Flagship Report Corporate Governance in Lebanon:

ADVANCING THE STATUS QUO

Flagship Report Corporate Governance in Lebanon: Advancing the Status Quo

Developed by GOVERN, the Economic and Corporate Governance Center
On request of the Lebanese Institute for Finance and Governance
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ABOUT THE IFG

The Institute for Finance and Governance (IFG) was established at the initiative of the Banque du Liban to develop a center of expertise in finance and governance in Lebanon. Officially known as Banque du Liban, the BDL is the central bank of Lebanon; established in 1963, it is currently one of the most important economic institutions in the country.

The IFG is managed by the ESA Business School, which has become a leading academic center in the region in twenty years. Established in 1996, ESA is a Business School dedicated to the education of executives and managers in Lebanon and the Middle East. With its mission to form the elite of Lebanon and the region into the leaders of tomorrow, ESA has become a beacon of academic excellence within Lebanon, and a platform for interaction and meetings between Europe, the Middle East and Lebanon.

Officially inaugurated in June 2015, the Institute is based at the Villa Rose, on the ESA campus.

The IFG currently provides research and training on corporate governance for banks for corporate entities at large, with a focus on Lebanon but also for other countries in the region. The project on improving corporate governance in Lebanon that this report is a fundamental pillar of one of the flagship projects of IFG since its establishment. IFG's projects can be accessed at https://www.esa.edu.lb/en/ifg.

ABOUT GOVERN

GOVERN - the Economic and Corporate Governance Center is a niche advisory and research institute specialising in economic and corporate governance in emerging markets. We work alongside decision-makers to create legal and regulatory policies as well as construct institutions that promote business integrity, corporate governance and support the competitiveness of the region's capital markets and firms.

The Institute provides specialist advice on capital markets development and corporate governance to stock exchanges, securities regulators, Central Banks, Ministries, sovereign actors and other regulators in the region. The team is comprised of senior practitioners with experience in leading securities regulators, stock exchanges, banks, academia and international organisations.

GOVERN's experience developing policies for regulators and implementing them for corporates is complementary and gives us the flexibility to create teams of professionals with targeted regulatory, financial and economic experience. GOVERN Senior Advisors have accumulated expertise in a range of financial markets and governance matters as well as relevant academic and private sector experience.

With a decade long advisory and research experience in the Middle East, GOVERN experts have also spent decades working on corporate governance in other emerging markets as well as in Europe and North America. GOVERN has published a range of reports and articles on governance in the MENA region which can be accessed at www.govern.center

FORWORD

The adoption of good corporate governance practices has been of growing interest and policy importance across the Middle East region but subject to insufficient empirical research. Although Lebanon was one of the first jurisdictions in the region to pay attention to good governance practices, there is a dearth of analysis on both the policies introduced to support this and the practices in place in Lebanese companies. This lack of regulatory and company-specific analysis has in fact stymied the adoption of better practices in the country.

Although both regulators and the private sector have demonstrated an early interest in corporate governance at the same time as other leading jurisdictions in the region, this early interest was until recently not followed by corresponding regulatory advances and the private sector, dominated by family-controlled companies, has been reluctant to adopt internationally accepted governance norms.

Highlighting the opportunities for improvement in both the quality of the regulations bearing on corporate governance and their implementation, this Flagship Report on Corporate Governance in Lebanon seeks to provide an overview and analyse the regulatory framework for corporate governance in Lebanon and the extent of the progress realised by the private sector. These objectives were addressed through a dual approach, including regulatory benchmarking of Lebanon against select peer jurisdictions in the region and a survey of a wide range of Lebanese private sector companies.

The survey was disseminated to a cross-section of private sector firms of variable size, including industrial, trade, banking and other companies representative of the Lebanese economy. Responses to this survey present a first of a kind comprehensive overview of the progress and the difficulties of implementing of good governance practices in Lebanon, therefore allowing to develop of recommendations for the policymakers and the private sector.

The IFG is looking forward to building on the analysis and recommendations presented in this Flagship Report developed by GOVERN to develop governance tools and guidelines that can pragmatically help boards and executives improve corporate performance and sustainability. In parallel, it will be working with the regulators to enhance regulatory capacity in the area of governance and with Lebanese companies to respond to their diverse priorities and needs, all with a view to improve the competitiveness of the Lebanese economy.

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For the regulators

The Lebanese Code of Commerce (hereafter CC) contains a number of provisions bearing on corporate governance such as the separation of CEO and Chairman posts and unlimited personal liability of board members which require to be revised in order to allow the regulators to amend the relevant provisions in their guidelines and circulars.

* * *

The Code of Commerce also needs to be amended to address shareholder rights more comprehensively, notably with the respect to percentage of shares needed to call a general and an extraordinary assembly. In most MENA countries such quorum is set at 5 or 10% and a similar threshold should also be adopted in Lebanon. The deadline by which shareholder assemblies must be held should also be specified.

* * *

Details such as notifications for shareholder meetings, cumulative voting and other mechanisms that facilitate the exercise of shareholder rights are not addressed by the existing legislation. These should be explicitly addressed both for regulated and for privately held firms. Likewise, the Ministry of Economy which receives the financial reports of privately held companies may request essential information on board composition and aim to improve disclosure to shareholders.

* * *

The requirement for board members to hold shares should be amended considering it leads to legal complications in practice, requiring controlling shareholders to selling and re-purchase shares. It also negatively impacts the ability of companies to recruit and regularly change independent board members as owners of privately held companies would, by Lebanese law need to cede a part in it.

In light of the ambitions to further develop the capital market in Lebanon, the regulators might wish to consider how the regulatory responsibilities in the area of corporate governance will be addressed in the eventuality that the Beirut Stock Exchange is privatised as envisioned by the 2011 Capital Market Law.

* * *

Other sectoral regulators (i.e. Insurance Control Commission) should consider introducing specific guidelines based on the relevant international standards such as the OECD Guidelines for Insurer Governance. Sectoral associations such as the Association of Insurance Companies of Lebanon (ACAL) can be a useful conduit in this regard. Insurance companies owned by banks may be the most pragmatic target to initiate this as they can leverage existing expertise in the banking sector.

* * *

The BDL and the Association of Banks have an important role to play in encouraging corporate governance not only as the regulator of the banking sector but also to stimulate banks' role in promoting governance in their lending and investment activities. For instance, it could be suggested for the BDL to introduce a set of voluntary corporate governance criteria for banks to consider in their lending decisions.

* * *

The regulators might wish to consider introducing more rigorous provisions, at least for non-executive and independent directors in terms limiting the number of concurrent board appointments they may hold, which will likely have multiple effects of forcing some board turnover, focusing directors on their duties but also perhaps encouraging companies to consider tapping into board pools beyond Lebanon.

For the banking sector

Considering the large number of banks in Lebanon, the governance framework for banks should introduce a concept of scalability in order to allow for bank governance frameworks to be appropriate to their size and complexity. This can be accomplished by introducing some mandatory provisions complementing them with recommendations which can be introduced on a comply-or-explain basis. This approach may lead the regulator to focus on systemically important banks.

* * *

Introducing a comply-or-explain culture in Lebanese banks might be beneficial to ensure boards and executives reflect on and justify their decisions as opposed to merely transposing the BDL recommendations in banks' own corporate governance codes which they are required to establish. Some aspects such as the number of board committee meetings may be useful to leave to such mechanisms. Furthermore,

BDL Circulars that pertain to corporate governance of banks could be collectively reviewed considering that they were adopted prior to the last revision of the Basel Corporate Governance Principles and the G20 OECD Principles on Corporate Governance with a view to identify any gaps. The BDL may wish to consolidate regulations in a single code on governance of banks which could be periodically amended to reflect industry developments, international best practices. Furthermore, the regulatory authority over listed banks should be clarified by the BDL and the CMA and made clear to the banking community.

* * *

BDL may wish to introduce a more rigorous process for approval of bank directors replacing the current process where the Council of Governors approves all new appointees (subject to lack of criminal record and good business reputation). This can be accomplished by introducing criteria for bank board members which includes specific criteria for the "fit and proper" requirements including lack of conflicts of interest. Similar provisions should apply to executives which may be in position to benefit from information about business opportunities/client information by virtue of their positions.

* * *

The appointment of qualified bank directors could be facilitated by board evaluations which are currently not mandated for banks. As a result, very few banks (i.e. Audi, BLOM) practice board evaluations and smaller banks are not familiar with the concept. Periodic board evaluations would facilitate a structured board renewal as well as identification of gaps in skills of board members. Board renewal is important considering that the number of successive board mandates are not limited.

* * *

The Central Bank may consider introducing specific arrangements to limit the number of members of the same family on the board in order to make sure that bank boards function less as family boards and more as corporate boards. Alternatively, it may be recommended that the CEO/General Manager role has to be performed by a non-family member, on a comply-or-explain basis. This would require banks to justify how family members are suitable for senior executive posts.

* * *

Monitoring the governance arrangements of banks in Lebanon is largely the responsibility of the Banking Control Commission (BCC). It reviews governance codes of individual banks and monitors the implementation of all BDL circulars bearing on governance through on- and off- site supervision mechanisms. A less compliance-oriented and more culture-oriented supervisory approach being adopted by BCC staff would help direct efforts of bank board and executives towards introducing the right governance culture. The BCC might wish to consider dedicating a specific section of their annual report to corporate governance of banks.

* * *

It may be beneficial for the Chief Risk Officer to report to the Risk Committee lead by an independent board member as opposed to the board as a whole which is led by the Chair/CEO who is generally also the owner of the bank. While the incentives of owners of family-owned banks are aligned with banks' long term performance, board Chairs/CEOs who are also owners may be able to unduly influence personnel and to circumvent normal risk management processes.

* * *

It is important to establish specific more detailed criteria for independence which in many countries globally and in the region is defined by a set of negative requirements when an individual is not regarded as independent. While the CMA's definition of independence contained in the Listing Rules is broadly in line with international definitions, the BDL does not specifically define independence requirements. An enhanced definition of independence for the banking sector is needed to introduce truly independent directors on boards.

For the non-financial sector

Most family businesses, which dominate the corporate landscape in Lebanon, have yet to introduce some formal governance arrangements. The awareness of the Code of Corporate Governance developed by the Lebanese Transparency Association appears to be low. Pragmatic guidelines for family businesses of various size and sector are needed for family businesses to introduce family constitutions and board charters to address their decision making, succession planning and long-term sustainability.

* * *

Further efforts aimed at raising awareness of the benefits of good governance should be deployed as business owners do not necessarily see the value of introducing good governance rules. Family groups can benefit from guidelines and practical toolkits to implement governance frameworks (i.e. family constitutions, etc.). Chambers of Commerce could be a useful conduit to offer such tools to companies that may be looking to restructure their governance arrangements.

* * *

There is a significant disparity between the awareness of the importance of good corporate governance among the regions of Lebanon. Notably, while firms that belong to the Beirut Chamber of Commerce and Industry appear more sensibilised as to the benefits of good corporate governance, members of other Chambers (Saida and the South, Tripoli and the North, Zahle and Bekaa) have less developed, largely informal governance and require more support.

* * *

A few Lebanese corporate groups such as SABIS and HOLCOM are recognised as having leading corporate governance practices. Further effort to understand how these were introduced should be made, including by developing case studies on leading firms and using them as examples in awareness-raising campaigns. Companies should also be sensibilised as to the consequences of not introducing good governance arrangements.

* * *

The quality of disclosure practices by unlisted firms is rather low and requires further consideration. Limited liability companies (SARL) are by law required to have 2 auditors but few publish their results though a dedicated website or otherwise. Disclosure of financial results would be important to address by the Ministry of Economy, especially for firms that have minority shareholders who should have access to the performance of companies they have invested in.

