

**BANQUE DU LIBAN**

**Basic Circular No 96 addressed to Banks**

Attached is a copy of Basic Decision No 8870 of October 20, 2004 relating to Murabaha Operations carried out with or through Islamic Banks.

Beirut, October 20, 2004

The Governor of Banque du Liban

Riad Toufic Salamé

## Basic Decision No 8870

### Murabaha Operations carried out with or through Islamic Banks

**The Governor of Banque du Liban,**

**Pursuant to the Code of Money and Credit, notably Article 70 thereof;**

**Pursuant to Law No 575 of February 11, 2004 on Establishing Islamic banks in Lebanon, notably Article 4 thereof;**

**Pursuant to Basic Decision No 8828 of August 26, 2004, on the Functioning of Islamic Banks in Lebanon; and**

**Pursuant to the Decision of the Central Council of Banque du Liban, taken in its meeting of October 14, 2004**

#### **Decides the following:**

#### **Article 1: Definitions:**

For the purpose of implementing the provisions of this Decision, the following expressions shall mean:

Murabaha: The sale of an asset at its initial price and a known mark-up.

Ordering Party: The customer of the Islamic bank.

Ordered Party: The Islamic bank.

Asset: Any movable or immovable asset being the object of a Murabaha operation and fulfilling the conditions of Article 5 of Law 575 of February 11, 2004.

Murabaha for the Ordering Party: A sale negotiated between two parties or more who promise each other to execute the terms of such negotiation which provide that the Ordering Party requests the Ordered Party to purchase and acquire an asset, and promises to repurchase the said asset from the Ordered Party at a price including a profit through a subsequent sale agreement executed once the asset is owned by the Ordered Party.

Hamesh Al-Jiddiya (Seriousness Margin): The amount paid by the Ordering Party at the Ordered Party's request to ensure the seriousness of the Ordering Party's request. Thus, if the Ordering Party declines the mandatory purchase of the asset, the actual loss incurred by the Ordered Party will be covered

by the said amount. If the value of such amount does not cover the value of the damage suffered by the Ordered Party, the latter shall request the Ordering Party to settle the remaining uncovered loss. However, in case the amount exceeds the damage, the Ordered Party must return the remaining balance to the Ordering Party.

Murabaha Assets: All assets being the object of Murabaha operations.

Uncompleted Murabaha Assets: Assets held for the purpose of executing Murabaha operations that did not take place because of the Ordering Party's failure to fulfill his/her purchasing promise.

Provisions for Depreciation of Assets: An amount allocated to cover the depreciation of the value of Murabaha operations' assets and reconstitute the value of these assets at cost value or at market value, whichever is less.

Unrestricted Investment Accounts: 1

Restricted Investment Accounts: 1

**Article 2<sup>2</sup>:** This Decision shall govern any Murabaha for the Ordering Party that includes the latter's binding promise to purchase.

**Article 3:** The Islamic bank must apply to the customer the binding purchase rule in all Murabaha sales. Accordingly, the said bank must not enter into any Murabaha where the customer does not promise to purchase the asset that shall meet the required specifications.

**Article 4:** The agreement of the Murabaha for the Ordering Party must at least, expressly and accurately include the following elements:

- 1- The rights and obligations of the parties presented in a way that proves that the operation is a Murabaha for the Ordering Party.
- 2- The Asset object of the agreement.
- 3- The expected price and all expenses, fees and taxes paid by the Ordered Party, in addition to those due by the Ordering Party, particularly the agreed upon profits.

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<sup>1</sup>- This definition was repealed pursuant to Article 1 of Intermediate Decision No 12498 of April 10, 2017 (Intermediate Circular No 456).

<sup>2</sup>- This Article was amended pursuant to Article 2 of Intermediate Decision No 12498 of April 10, 2017 (Intermediate Circular No 456).

- 4- All guarantees submitted by the Ordering Party.
- 5- The Hamesh Al-Jiddiya prepaid in cash by the Ordering Party with a value that is not less than 15% of the total amount expected to be paid by the Ordered Party.
- 6- The mode of payment of the sale price by the Ordering Party and the penalties on arrears.

**Article 5:** The Murabaha accounts shall be recorded in accordance with the Annex attached to this Decision.

**Article 6:** Uncompleted Murabaha Assets may not be held by the Islamic bank for more than six months from the date they are categorized within the Murabaha accounts. In addition, the Central Council may impose on the Islamic any measure deemed necessary for the liquidation of these assets.

**Article 7:** In addition to the provisions of this Decision, and unless otherwise provided for, Islamic banks shall abide by all the provisions, regulations and principles applicable to non-Islamic banks.

