of the investment account of the customer or the pledge of any item of real or moveable property, or the pledge of the subject matter of the Murabaha contract as a fiduciary pledge (or a registered charge), either without taking possession of the pledged asset, or by taking possession of the pledged asset.

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- It is permissible for the institution to require the customer to provide cheques or promissory notes before the execution of the contract of Murabaha to the purchase orderer, as a guarantee of the indebtedness that will be created after the execution of the contract.
- This is possible on the written condition that the institution is not entitled to use cheques or documents except on their due dates.
- The requirement to provide cheques as security is not permissible in countries where they could be presented for payment before their due date.

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- If the institution sells the asset as a result of the customer's failure to make a payment of the selling price on its due date, it must confine itself to recovering the amount due to it and must return the balance to the customer.
- In the case of the institution receiving a pledge from the customer, the institution is entitled to stipulate that the customer should make an assignment to the institution to enable it to sell the pledged asset for the purpose of recovering the amount due from the customer without recourse to the judiciary.

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- It is permissible that the contract of Murabaha consists of an undertaking from the customer to pay an amount of money or a percentage of the debt, to be donated to charitable causes in the event of a delay on his part in paying installments on their due date.
- The Shari'a supervisory board of the institution must have full knowledge that any such amount is indeed spent on charitable causes, and not for the benefit of the institution itself.
- It is not permissible to extend the date of payment of the debt in exchange for an additional payment in case of rescheduling, irrespectively of whether the debtor is solvent or insolvent.

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- When there is default in payment by the customer with regard to installments of the selling price that are due, the amount due is just the amount of the unpaid selling price.
- It is not permissible for the institution to impose any additional payment on the customer for the institution's benefit.
- It is permissible for the institution to give up part of the selling price if the customer pays early, provided this was not part of the contractual agreement.

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- It is permissible for the institution and the customer to agree, on the due date, that payment of the debt due on account of Murabaha to the purchase orderer may be made in a currency different from that in which the debt is denominated, provided any such payment is made based on the exchange rate of the day of the settlement.
- It is also a condition that either the settlement of the debt is completed in full or that the amount agreed be paid in the different currency is paid in full, so that there remains no balance owing in that different currency.

Process Flows

Local Murabaha:

- CLIENT approaches the Bank and expresses its desire to purchase particular asset/goods from the Bank on Murabaha basis.
- The Bank signs a Master Agency Agreement with CLIENT, drawing the parameters, terms and conditions of the Murabaha transactions that will be executed with the client and explaining the duties and functions of the client in its capacity as the agent of the Bank.

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- Whenever the Client desires to purchase an asset, it shall submit, with reference to the Master Agency Agreement, an offer containing the nature and specifications of the goods desired to be purchased and seeking authorization from the Bank to purchase the asset on the Bank's behalf. In the same offer, the Client shall promise to purchase, on Murabaha basis for the agreed price cost plus the agreed profit, the asset from the Bank upon the Bank's getting the title and possession of the asset and submit to the Bank a payment schedule.
- The Bank shall inspect the goods and accept the offer and thereby authorize the Client to purchase the asset on behalf of the Bank.

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- Once the Client receives the title to and physical or constructive possession of the asset on behalf of Bank it shall offer immediately to purchase the asset on Murabaha basis against the agreed price which is the cost plus an agreed lump sum amount a percentage of the cost whether flat or benchmarked. The offer shall contain schedule of payment by the Client.
- The Bank shall send its acceptance of the Client's offer, which will complete the sale of the asset to the Client by passing the title and risk to the Client.
- Since, the goods shall be already in possession of the agent, albeit in its capacity as an agent and trustee, the Bank shall not have to deliver the goods to the Client, as he shall be assumed to have received the goods. However, with the acceptance of his offer by the Bank, the nature of the Client's possession of the goods shall change as the risks of ownership shall pass from the Bank to the Client.

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- After that, the Bank may execute a Murabaha agreement with the Client to perfect the sale transaction.
- Supplier's price, plus tax and any other cost incurred by the Bank will be considered as the base amount for calculating Bank's profit at an agreed rate. Cash margin paid by the Customer, if any, must be deducted while calculating Murabaha profit which should be calculated from the date the Bank had paid the price to the Supplier.

LC Murabaha:

- DIBPL will sign a Master Agency agreement with the Client for importing assets on behalf of DIBPL, drawing the parameters, terms and conditions and explaining the duties and functions of the Client in its capacity as the agent of DIBPL.
- Whenever the Client desires to import above mentioned assets, it shall negotiate with the Supplier but before finalizing the deal, it shall submit, with reference to the Master Agency Agreement, an offer containing the nature and specifications of the assets desired to be imported and seeking authorization from DIBPL to import the asset on DIBPL's behalf. In the same offer, the Client shall (in the form of Exhibit A) promise to purchase, on Murabaha basis for the agreed price cost plus the agreed profit, the asset from DIBPL upon the DIBPL's getting the title and possession of the asset and submit to DIBPL a payment schedule.

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- DIBPL shall accept the offer and thereby authorize the Client to import the asset on behalf of DIBPL.
- On receiving DIBPL's acceptance the customer will conclude the purchase transaction with the supplier, in case of Master Agency Agreement under LC, by establishing an L/C through the Bank where it would be portrayed as the purchaser, rather the Bank, albeit it would be acting as Bank's undisclosed agent.
- The supplier would make the bill of lading in the name of DIBPL and ship the asset.

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- Upon receipt of shipment documents and bill of lading (title and constructive possession by the Client on behalf of the Bank), the Client shall offer immediately to purchase the asset on Murabaha basis against the agreed price which is the cost plus a percentage of the cost whether flat or benchmarked or a lump sum amount in line with the Promise to Purchase already submitted by the Client. All this will be evidenced through the exchange of Exhibit B by both parties.
- The costs incurred by DIBPL for importing the assets may include taxes, levies, duties, clearing charges, Insurance cost and any other charges/income.

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- DIBPL shall send its acceptance of the Client's offer, which will complete the sale of the asset to the Client by passing the title and risk to the Client. DIBPL may perfect the sale through signing Murabaha Sale contract (Exhibit C) with the Client.
- Subsequently, DIBPL would endorse the documents and hand them over to the Client.
- If the Client wants to pay the L/C amount from his own sources at the time of arrival of the documents, he may approach the Bank and arrange for the payment of the amount. The Bank shall recover, or would have already recovered, the L/C charge and it shall endorse the documents in favour of the Client. There would be no need for a Murabaha agreement.

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- In case of LC Sight, if the Client wants to pay the L/C amount from his own sources at the time of arrival of the documents, he may approach the Bank and arrange for the payment of the amount. The Bank shall recover, or would have already recovered, the L/C charge and it shall endorse the documents in favour of the Client. There would be no need for a Murabaha agreement.
- In case of LC Usance, if the Client wants to pay the L/C amount from his own sources at the time of payment, he may approach the Bank requesting it to revoke the Murabaha agreement against payment of some compensation to the Bank. This will be done at the time of settlement/payment by the Client and could/should not be pre-stipulated or pre-advised to the Client.