* * *

The introduction of a director representing minority shareholders would be useful to consider in Lebanon where informed observers question the actual independence of directors appointed on boards of banks and listed companies. Further measures to enhance director independence such as limits on successive terms can be considered by regulators and companies to enhance board objectivity and effectiveness.

* * *

The presence of women on boards of Lebanese companies remains limited and driven largely by the appointment of daughters on the boards of family-owned companies. Even in family-owned companies, the participation of women on boards is limited by cultural and historical traditions whereby male offspring is usually appointed first and where transition of businesses to daughters is limited since company founders are concerned that firms will not remain "in the family".

* * *

Banks and large firms should be encouraged to introduce dedicated, professional board secretaries. Already, a number of large financial and non-financial sector firms have introduced corporate secretaries to professionalise the conduct of board meetings and larger corporates should consider introducing this role, at the minimum using executive team members. For larger companies with outstanding public equity, the role of the investor relations officer should also be introduced.

PART I. EMERGENCE OF A REGULATORY FRAMEWORK

Global and regional context

In the wake of the second most significant financial crisis in global economic history, the importance of sound corporate governance is now recognised globally and policymakers have been active in recent years creating and fine-tuning domestic governance regulations. The G20/OECD Principles on Corporate Governance updated in 2015 suggest that effective corporate governance requires a sound legal, regulatory and institutional framework that market participants can rely on when they establish their private contractual relations.

In the Middle East region, the development of governance laws, rules and recommendations started in early 2000 as a voluntary effort, with regulators, private sector associations and civil society formulating national governance recommendations to inspire better governance implementation. This has had an important impact on raising the awareness of international governance norms and on improving governance practices of listed companies across the region.

The financial crisis in the Gulf in 2006 has led to the institutionalisation of the securities regulators in the region and to more rigorous application of corporate governance regulations for listed firms. Over the years, most regulators in the region – whether securities or banking – have moved towards comply-or-explain or mandatory approaches and now all but one country in the region have a national corporate governance code, which have been progressively reviewed to align with international standards.

Corporate governance regulations and frameworks in the region are dynamic, responding to international regulatory developments such as the revision of the OECD Principles of Corporate Governance and the Basel Committee Guidelines for Banks, with a number of jurisdictions revising their codes in recent years (i.e. Oman in 2015, Saudi Arabia in 2017), listing requirements (i.e. Egypt and Saudi Arabia in 2016), and corporate laws (i.e. Kuwait in 2014, UAE in 2015, and Saudi Arabia in 2016).

The growing competition for portfolio investment, not only among oil-importing but also among oil-exporting countries of the Arabian Gulf, is expected to have a growing positive impact on the adoption of governance standards that correspond to the expectations of international investors. Corporate governance is also becoming critical in Lebanon as the country seeks needs to attract regional and international capital and support the internationalisation of domestic firms.

Evolution of governance standards in Lebanon

Key provisions on corporate governance in Lebanon are enshrined in the Code of Commerce (originally issued in 1942 and subsequently revised) which establishes basic standards, notably with respect to board composition, remuneration and liability. Considering that the law is dated, several of its provisions are not in line with internationally recognised corporate governance practices.[1]

On the contrary, a number of its articles such as the combination of Chair and CEO posts and the establishment of unlimited personal liability for board members are problematic from the perspective of advancing good governance. In fact, these provisions – the modification of which require a Parliamentary approval – constitute an impediment for the regulators to issue more modern governance standards as they would be inconsistent with some aspects of the Law and hence illegal.

The Lebanese corporate governance framework has been developing slowly by regional standards and until recently with the focus on the banking sector as it underpins the Lebanese economy. This is consistent with the approaches taken in other countries of the region where the banking sector was the “cradle” for the development of governance rules. Unlike most other MENA economies however,

1 For a full list of governance relevant provisions contained in the Code of Commerce, refer to Annex I.

the low level of equity market development in Lebanon has not facilitated the adoption of governance rules or recommendations beyond the banking sector.

As a result, the key actor involved in raising the standards of governance historically has been the Central Bank of Lebanon (Banque du Liban, hereafter BDL) which starting in 2006 has issued a number of governance-related circulars. Considering that the Capital Market Authority (CMA) was established only in 2013[2], the regulatory framework for listed companies – including on corporate governance - was developed late by comparison with other jurisdictions in the region.[3]

For privately-held firms, the drive to establish better governance standards in Lebanon has emanated from the civil society. Notably, the Lebanese Transparency Association (LTA), established in 1999 as a chapter of Transparency International, was the initial force behind raising awareness of the importance of good corporate governance. The LTA launched the Lebanese Corporate Governance Taskforce (LCGT) in 2002, comprised of public, private and civil society stakeholders which developed the country's first Corporate Governance Code in 2006.

The intention of the Code was to establish a set of progressive recommendations for the private sector, beyond the provisions included in the Code of Commerce. The Code was developed primarily for Lebanese joint stock companies (Societe Anonyme Libanaise, hereafter SAL) and in particular targeted family-owned companies as they are known to represent the vast majority of the economy. While the Code served as the first awareness raising tool, primarily used by the LTA and the Lebanese Institute of Directors, its impact appears to be limited.

Considering that until now there have been no empirical studies measuring the evolution of governance in Lebanon, it is challenging to determine the impact of the Code and this is indeed the gap this first comprehensive report on the state of corporate governance in Lebanon is seeking to address. The IFG is subsequently seeking to develop a set of recommendations on corporate governance for privately held firms, based on the conclusions of this research, and on the conclusions of the round tables it conducted with the various professional associations.

2 Although it was established by law in 2011, the CMA became operational in 2013.

3 Along with the Kuwait, Lebanon was one of the last countries in the region to have introduced a securities regulator.

A major evolution of the corporate governance framework was realised as a result of the adoption of the Capital Markets Law 161 in 2011 which established the CMA with responsibility, inter alia, to introduce and enforce corporate governance rules. Given the small size of the capital market, with less than a dozen issuers and representing less than 10% in terms of the GDP, the CMA has focused on regulating the activities of market intermediaries, issuing notably Business Conduct and Market Conduct Regulations in 2016.[4]

The Business Conduct Regulation (3201) addressed to the market intermediaries the CMA supervises, contains provisions on corporate governance that are rather general. In essence, the Regulation suggests that the governance organs must have the necessary authority and means to oversee the implementation of corporate objectives. Most governance-related provisions of the regulation provide general recommendations as opposed to binding regulations: for instance, the introduction of the Audit Committee is recommended but not mandated.

4 Business Conduct Regulations (3000) is intended to address the conduct of market intermediaries, in terms of notably customer interactions, governance and recordkeeping. Market Conduct Regulations (4000) further address market integrity issues by prohibiting insider dealing and market manipulation.

Requirements for listed companies

CMA's Listing Regulations address corporate governance requirements for listed companies and apply to new and existing issuers, superseding any other rules and regulations issues in earlier years. The Listing Regulations (7301) were developed in preparation for the planned restructuring of the stock exchange, anticipated to result in a much needed influx of new issuers to revitalise the Beirut Stock Exchange.[5]

The Listing Regulations contain a number of governance provisions, including on shareholder rights, the conduct of AGMs, board composition and disclosure. The CMA Listing Requirements are in some respects more comprehensive and rigorous than BDL's requirements.[6] For instance, the

5 The Capital Market Law adopted in 2011 previewed the privatisation of the Bourse de Beirut two years following the introduction of the CMA.

6 For instance, the CMA regulations are more detailed than those of the BDL on board composition issues. Refer to Annex III for a detailed summary of the requirements and their benchmarking against select MENA jurisdictions.

CMA establishes an optimal board size and recommends that the majority of the board must be non-executive and at least one-third independent, whereas banks need to have 3 independent board members.

The Listing Regulations also address shareholder rights, requiring issuers to treat all holders of each class of its listed securities equally and ensure they have equal access to disclosure, reports and other information. They also address disclosure practices, by requiring issuers to prepare audited annual financial statements in accordance with International Financial Reporting Standards (IFRS) and to have interim and annual financial statements approved by the board (7305).

In principle, the CMA's and BDL's requirements are similar. Similarly to the BDL regulations, the CMA requires all issuers to establish and disclose a corporate governance policy. However, unlike the BDL requirements which are mandatory, issuers would have to disclose their adoption of the CMA Listing Rules in their annual report on a comply-or-explain (CoE) basis. This is the first time the CoE approach been introduced in Lebanon.

While some Lebanese banks are listed, the BDL retains the exclusive responsibility for the oversight of their corporate governance, including for banks with listed equity[7], with the exception of banks' brokerage activities.[8] Discussions with Lebanese banks have highlighted that they are unaware of how supervisory responsibilities will be carried out and coordinated between the securities and banking regulators. This an important point to address to establish a clear regulatory framework.

The Listing Requirements supersede the requirements of the Beirut Stock Exchange (BSE). The BSE is a government-operated entity, and is currently the only exchange operator in the country, though its privatisation is planned as per the Law 161. At the time of the preparation of the report, timelines for privatisation were unclear, pending a Parliamentary decision.[9]

7 According to the Listing Requirements, a listed issuer must comply with any binding requirements on corporate governance set out in laws, circulars of the Banque du Liban or other regulations that apply to the issuer.

8 Further to its Circular 437, the BDL has requested all banks that do not already have an investment banking activity to establish a brokerage business: while the commercial banking operations will be fully overseen by the BDL, while brokerage activities will be overseen by the CMA.

9 This is despite the fact that despite the deadline for the privatisation of the BSE set in the Capital Markets Law has already expired.

The current proposal submitted to the Parliament entails the privatisation of the BSE and the creation of another tier of the exchange with more flexible listing requirements which would be operated by the same entity.

Though in principle, the exchange has some regulatory functions[10], it is not an active regulatory entity. In theory, the BSE has by virtue of its by-laws the mandate to protect the interests of all public equity investors as well as to oversee the activity of issuers and the disclosure of public company information to brokers. Indeed, the stock exchange has played a greater role prior to the introduction of the CMA, notably with respect to facilitating disclosure by listed issuers.

Considering a lack of listings, the application of the CMA's new Listing Regulations remains untested. Indeed, very few large Lebanese companies have accessed public equity markets and were as a result encouraged to re-evaluate their governance frameworks according to the standards of other jurisdictions. Only 4 Lebanese companies currently trade on the London Stock Exchange (Bank Audi, BLOM Bank, Byblos Bank and Solidere).[11]

10 The BSE has the right to issue regulatory circulars that deems necessary to ensure the proper functioning of the Stock Exchange. (Trading, listings, Issuing brokers licenses, transparency and disclosure, etc). Until the establishment of the CMA, issuers signed a contract with the BSE requiring them to provide certain information to the exchange such as the minutes of its meetings, changes in ownership and generally speaking all material disclosure announcements.

11 Solidere was previously also listed in Kuwait but this arrangement was terminated due to differences in the supervisory and disclosure regimes.

Requirements for banks

Considering the slow development of the equity market in Lebanon, it is unsurprising that the most rigorously regulated sector in terms of corporate governance has been the banking sector. The banking sector is also the largest contributor to the country's economy, with 69 banks operating in Lebanon, of which 19 investment banks (Association of Banks in Lebanon, 2016). The role of the banking sector is similarly important in other countries of the MENA region where it remains approximately 3-4 times larger than equity markets.

Unlike other countries of the region that have opted for a comprehensive bank governance code (refer to Table 1 hereafter), the BDL has issued a series of circulars bearing on corporate governance over the 2006-2016 period.[12] In essence, the Central Bank requires banks to formulate their own codes of good governance and to publish a summary thereof in their annual report. The nature of these codes is left quite general, although there are specific requirements concerning disclosure of the structure of the board as well as succession planning.

12 The key BDL decisions bearing on corporate governance include notably circulars 106 (on corporate governance of banks) and 112 (on corporate governance of Islamic banks), they have been supplemented by other circulars on risk management, establishment of specific board committees, etc.