**Article 8:** This Decision shall be effective upon its issuance.

**Article 9:** This Decision shall be published in the Official Gazette.

Beirut, October 20, 2004

The Governor of Banque du Liban

Riad Toufic Salamé

## **Accounting Treatment of Murabaha Operations**

### ***a- Promise to Purchase (first agreement executed in a Murabaha operation)***

The agreement is recorded as an off-balance sheet item at its face value, under “Commitments”. It is then credited upon the fulfillment of the promise (the second agreement executed in the Murabaha operation), or upon failure to fulfill at the same value as an off-balance sheet item under “Memorandum Accounts”.

### ***b- Assets related to Murabaha operations***

#### ***b-1 Murabaha Assets.***

These Assets are recorded at the date of the agreement to purchase at their historical cost as on and off-balance sheet items and in accordance with financing ratios, in addition to any other expenses borne by the bank for acquiring, owning or receiving the Assets. Any subsequent material change will be deducted from this cost before pursuing the promise to purchase and will be charged on the Ordered Party and/or investors’ accounts, in accordance with financing ratios.

#### ***b-2 Uncompleted Murabaha Assets.***

These Assets are re-classified at their book value under “Uncompleted Murabaha Assets” item. This value will be subsequently modified in case of any material change and this change will be charged to the Hamesh Al-Jiddiya. Any financial change resulting from a discrepancy between the market price and the book value (the modified cost) will be recorded under “Provisions for Losses in Asset Value” item.

### ***c- Provisions for depreciation in Asset value***

Should the market price of the Asset fall below cost, a provision equivalent to the value of the decrease must be set aside. However, if the market price rises again, an amount equivalent to the value of the increase will be released from the provision. The concerned assets shall be reevaluated, when preparing monthly financial statements, in order to set aside or release the provision.

### ***d- Hamesh Al- Jiddiya***

d-1 This cash margin amount is recorded on the balance sheet, under “Commitments”.

d-2 Upon execution of the second Murabaha contract, the Hamesh Al-Jiddiya recorded under “Commitments” (d-1) will be credited to “Murabaha sales receivables”.

d-3 Upon liquidation of Uncompleted Murabaha Assets, losses will be deducted from the Hamesh Al-Jiddiya. Any remaining balance will be restituted to the Ordering Party or, otherwise, any deficit will be recorded under “Receivables”.

**e- *Murabaha deferred sales receivables***

- e-1 Upon fulfilling the promise to purchase, the face value of the second contract is charged to the Ordering Party's account, under "Murabaha deferred sales receivables" on and off balance sheet, in accordance with financing ratios. The value of the provided guarantees, if any, will however be recorded off-balance sheet, under "Material or financial guarantees received in kind". These guarantees will be liquidated whenever they are no more needed or whenever they are acquired.
- e-2 In case the customer ceases to pay the amounts due, his/her account will be classified under "Doubtful deferred sales receivables", on and off balance sheet, in accordance with financing ratios. A provision for doubtful receivables shall be constituted against the portion of the Ordering Party, after taking into consideration the existing guarantees held by the latter.

**f- *Deferred profits***

- f-1 Upon fulfillment of the promise to purchase by executing a deferred sale, profits will be recorded in a deferred profits account under "Murabaha deferred sales receivables". Such profits will be qualified as revenues of the Ordered Party and/or returns to investors, in accordance with financing ratios on accrual basis (i.e. periodically).
- f-2 Upon recording the Ordering Party's account under "doubtful receivables", deferred profits will be classified accordingly. Upon the collection of each installment, these profits must however be qualified as revenues of the Ordered Party and/or returns to investors, in accordance with financing ratios.

**g- *Discount obtained after purchase/discount granted after sale***

- g-1 Discount obtained after purchase  
A discount obtained after the purchase of the Asset by the Ordered Party and before its resale is considered as a reduction in the Asset value. However, if the discount is obtained after selling the Asset, it will be qualified according to the Sharia board's opinion.
- g-2 Discount granted after sale  
When the Ordered Party agrees with the Ordering Party to grant the latter a discount due to his/her prepayment of one installment or more, the Ordering Party's account as deferred sales receivables will be reduced in parallel with an equal reduction in the deferred profits not yet qualified as revenues. Otherwise, revenues of the Ordered Party and/or returns to investors will be reduced in accordance with financing ratios.

**h- <sup>1</sup>**

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<sup>1</sup>- This paragraph was repealed pursuant to Article 3 of Intermediate Decision No 12498 of April 10, 2017 (Intermediate Circular No 456).