Table 1. Bank Corporate Governance Codes in the Middle East

Country	Bank Guidelines	Date
Algeria	No	-
Bahrain	Yes	2015
Egypt	Yes	2011
Iraq	No	-
Jordan	Yes	2007
Kuwait	Yes	2012
Lebanon	Yes	2006-2016
Morocco	Yes	2010
Oman	Yes	2014
Palestine	Yes	2014
Qatar	Yes	2008
Saudi Arabia	Yes	2014
Tunisia	Yes	2011
United Arab Emirates	Yes	2009
Yemen	Yes	2013

Source : GOVERN Research, 2017.

A number of BDL circulars bear specifically on board and committee composition. The BDL refers to the Basel Committee Corporate Governance Guidelines, which require boards to have a "sufficient number of independent and non-executive directors". Though there are no specific requirements on the presence of non-executives, BDL requires that the Audit, Compliance and the Risk Committees are headed by independent chairs who cannot simultaneously sit on another committee. This implies that bank boards in Lebanon should contain at least 3 independent board members out of a maximum 12 members (i.e. at least 25% of the board must be independent).[13]

The BDL has introduced additional provisions for Islamic Banks, notably requiring them to introduce a Corporate Governance Unit to monitor the implementation of good governance practices and a Sharia Auditing Unit whose function is to evaluate and monitor the compliance of banking operations with the opinions of the Consultative Body on Shari'a compliance. These apply to a limited number of banks as the vast majority of Lebanese banks are conventional. Few Lebanese banks have adopted Shari'a Boards, for example Banque Audi has adopted one.

A number of the issues covered by the BDL regulations are furthermore addressed by the Corporate Governance Guidelines for Banks issued by the Association of Banks in Lebanon (ABL) in 2011, based on international best practices.[14] Similarly to the Basel Committee's and OECD's recommendations, these Guidelines are formulated as an aspirational standard. While Lebanese bankers refer to the requirements imposed by the BDL, few refer to the recommendations of the ABL though they are in some respects more comprehensive.[15] ABL's recommendations address notably banks' interactions with the BDL and the Banking Control Commission (BCC).

The BCC is the entity responsible for bank supervision in Lebanon, which represents a unique supervisory approach

13 In practice, bank boards rarely reach 12 members and hence the independence requirements imposed by the BDL are comparable with those imposed by other jurisdictions in the region.

14 The ABL, and notably its Corporate Governance Committee, reviews regulatory BDL drafts and provides industry comments. The Governor of the BDL also meets with the head of the ABL on a monthly basis.

15 For instance, on issues such as board evaluations and governance of subsidiaries which are not specifically addressed by the BDL, ABL recommendations are more specific.

in the region where this function is generally performed by Central Banks. The BCC follows closely banks' operations and reviews governance protocols and processes at banks on a regular basis through both on- and off-site supervision. It reviews governance codes of individual banks and monitors the implementation of all BDL circulars bearing on governance through reporting provided by banks based on BCC reporting templates which are more detailed than the public filings made by banks.[16] It is noteworthy that the capital adequacy assessment includes a yearly review of bank governance which may lead to capital surcharges in case of deficiencies.

On the other hand, the Corporate Governance Unit of the BDL is charged with policymaking responsibilities and does not monitor governance of banks. The Unit tracks board memberships in Lebanese banks which are approved by the Central Council of the BDL composed of the Governor, Vice Governors and 2 ex-officio directors representing the Ministries of Economy and Finance.

16 Banks are required to submit meeting minutes immediately after board meetings to the BCC for review.

Market forces

The market forces for the adoption of good governance in Lebanon have been weak. The size of companies comprising the Lebanese corporate sector has been an important barrier to the adoption of good governance.[17] In addition, the challenging economic climate that has characterised recent years implies that family founders are preoccupied with more pressing commercial imperatives and perceive governance as an additional cost as opposed to a source of value.

Considering that the majority of Lebanese companies are not listed, their governance arrangements are legally subject only to the Code of Commerce. Beyond these basic requirements, few firms appear to have institutionalised formal corporate governance frameworks. Only a few large family groups (e.g. Debbas, Fattal, Malia, etc.) have introduced formal governance frameworks. Of these, very few corporate groups such as SABIS are recognised as leaders in corporate governance.

17 UNIDO has estimated that enterprises employing more than 50 employees account for only 0.05% in the agricultural sector, 0.1% in the service sector, 0.63% in industry and 0.3% in the leisure sector.

Fundamentally, the family-dominated nature of most of Lebanese companies (including banks), coupled with weak equity market development, have stymied the adoption of good governance principles in Lebanon. Specific motives such as succession planning, company diversification and entry of new investors into capital has motivated the evolution of governance standards in family firms. In most cases, these pressures have resulted in the establishment of holding companies with governance structures to oversee subsidiaries operating in specific sectors.

For instance, the HOLDAL group, which has been recognised for its social impact across the Arab world, was established to oversee a growing number of operating companies across a range of sectors. The company sees its corporate governance transformation as a decade long process which started in 2010 and which include the company's employees and customers.

Few privately held firms have decided to adopt progressive governance standards due to the patriarchal corporate culture whereby companies have historically been led by the Chair/CEO. The reluctance of Chairs to devolve their powers to other executives is reinforced by the existence of ultimate legal responsibility of the Chair. This has incidentally also stymied the appointment of outside, non-family member CEOs which has been demonstrated to be a critical success factor to the professionalisation of Lebanese companies (i.e. Debbas, BLOM, etc).

The appointment of an outside CEO is generally seen as a long-term process and generally undertaken after significant governance changes at the level of the family and the board have already occurred. For instance, the HOLDAL Group will be seeking to introduce a non-family CEO following a decade-long process to restructure the governance of the family holding, which started with the introduction of independent directors. In the case of HOLDAL, the family has decided that they wish to bring in professional management team which adheres to the values of the owners.

A number of observers believe that introducing a CEO who is not an owner is important to professionalising the conduct of banks and other firms, as the relationship between a professional CEO who is not a major shareholder and other executives or employees tends to follow the established line of accountability, whereas an owner-CEO may be in position to exercise undue pressure on employees. Some, however, felt that it is precisely this alignment between ownership and management incarnated in "owner-CEO" that has reduced short-termist tendencies.

This example echoes the general challenges of introducing formal governance arrangements in Lebanon which imply, at some level, the separation of family and corporate governance. This has indeed been a key challenge in the wider region, where the governance of family-owned firms has been under spotlight considering their systemic importance to the local economies.[18] Although exact figures on the transition of Lebanese companies to the next generation are not available, their long term sustainability is far from guaranteed in the absence of a clear governance framework.

Indeed, the survey and interviews with stakeholders in Lebanon highlighted that succession planning is the most common reason for the implementation of governance arrangements, including modifications to company by-laws and the introduction of family constitutions. In a minority of cases, the introduction of an outside shareholder or partner has also necessitated the introduction of formal governance arrangements, notably guaranteeing their board representation.[19]

At the same time, considering that most firms finance themselves either through internal sources or though bank finance, there has been relatively little external pressure to adopt good governance requirements. Few financial (i.e. Bank Audi) and non-financial firms (i.e. Rifai) that have external shareholders have moved to introduce better corporate governance practices, including stronger boards, professional management, and non-family member CEOs, leading to a less concentrated decision making structure.

The introduction of outside investors, notably private equity (PE) players, has had a positive impact on corporate governance. Private equity has been and has the potential to be an important source of investor-driven governance improvements as the country has no other active, developed sources of institutional capital (i.e. pension funds, insurance companies, etc.). Indeed, Lebanon has

18 In the GCC for example, an estimated $1 trillion USD of assets will be handed over to the next generation over the next 5-10 years (Economist, 2015).

19 Interestingly, interviews revealed that most families are unfamiliar with the concept of dual voting rights that are attached to their shares. Apparently, it does not seem to pose an issue vis-a-vis outside investors' entry into capital of Lebanese companies as in practice this provision is not used.

been identified as one of the top 3 markets for private equity in the region.

According to a recent survey by Wamda, 35% of funds plan to increase their activity in Lebanon and indeed the number of investments in 2009-2013 has increased (Wamda, 2014). Whereas in 2014, over 75% of investments by value were concentrated in the UAE and Saudi Arabia, in recent years Egypt, Jordan, Tunisia and Lebanon increasingly account for more deals (MENA PE Association, 2016).

In addition, the BDL circular 331 introduced in 2015 has encouraged banks to invest in innovative enterprises and has further spurred the development of the PE in the country. The prevalence of SMEs in the economy and support from the BDL have stimulated PE/VC activity and are reported to have boosted the Lebanese start-up environment. The awareness of good governance is growing among the new wave of start-ups as they are seeking to attract capital.

Regional benchmarking

The adoption of good governance rules is an interplay between several factors, including regulatory pressure, company-specific needs, and investor pressure. As described above, regulatory pressure has not been a major factor in Lebanon so far apart from the banking sector. Institutional investors such as pension and mutual funds and insurance companies have so far had no impact on corporate governance since they are small relative to the size of the economy.

To date, efforts by policymakers and the civil society have not so far substantially improved the implementation of governance practices in Lebanon, with the result corporate governance is today not a priority for the corporate sector. At the same time, no surveys have been undertaken to address the evolution of corporate governance practices in Lebanon in a regional or international context. In order to address this void, a benchmarking of key aspects of the regulatory framework in Lebanon was conducted for the purposes of this report.

Overall, the regulatory requirements in Lebanon are in some respects less developed than those of leading jurisdictions in the region.[20] Currently, the Listing Requirements and the BDL Circulars are the most comprehensive source of corporate

20 It bears to note that these countries have more developed equity markets than Lebanon and hence the securities regulators have had more leverage to encourage the introduction good governance principles.

governance rules in the country but apply to few companies (less than 70 firms). Annex III provides a benchmarking of key corporate governance provisions in Lebanon vis-à-vis select Middle East countries, including Egypt, Bahrain, the UAE, Saudi Arabia.

Lebanon's governance framework stands out in terms of the regional norms in a number of key respects. Notably, the separation of Chair and CEO roles, which has been mandated or recommended in most other countries of the region is not required and is indeed forbidden by law. By virtue of the Law, the Chairman in Lebanese companies behave more like executives and are considerably more "hands on" than peers elsewhere.

In practice, a number of banks have effectively separated the two posts by appointing an assistant General Manager or equivalent[21] or alternatively, establishing several functional heads of departments. For instance, Al Mawarid Bank Chair/CEO has delegated his operational authority to 3 senior executives. Furthermore, some banks and larger corporates have appointed an assistant General Manager who is not a family member, which effectively liberates the Chair/CEO to take a more hands off approach and focus on governance at the level of the board.

Importantly, in terms of shareholder protections, progress remains to be made. One issue in terms of the exercise of shareholder rights in Lebanon is the dual voting shares which exist in all companies by virtue of the Code of Commerce.[22] In the Lebanese context, this provision allows the entrenchment of family shareholders at the expense of other investors. For this and other weaknesses in shareholder protections, the World Bank has ranked Lebanon 145 out of 190 economies in terms of protecting minority investors, against a regional MENA average of 121 (World Bank, 2017).

21 It is not possible to distinguish between the functions of Chairman and General Manager; the Chairman-General Manager may, however, suggest to the board the appointment of an assistant General Manager who will act on his behalf and at his or her personal liability. This practice remains still common in Egypt, Morocco, Tunisia and to a lesser extent in Kuwait.

22 Without prejudice to the double voting power which is the privilege of holders of registered shares for at least two years beforehand, each shareholder has as many votes as the shares he holds or represents, without limitation thereon, unless such limitation is formally provided by the Articles, and on condition it is identical for all shares, irrespective of the category to which they belong.

PART II. SURVEY RESULTS & ANALYSIS

Methodology

While listed companies and banks are required to comply with the existing regulatory requirements, these companies represent a relatively negligible part of the overall corporate sector in Lebanon. Until now, little information has been available on governance practices in the overall corporate sector. To collect this data and information, GOVERN has developed a comprehensive 50 question online survey that was distributed in 2017 to a range of Lebanese private sector companies, including industrial, financial and services sectors.

The survey was a first-of-a-kind effort to collect data and information on the Lebanese corporates and sought to gather views from the board members and senior executives on practices, challenges and views on improving corporate governance in Lebanon. The survey was disseminated widely to sectoral associations, chambers of commerce, large family groups and banks in order to constitute a representative sample. Over 40% of respondents represented industrial (42%) and financial sectors (29%), with trade and services occupying third and fourth positions respectively.

While this does not reflect the composition of the Lebanese economy, it represents the sectors where large companies are active. The majority of respondents represented companies with assets over 100 million USD (38% of the sample) that have implemented formal governance structures. The sample size is also skewed to larger companies (banks, listed and large family holdings) as smaller firms that have not introduced governance practices. Likewise, there is a bias towards firms from the Beirut governorate as firms in other regions of the country are less sensibilised of the importance of good governance.

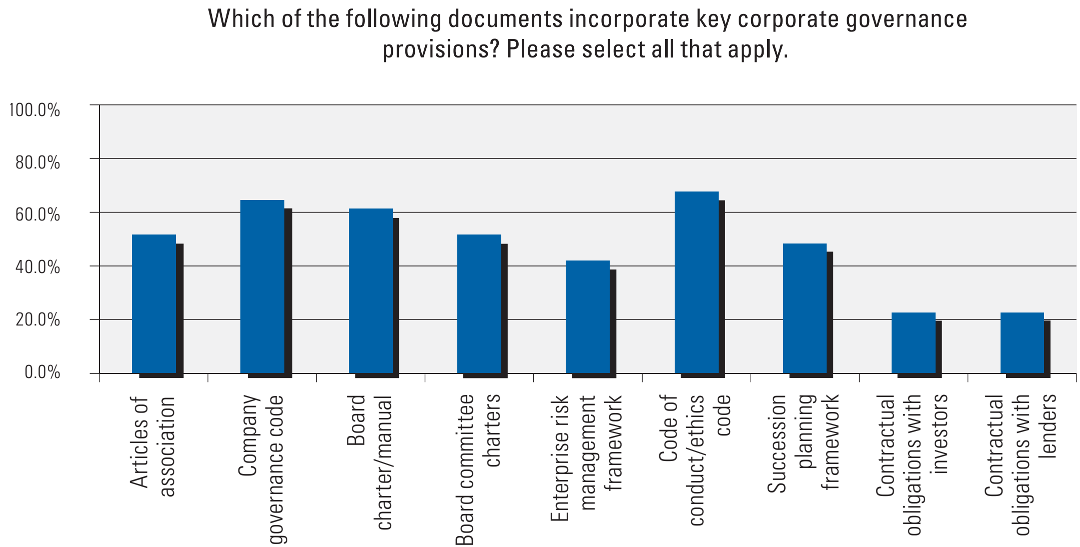
The respondents most frequently occupied the role of the CEO or a board member, while other roles such as Chief Risk and Compliance Officers were less represented. Close to 75% of respondents were male, which reflects the low representation of female in executive and board positions in Lebanon. Female representation on boards is indeed an important theme that will be treated in this report. Important differences can be noted when analysing the results by gender, but also type of the respondent and type of company which will be highlighted throughout the report.

Unsurprisingly, the ownership of companies in the sample was controlled by a few key investors (61%), mostly by a single family. While a few Lebanese banks and family holdings have accepted outside investors, resulting in an ownership structure characterised by a few blockholders, these still accounted for a relatively small portion of the sample (16%).The majority of respondents (77%) were organised as joint stock companies (SAL) whereas less than 10% of firms were organised as limited liability (SARL) or holding company structures, respectively.

Company governance frameworks

Despite the fact that the survey responses were naturally skewed towards larger firms, not all companies in the sample had formal governance frameworks, including a corporate board. Most companies have responded that governance requirements are encapsulated in the articles of association, company corporate governance code, board and committee charters. Interestingly, close to 68% of the sample commented that they also have a code of conduct or a code of ethics.

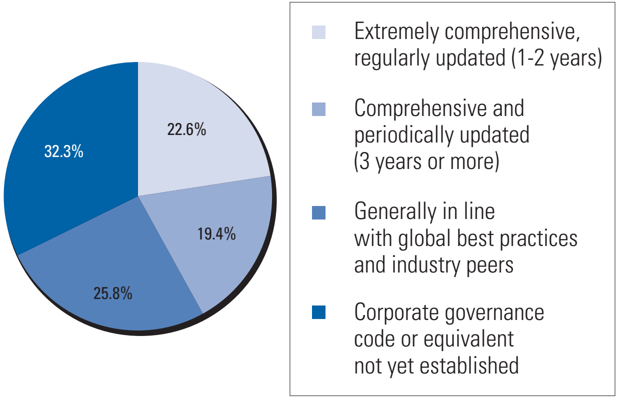
Figure 1. Source of Corporate Governance Provisions



About 40% of the respondents believe that their governance framework is comprehensive and regularly or periodically updated, while 32% note that they have not yet established a corporate governance code or equivalent. Approximately a quarter of the respondents believe their corporate governance framework to be in line with international best practices.

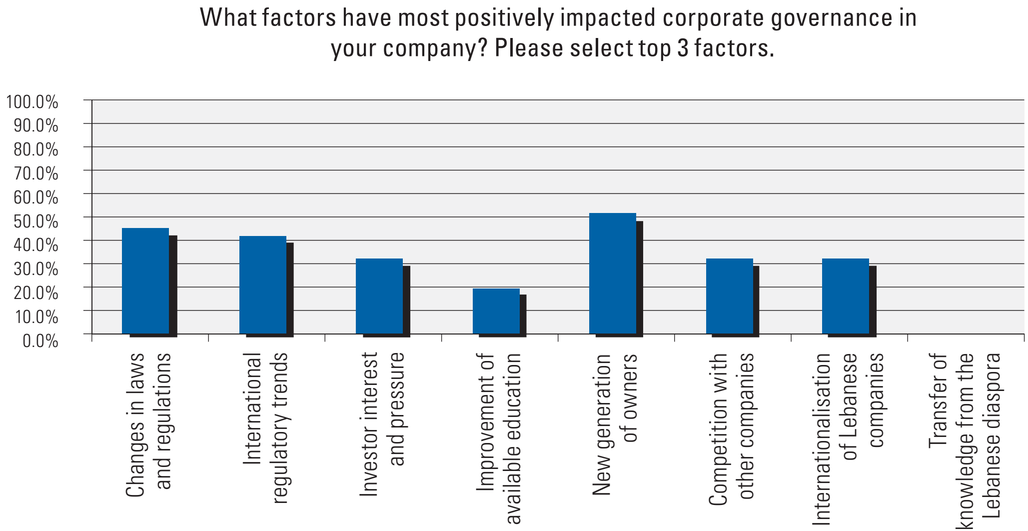
Figure 2. Comprehensiveness of Company Governance Code/Framework

How comprehensive would you assess your corporate governance code/documents to be?



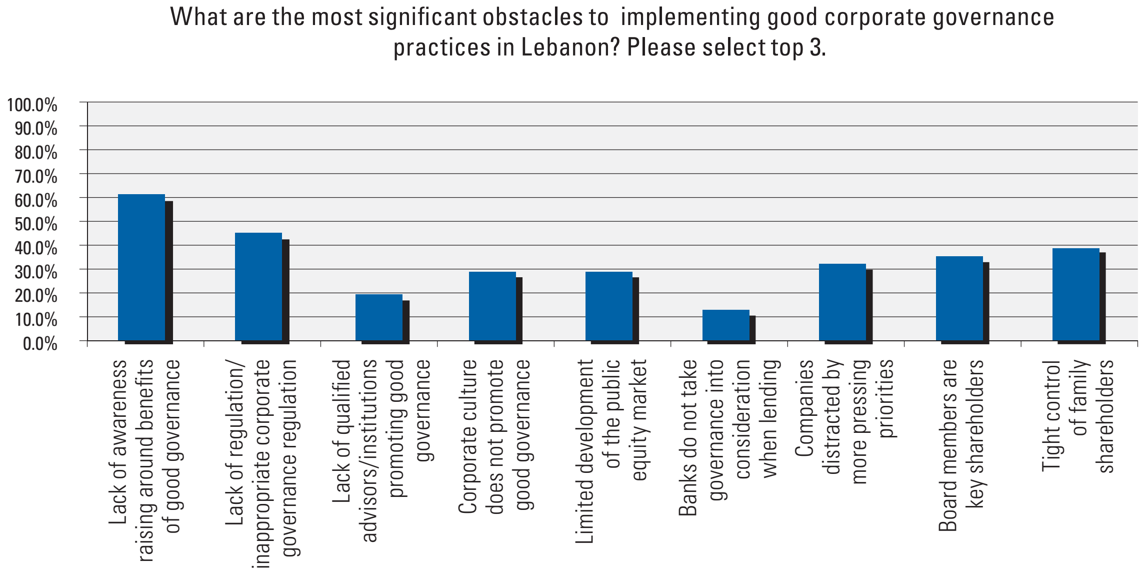
For over half of the companies surveyed, the new generation of owners was the factor which most prominently drove governance changes, followed by changes in laws and regulations and international regulatory trends, which have also had an impact on the Lebanese corporate governance framework, notably for listed companies and banks. On the other hand, the availability of governance education was cited as the least important factor (19%), whereas the transfer of knowledge from the Lebanese diaspora was not seen as being useful by any of the respondents.

Figure 3. Factors Positively Affecting Governance



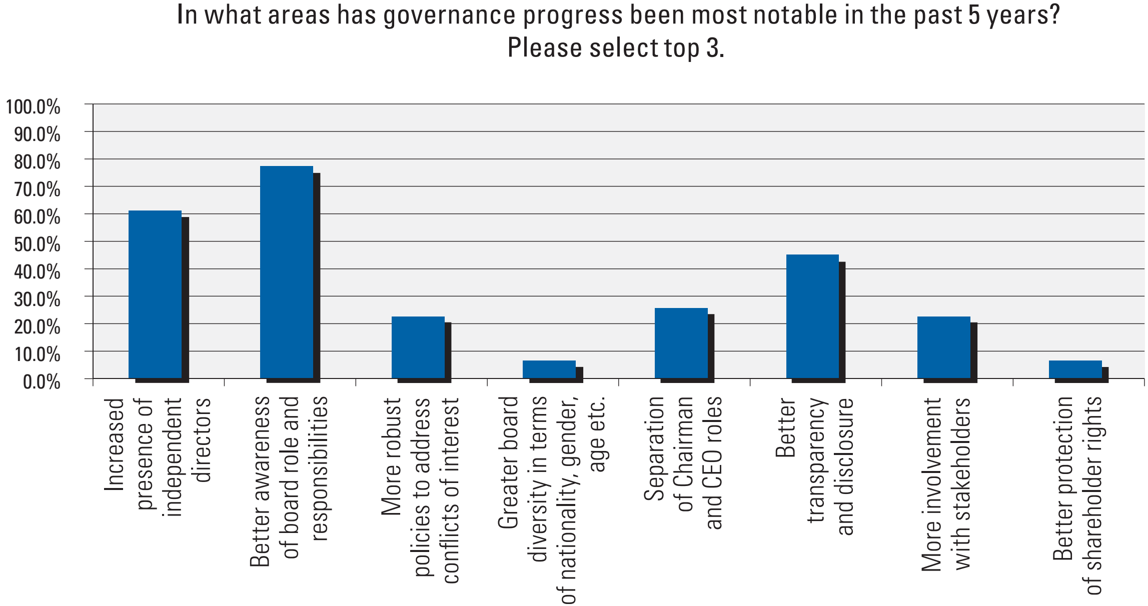
Interestingly, areas where respondents perceive most significant deficiencies are also the ones where they note most significant process has been realised. Lack of regulation on corporate governance appears to rank highly on the list of executives' and board members' concerns, with 45% of respondents considering that lack of or inappropriate regulations are a key factor to consider. Furthermore, 61% of respondents consider that lack of awareness around the benefits of corporate governance is the most significant obstacle. Other reasons cited include the limited development of the equity market and the corporate culture in the country.

Figure 4. Most Significant Governance Obstacles



Echoing previous responses, the development of a corporate governance code was ranked as a priority by 74% of respondents followed by the provision of training (65%) and and regional benchmarking (55%). On the other hand, board awareness of their responsibilities appears to have improved as has independent directors on boards which are of connected and mutually reinforcing. Last but not least, respondents referred to progress in better corporate transparency and disclosure but this was not necessarily corroborated by research conducted for this report.

Figure 5. Governance Progress Realised



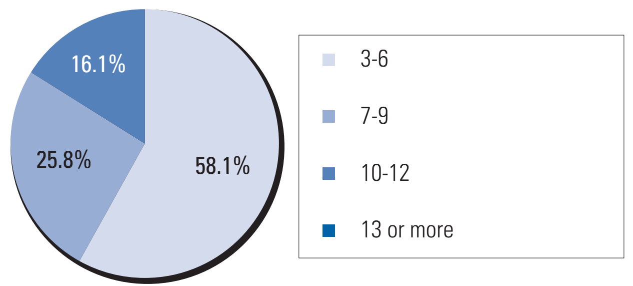
Board Structure and Composition

Board structure varies significantly, though the one tier board has become a common standard internationally and in the Arab world. In the OECD countries, the minimum size of the boars is set at 3-5, while a maximum requirement is less common (OECD, 2015). These limits are similar to global figures on board size and composition, whereby the average size of a board globally is 8.5 members (Spencer Stuart, 2016) while the European average is larger at 12.1 directors (Heidrick and Struggles, 2014).

Similar regulatory requirements are in place in Lebanon: according to the Code of Commerce, all joint stock companies in Lebanon need to establish a board comprised of 3-12 members, though the maximum is rarely attained in practice. In reality, 58% of respondents commented that the board consists of 3-6 individuals, while boards with 7-9 members account for a further 26% of the companies. This reflects the fact that many family companies have not yet established corporate boards, instead having family boards led by the patriarch.

Figure 6. Size of Boards

How many individuals sit on the company board?



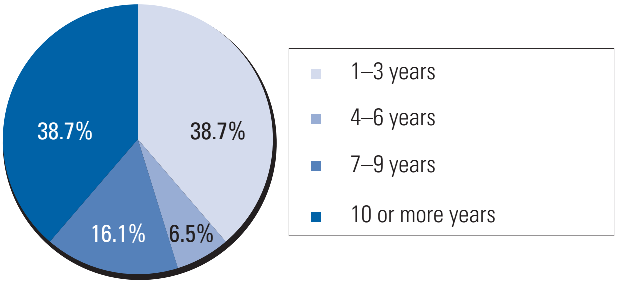
Lebanese boards tend to be older and do not experience much turnover. As demonstrated in Figure 7, most directors have more than a decade of tenure (39%) while another 39% have less than 3 years of experience. The latter illustrates the entry of second or third generation of owners in the formal governance organs of Lebanese companies which will likely change board dynamics going forward.

In developed markets, the maximum term of office of members varies from 1 to 6 yeas and is most commonly 3 years. Indeed, similar limitations have been set in the MENA region. Globally, a little more than one-third of boards have term limits for directors, averaging 6 years, while approximately one-quarter of boards have a mandatory retirement age, averaging 72 years. (Spencer Stuart, 2016). On the other hand, the European average of the number of years on board is 6 years (Heidrick and Struggles, 2014).

In Lebanon, by virtue of the Code of Commerce, board mandate is set at 3 years with no limits for renewal, except for the first mandate which is set at 5 years. Directorship is limited to 6 concurrent appointments and director age at 70, at which age directors may not hold more than 2 memberships. There are no limits for banks or listed companies. Very few organisations have introduced limits on successive mandates: for example, Al Mawarid bank limits term to 2 successive terms.

Figure 7. Director Tenure

The average tenure of a board member is:



A number of regulators in the region have moved to place limitations on tenure for independent directors and some have gone so far as to require boards to evaluate and confirm director independence annually. The limit typically adopted in the region is approximately 9 years. Globally, 43% of directors believe that a director loses his or her independence after 10 years (Spencer Stuart, 2016). A similar requirement may be useful in the Lebanese context to ensure independence of directors, at least in listed companies and banks.

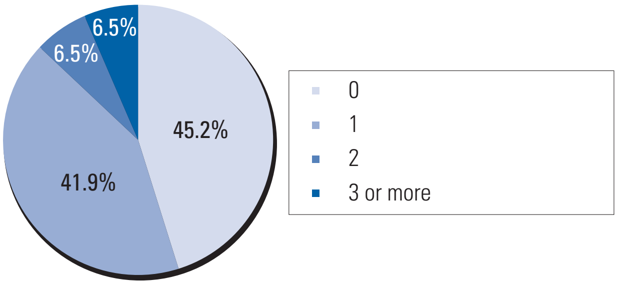
While constant director turnover may be a deterrent to board effectiveness, an automatic re-appointment of board members for multiple mandates may lead to reduced board independence in Lebanon. Indeed, 60% percent of respondents think that boards should have mandatory term limits for directors, and 45% think that there should be a mandatory retirement age.

As mentioned, Lebanese boards remain rather homogeneous in terms of age, gender and nationality. Most Lebanese companies do not have foreign board members, unless they have had outside, usually Gulf investors. As highlighted by the survey, female participation in boards tends to be low across all companies. 42% of survey respondents indicated to have 1 woman on the board, 13% 2 or more and 45% no women on their board.

Interviews corroborated that female presence on boards is rare and usually motivated by the desire of the company founder to include his daughters in the governance organ of the firm.

Figure 8. Female Participation on Boards

How many female board members sit on the board?



Globally, on average, 18% of board members are women and 13% of them have been appointed in the past 12 months. (Spencer Stuart, 2016) Female participation in boards has been increasing in recent years due to recommendations and quotas introduced, especially in European jurisdictions such as France, Italy and Germany. The proportion of women on European boards has increased by nearly 70% over the last four years (Heidrick and Struggles, 2014).

Progress has been slower on this front in the Middle East as no country has so far introduced formal requirements on female participations on boards. That said, the UAE's securities regulator has asked that companies nominate one female board members and disclose female participation on boards. There are, for the moment, no available statistics on the success of this measure.

While significant empirical research has confirmed the benefits of board diversity for company performance, it is debatable whether board diversity in Lebanon should be fostered through regulatory measures such as minimum quotas or other less intrusive mechanisms such as mentorship programmes (e.g. Reach or 30% Club). In this regard, it is instructive to examine the progress realised by countries where quotas were introduced as well as peer jurisdictions that have sought to increase female participation on boards through other mechanisms.

Lebanese boards may benefit from other measures aimed to improve their diversity. For instance, in a recent survey of European boards, 63% of survey respondents rated a diverse gender and nationality mix as being important for board effectiveness. The proportion of non-national directors on boards is now 30%, up from 23% in 2009 (Heidrick and Struggles, 2014). In particular, companies are increasingly eager to add board members with experience in Asia. The addition of directors with expertise in international markets that Lebanese companies attempt to penetrate may be of benefit, especially to larger companies.

Board independence and objectivity

Global corporate governance standards such as the OECD Principles of Corporate Governance stress the importance of board independence and objectivity for the exercise of good governance: "In order to exercise its duties of monitoring managerial performance, preventing conflicts of interest and balancing competing demands on the corporation, it is essential that the board is able to exercise objective judgement (OECD, 2015).

In most developed markets, the common standard is for the majority of the board to be comprised of independent directors. Reflecting this, 80% of European boards are comprised of majority of non-executive directors, ranging from a high 98% in Norway to 59% in Poland (Heidrick and

Struggles, 2014). Norway, Switzerland, Sweden and France have more than 90% non-executive representation, while Portugal and Poland have around 60%.

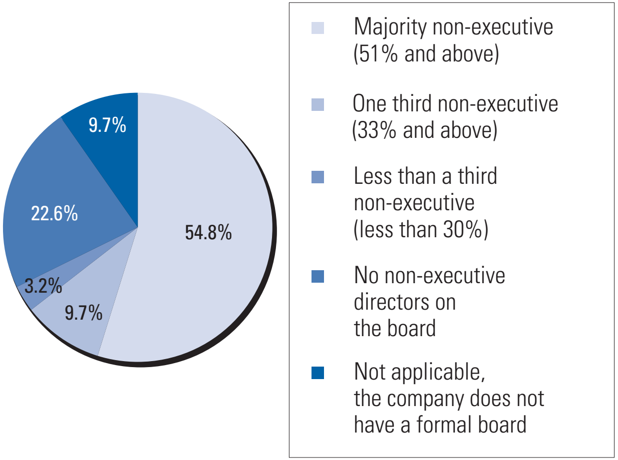
In the MENA region most regulators (i.e. UAE, Saudi Arabia, Egypt) now suggest that a third of the board be independent and that the majority of the board be non-executive. Oman requires all of board members to be non-executive. In Lebanon, banks are required to have at least 3 independent board members and listed companies at least a third of the board of 2 board members, whichever is greater.

This is largely in line with the requirements imposed by regulators in the region, however in practice, these requirements apply to a minority of firms in Lebanon (i.e. listed companies and banks). For instance, given that there are approximately 60 banks subject to BDL supervision, and that each requires 3 independent board members, a pool of 180 directors is required to fill all posts. Some have commented that the local director pool is insufficient whereas foreign directors are difficult to train since they are not familiar with the local economy and the legal framework.

On the other hand, only a few non-financial privately held companies (i.e. Debbas, Malia, Tamaris) have introduced independent directors or see the value in doing so. That said, 55% of the sample noted that the board is composed of majority non-executive directors, while 10% have a third of the board non-executive and 3% have less than a third comprised of non-executive directors. This demonstrates a large gap between “best in class” companies in terms of their governance and the rest of the sample.

Figure 9. Non-Executive Directors on Boards

What is the percentage of non-executive directors on the board?



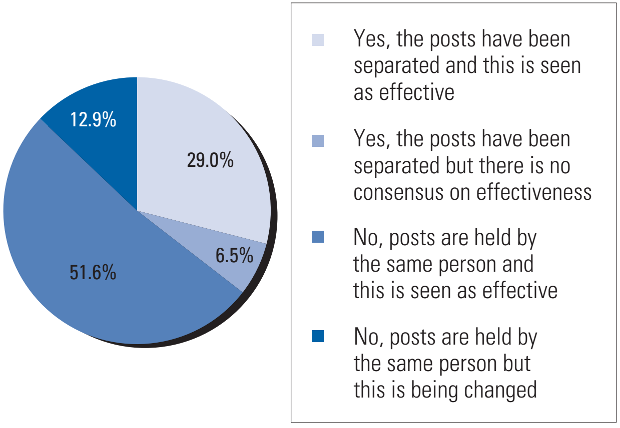
The presence of independent directors on boards was rather variable reflecting the industry and the ownership structure of companies. While 39% of the sample noted that they have no independent directors on the board, 29% noted that they have majority independent boards and a further 19% one-third of the board independent. Survey responses and interviews conducted highlight a number of factors linked to the low presence of non-executive and independent directors (other than in banks and listed companies), including the reluctance to reveal family secrets, the culture of a dominant Chair, and the fact that directors in Lebanese companies need to be shareholders.

The introduction of outside, non-executive directors in family groups is driven by the opening of capital to non-family shareholders, who in addition to board representation, occasionally require founding shareholders to add additional specialised expertise on the board. In family-controlled firms, these independent board members tend to have more of an advisory role to the family as opposed to challenging the decisions of the Chair.[1]

1 Even in regulated firms, some Chairs felt that independent board members do not challenge their views.

Figure 10. Independent Directors on Boards

Have the posts of the Chairman and the CEO been separated in practice and is the current arrangement seen as being effective?



A detailed definition of independence is key to ensuring truly independent boards. While the CMA's definition of independence contained in the Listing Rules is broadly in line with international definitions, the BDL does not specifically define independence requirements. A better definition of independence for the banking sector is needed to introduce truly independent directors on boards. The BDL may wish to define "fit and proper criteria" for bank directors and define specific negative criteria which would compromise director independence.

Indeed, interviews conducted for this report corroborated the fact that independent directors are often appointed purely for the form. The requirement that directors are shareholders is in fact detrimental from the perspective of board independence. It requires companies to either sell shares or enter into a "repo" type agreement whereby the founding shareholder sells and repurchases shares.[2] The practice of board members being required to hold shares in the company – while common across region, should eventually be abolished.

2 If directors would actually purchase shares, they would need to pay to sit on the board.

The appointment of directors representing minority shareholders can significantly enhance the corporate governance culture in Lebanon. Such directors, may be intrusted specific duties notably with regard to approving related party transactions. Policies concerning the appointment of minority directors can be inspired by the Italian rules.[3] Italian listed companies are required to have at least one director appointed from a list submitted by the minority shareholders.[4]

An alternative example has been adopted in the United Kingdom where the Financial Conduct Authority (FCA) published a rule in May 2014 that provides additional voting power to minority shareholders in the election of independent directors for a premium listed company where a controlling shareholder is present. It requires independent directors to be separately approved both by shareholders as a whole and by the independent shareholders as a separate class.

Some banks in Lebanon (i.e. BLOM) have already introduced the role of a lead independent director, elected by independent directors, who also hold discussions separately form the main board. Although the role of a lead independent director may be useful, the role of a director appointed specifically by the minority shareholders would be potentially more impactful considering the ownership structure of banks and non-financial corporates in Lebanon.

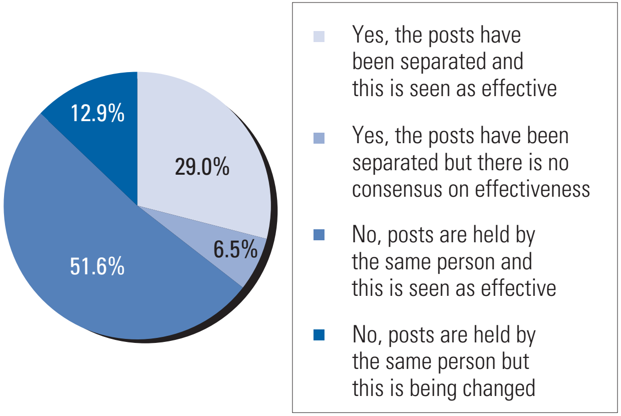
Another risk that the policymakers need to address is, as mentioned, the combination of CEO and Chairman posts in Lebanon. Over half of the companies responding to the survey noted that the posts are joined and that this is seen as an effective practice, while 13% commented that they intend to be changing this. Some companies have created multiple roles including Vice Chairman (in addition to Chairman) and Managing Director (in addition to the CEO).

3 Brazil, India, Portugal and Turkey have also established special arrangements to facilitate the engagement of minority shareholders in the process of board nomination and election.

4 In addition, stricter requirement for the board to be composed of a majority independent directors is imposed in cases involving integrated company groups with pyramid structures that may contribute to more concentrated control. This arrangement might also be beneficial considering that most long term shareholders in Lebanon get dual voting rights.

Figure 11. Chair and CEO Separation

Have the posts of the Chairman and the CEO been separated in practice and is the current arrangement seen as being effective?



The OECD recommends that the separation of the two posts is generally regarded as good practice, as it can help to achieve an appropriate balance of power, increase accountability and improve the board's capacity for decision making independent of management (OECD, 2015). While the separation of Chair and CEO is generally considered as a well-accepted corporate governance practice, in practice only a third of OECD countries require or encourage the separation of the two posts (OECD, 2015).

Practices globally are moving in this direction, with only 1 in 5 boards in the EU having the two roles combined (Heidrick and Struggles, 2014). The only European countries where CEO and Chairman roles still tend to be combined in the majority of firms include the Netherlands, Austria, France, whereas in other countries such as the UK this practice is forbidden.

This is an area where most securities regulators and central banks in the region have taken a more stringent approach requiring the separation of the two posts as their combination has a risk of creating a dominant Chair whose judgement is not effectively challenged by the board. Indeed, in a recent assessment of GCC corporates, S&P has recently noted that the combination of Chair and CEO positions as a key risk (S & P, 2017).

Board Committees

With growing responsibilities placed on boards globally, recent years have seen the proliferation of board committees to address specific responsibilities and risks that boards need to grapple with. The vast majority of OECD countries require the establishment of an independent Audit Committee, while the establishment of other committees are generally left up to the individual companies (OECD, 2015).

The European average in terms of the number of Audit Committees is 3.4, ranging from an average of 4.4 committees in the UK to 2.1 in Poland (Heidrick and Sruggles,2014). Audit, Remuneration and Nomination remain the primary committees but, increasingly, boards are adding Strategy, Governance and Risk committees. In the region, banks and listed companies are also required to establish Audit Committees, while in many countries Remuneration and Nomination committees are also required, in some instances to be led by independent directors.

In Lebanon, the CMA requires that every issuer must have a majority independent Finance and Audit Committees as well as a Nomination and Governance committee the Chair of which should be non-executive. The BDL requirements impose the establishment of Audit, Risk, Remuneration and Compliance committees.[5] 3 of these committees must be headed by an independent chair who cannot lead another committee. Private companies are not required by law to establish any board committees.[6]

While some banks have introduced other committees of the board, in addition to multiple management committees, few private companies have effective board level committees. The survey highlighted that so far 65% of Lebanese private sector companies have established an Audit committee, 52% a Risk committee, 42% a Remuneration committee and 29% a Nomination and Corporate Governance committees, respectively.

Some banks have joined functions of certain committees: for instance, Banque Libano-Francaise has introduced a

5 The exact composition of each of the committee for listed companies and for banks is contained in Annex IV which benchmarks Lebanon to other jurisdictions.

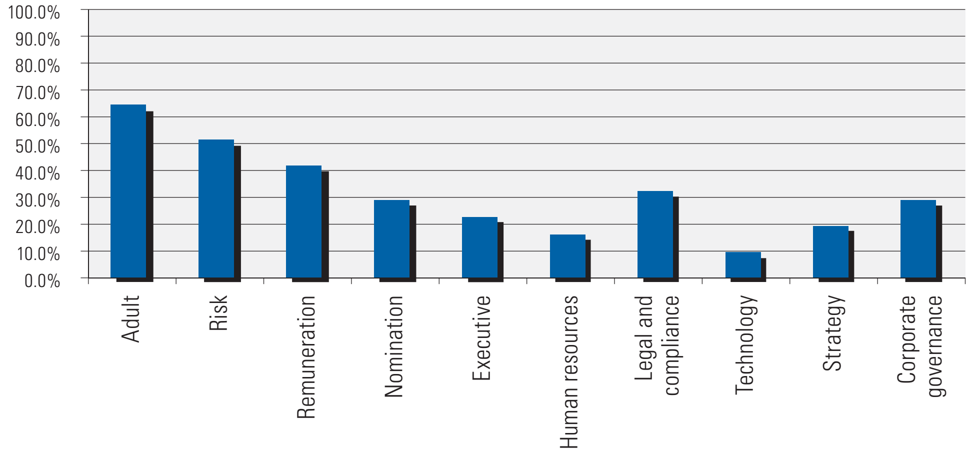
6 By virtue of the recently revised Saudi Companies Law, private companies now also need to have an audit committee.

Remuneration and Corporate Governance Committee. In addition to the combination of functions, some banks still have quite unorthodox practices in terms of the composition of these committees. The fact that Chair and CEO roles are joined is particularly problematic in the context of Nomination Committee for instance.

The Risk Committee is prevalent in banks where it is required by the BDL. Indeed, the introduction of a committee responsible for risk management is also growing increasingly common globally, especially in financial sector institutions. In OECD countries, the board's responsibility for risk management is explicitly stipulated in the majority of jurisdictions (by regulations in 26% of the countries, by corporate governance code in 36%). (OECD, 2015).

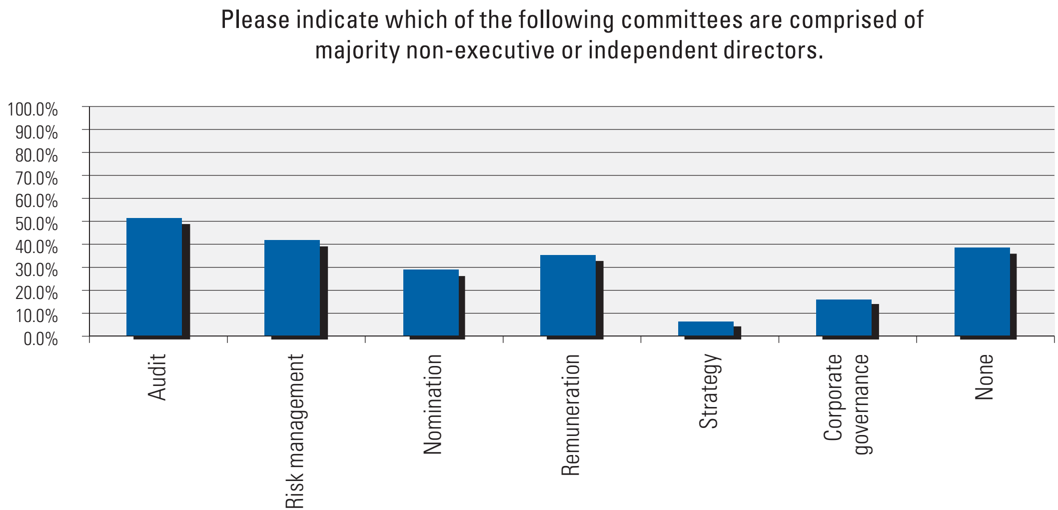
Figure 12. Board Committees

What board committees have been established?



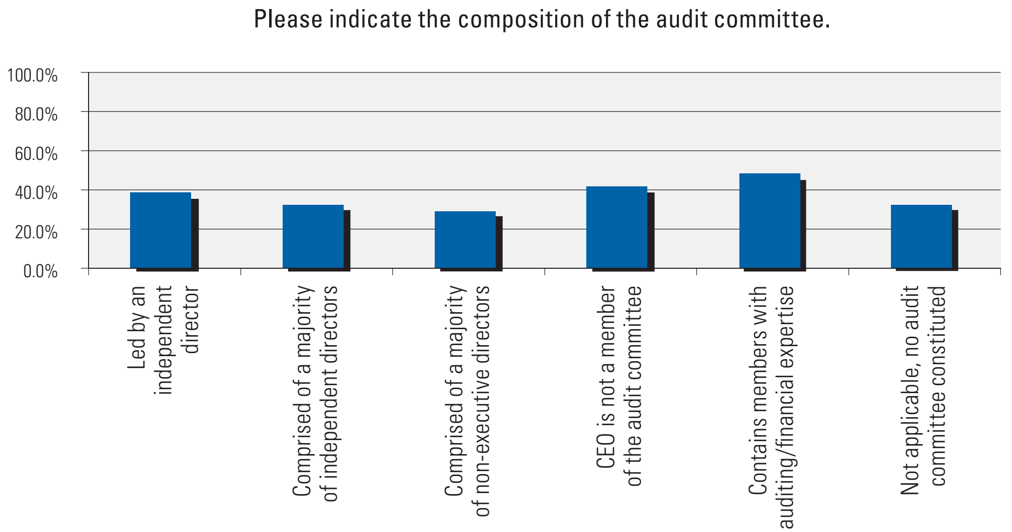
In addition to addressing board independence, the survey inquired about the independence of board committees and the composition of the Audit committee specifically. Full or majority independent membership is required or recommended for all three committees in most OECD countries and provisions regarding Audit Committee Chair independence are also common. Half of the respondents indicated that the majority of the Audit committee is comprised of non-executive or independent directors, and a high proportion of Risk and Remuneration committees are likewise majority non-executive or independent.

Figure 13. Committee Independence



While these results highlight progress in the independence of board committees, further questions regarding the composition of individual committees highlights progress that can be realised. Importantly, the composition of the Audit Committee shows opportunities for improvement as in most companies it is not sufficiently independent. 32% of companies have an Audit committee comprised of majority independent directors and only 48% believe it contains a sufficient number of audit and financial experts. Audit Committees have not been established in a third of the companies surveyed.

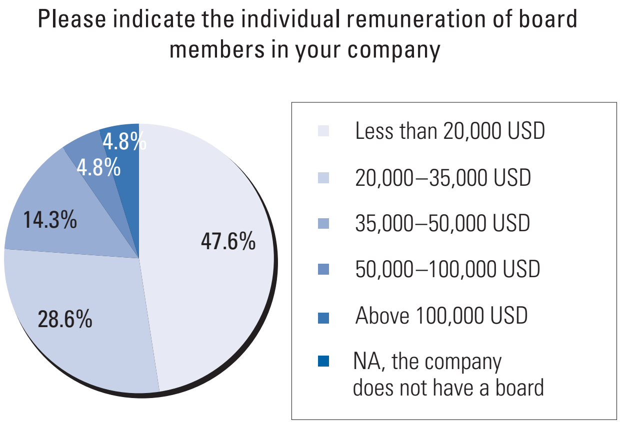
Figure 14. Audit Committee Independence



The establishment of Remuneration Committees is also an important policy issue as governance of the remuneration process has been a major area of focus following the financial crisis, with many countries moving to require the introduction/reinforcement in the operation of Nomination/Remuneration Committees and periodic shareholder approvals (voluntary or binding) of board and executive remuneration. In OECD countries, 39% of countries require companies to establish criteria for board and executive remuneration while a further 44% recommend it (OECD, 2015).

Furthermore, a majority of the developed countries and some advanced MENA jurisdictions have required the disclosure of remuneration policy and actual remuneration of board members and top executives. In order to improve the transparency of largest Lebanese corporates, notably banks and listed companies, the authorities may introduce similar arrangements to align with best practice jurisdictions. In leading jurisdictions, a breakdown of remuneration for the board and the executives should be provided.

Figure 15. Board Remuneration

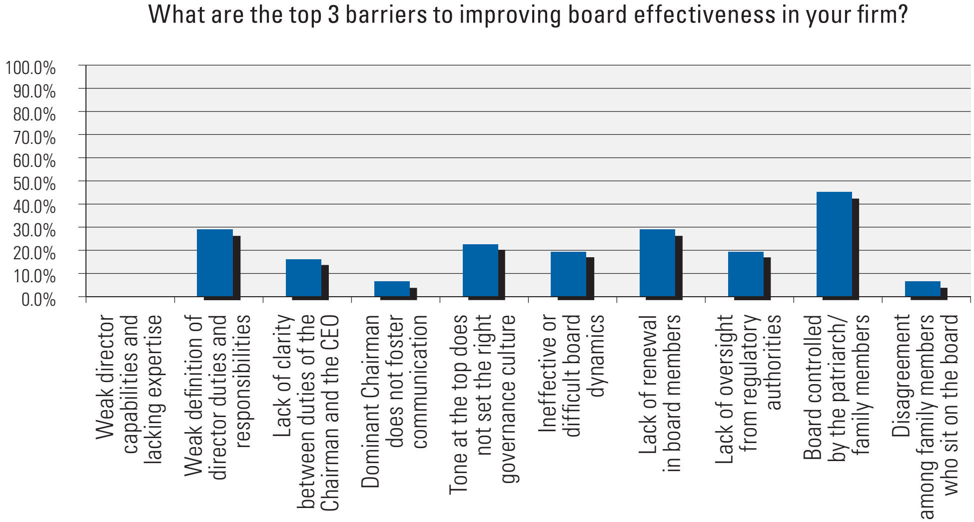


Based on the sample of responses collected, remuneration of individual board members for almost half of the firms (48%) is generally less than 20,000 USD and between 20-35,000 for a further 29% of the companies. It is understandably higher for larger companies and financial sector institutions. Indeed approximately 5% of respondents corresponding to banks noted that board remuneration exceeds 100,000 USD. Some banks confirmed that given the deficit of qualified directors, remuneration can exceed 200,000 USD.

Board Effectiveness

Board effectiveness is a combination of factors that are challenging to define, although global and national regulators have sought to do so, recognising the central role of the board in corporate governance. Survey respondents have indicated that the top barrier to improving board effectiveness in Lebanon is the presence of a patriarch or family members who control the board (45%) which resulted in lack of renewal of board members (29%) and a weak definition of director duties and responsibilities (29%).

Figure 16. Top Barriers to Board Effectiveness



The CMA and the BDL regulations do not set detailed standards for qualifications of board members or address issues such as board education or evaluations. Globally, the majority of OECD countries establish requirements or recommendations for board member qualifications[7] and these tend to be especially stringent for financial sector institutions where Central Banks normally establish a set of "fit and proper" requirements.[8] (OECD, 2015) In Lebanon, the "fit and proper" standards for bank boards are rather general and could be reinforced.

Board effectiveness is also function of the structure of the board, but also of the time board members dedicate to the exercise of their duties and responsibilities. Globally, directors report to be dedicating an increasing amount of time to the exercise of their duties. For instance, a recent Mckinsey survey found that directors reporting that they had a very high impact worked about 40 days a year, while those who said that their impact was moderate or lower averaged only 19. (McKinsey, 2014)

A survey of board members of European boards revealed that the average number of hours dedicated to board service was 215 in 2013, up from 155 a decade earlier (Heidrick and Struggles, 2014). These figures are indicative of the time commitment that high performance boards require to not only oversee compliance but also to spend more time on strategy and performance management (McKinsey, 2014).

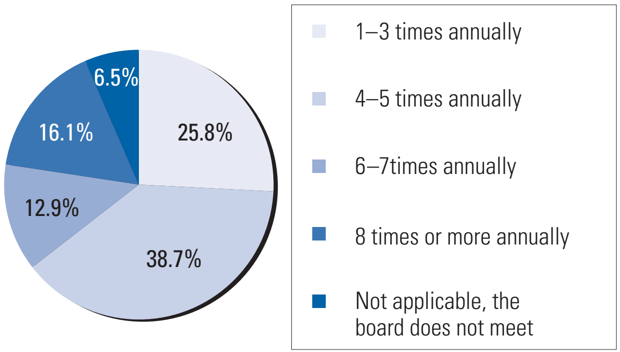
To determine the time directors spend, survey respondents were asked about the frequency of the board and committee meetings as these are addressed by the Lebanese regulatory requirements. The BDL and CMA requirements are identical, requiring at least 4 board meetings to be held annually, at least 2 of which in Lebanon. For 38% of firms, the frequency of board meetings was indeed on a quarterly basis (4-5 times a year), while 29% of respondents – corresponding to the non-regulated firms – noted board meetings occurred 1-3 times annually. Interviews indicate however that the quality of board discussions varies widely.

7 2/5 of OECD countries require information regarding the qualification of the candidates and the relationship between the candidates and the company to be provided to shareholders (OECD, 2015).

8 "Supervisors should evaluate the processes and criteria used by banks in the selection of board members and senior management and, as they judge necessary, obtain information about the expertise and character of board members and senior management" (Basel Committee, 2016).

Figure 17. Frequency of Board meetings

What is the frequency of board meetings?

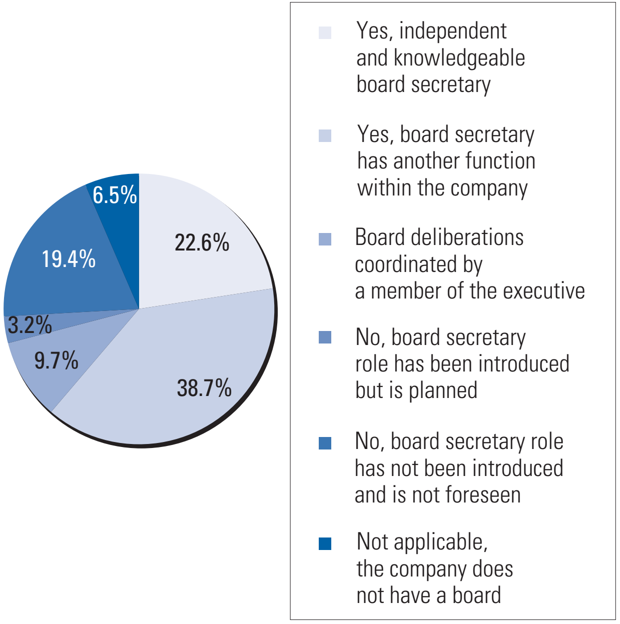


22% of respondents noted that the board has a dedicated board secretary and a further 39% noted that the corporate secretary has an additional executive role. This is not surprising considering that neither the CMA nor the BDL require the introduction of a corporate secretary, while the Code of Commerce requirements in this regard are rather general. Only banks and a few large Lebanese groups have introduced a dedicated corporate secretary whereas most in other firms the role of the corporate secretary is frequently entangled with other board and senior executive responsibilities.

The role of the corporate secretary is being recognised in a few leading companies. Indeed, in the case of Malia Group the corporate secretary was instrumental in establishing the corporate governance framework of the group, including structuring a formal board of directors. In some cases, one of the board members has taken the role of the corporate secretary (i.e. Debbas). Some organisations such as BLOM has moved from having a corporate secretary who was previously the head of the legal department to have a dedicated corporate secretary role.

Figure 18. Company Secretary Appointment

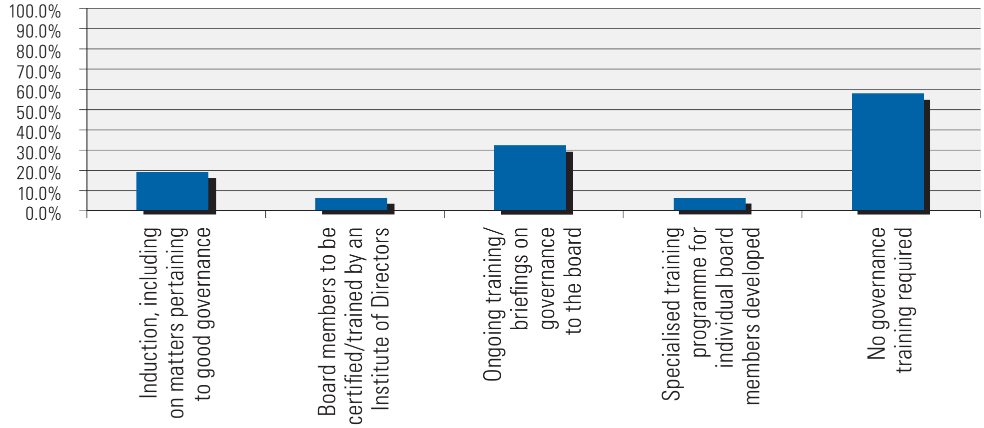
Does the board have a dedicated Company Secretary?



Since corporate secretaries are said to facilitate board effectiveness, the importance of the role of a board secretary is also tackled in international standards. In addition to coordinating board interactions, board secretaries play an important role in organising board evaluations and coordinating the education of board members. The type of governance training provided to board members in Lebanon varies considerably as can be seen from Figure 19 below. While most respondents believe that they do not require governance training, over 30% of companies confirm that they provide some ongoing training and 20% induction for new board members.

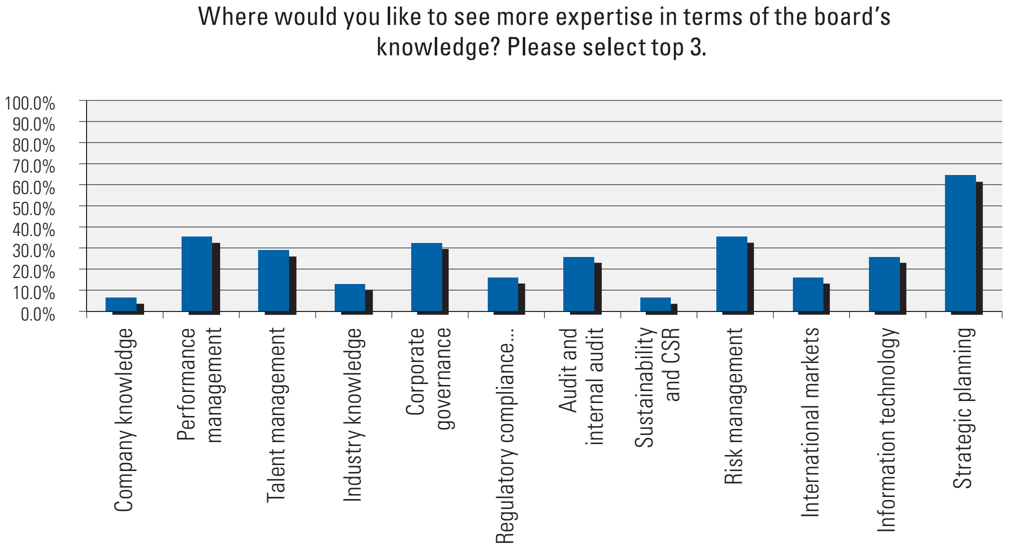
Figure 19. Board Member Education

What governance training is proposed to board members in your company? Select all that apply.



Lebanese boards believe they need to particularly enhance their knowledge in strategic planning (65%), risk management (36%) performance management (35%), audit and internal audit (25%). Corporate governance was selected as an important area for improvement by 32% of respondents. This corresponds to other results of the survey, notably the need for the board to spend more time on strategy as opposed to operational oversight.

Figure 20. Enhancing Board Knowledge



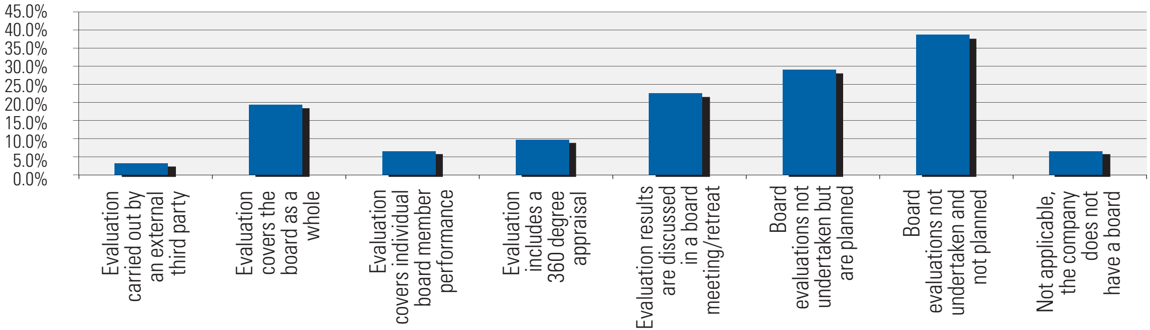
Regulators have imposed requirements or introduced recommendations requiring them to conduct periodic performance assessments and in some instances, to disclose the result of such assessments. In Europe, 70% of boards on average undertake a formal review annually and only 16% have never undertaken a board evaluation (Heidrick and Struggles, 2014). Although this is a relatively recent practice in the MENA region, the concept of board evaluations is being accepted among leading corporates in the region.

In Lebanon, board evaluation is recommended by the CMA for listed companies, whereas the BDL has not yet recommended it. 39% of respondents confirm that board evaluation has not been undertaken and is not planned while 29% would like to implement it. Only the largest banks in the country have gone through a board evaluation, usually led by the Chair/CEO. Although this process may be effective in evaluating the effectiveness of the board, it does not allow to gauge the effectiveness of the CEO since the two posts are joined.[9]

9 To address this issue, in Bank Audi, the board evaluation process is led by the independent Vice Chair of the Board who reports back to the board.

Figure 21. Board Evaluations

What is the process of assessing board effectiveness? Please select all that apply.



Lebanese firms that undertaken board evaluations usually focus on the performance of the board as a whole as opposed to individual members and rarely resort to external facilitators. Indeed, individual evaluations tend to be more sensitive even in developed markets: in the United States for instance, less than half of boards evaluate individual directors (NACD, 2011). While mandating specific means or scope of board evaluations may be unnecessary, the BDL may wish to consider introducing requirements to require banks to conduct these and to report results to the BCC.

Board evaluations would also support an overview of the remuneration of the board. In Lebanon, the remuneration of directors consists either of an annual remuneration, attendance fees or is set as a percentage of the net profit, or a combination of such benefits (article 145 of the LCC). Also, by virtue of the Code of Commerce, board members in Lebanon are personally liable in front of the shareholders for any wrongdoing. Although this provision has been rarely evoked as it requires the proof of wilful malicious conduct by board members, it is frequently evoked as a justification for higher remuneration of board members.

Risk Management and Oversight

Another important board responsibility is to oversee risk management and compliance functions. Globally, board responsibility for risk oversight is of growing importance with boards not merely considering top risks but looking to address a range of strategic and operational risks, define risk appetite and monitor a number of emerging threats such as cybersecurity. Yet, surveys of directors demonstrate that boards continue to grapple with notions of effective risk oversight and lack confidence that key risks are addressed.

There is scope for improving how risk management practices are addressed in the Lebanese laws and regulations, including in the banking sector. Currently, the BDL requires banks to establish a Risk Committee comprised of at least 3 board members to be led by an independent Chair. Banks are also required to have a Chief Risk Officer (CRO) reporting to the board (Circular 242).[10] In some best practice cases, the CRO reports not to the board as a whole but specifically to the Risk Committee which is led by an independent board member.

Risk management practices are less explicitly addressed in the CMA requirements than those of the BDL. At the same time, the current political and macro-economic climate in the region would call for enhanced risk management practices, and survey responses highlight the various practices adopted by Lebanese companies to deal with risk. The most common practices put in place to address risk focus on internal audit and controls as well as auditor rotation, which is not currently addressed in the regulations.[11]

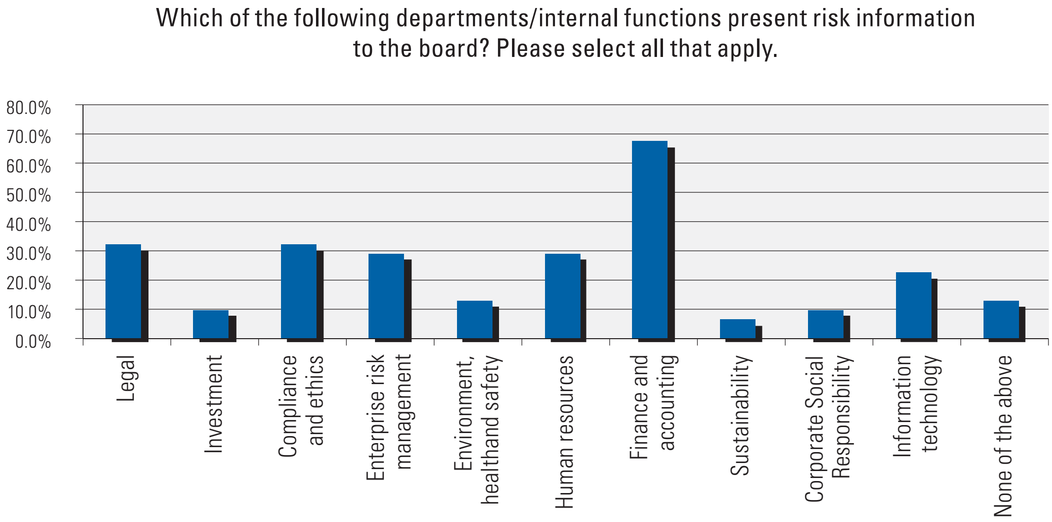
10 Specifically, bank boards are responsible for « appointing an independent Risk Manager who reports directly to the board and Senior Management (the Risk Manager can have other responsibilities such as credit risk manager, on condition that he does not have any executive responsibilities). The BCC should be informed of this appointment and any changes that might occur" (BDL, 2004).

11 Some banks such as Audi have adopted the rotation of audit partners without necessarily rotating the auditors which is a step towards the adoption of international practices.

Figure 22. Risk Management Practices

Although the risk management function does report to the board in some large firms, survey results highlight that the department with most reporting lines to the board is finance and accounting (68%), whereas other departments such as legal and compliance have a reporting relationship to the board in less than a third of firms. Sustainability related functions have the least exposure to the board, likely because they do not exist in most firms.

Figure 23. Board Role of Management of Risks



In board discussions, succession planning is, unsurprisingly, getting most significant attention with 42% of respondents ranking it as being a top priority, followed by separating board from family governance (32%) and introducing/reinforcing board committees (35%). 39% of boards are communicating with management on succession planning, though only 13% of boards have adopted a formal CEO succession plan. CEO evaluation in most companies (58%) is the responsibility of the full board, whereas the Nominating/Governance Committees curiously appear to have no role in the CEO evaluation.

Figure 24. Governance Priorities

What are the top governance priorities for your firm? Please select top 3.

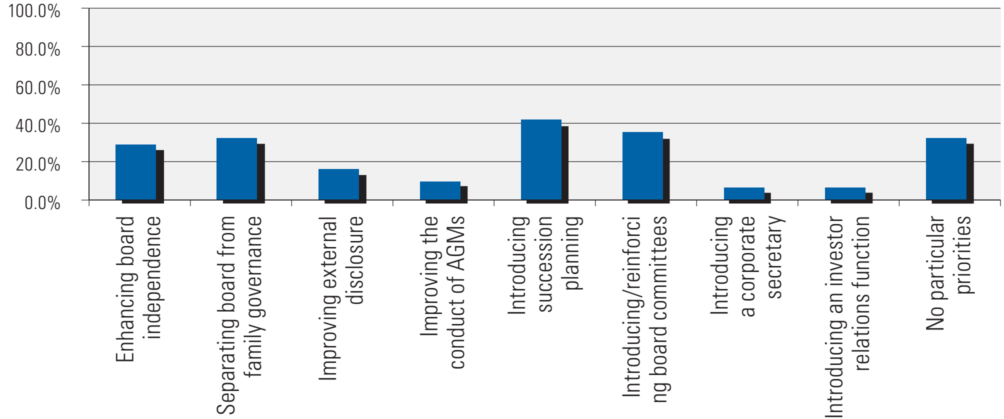
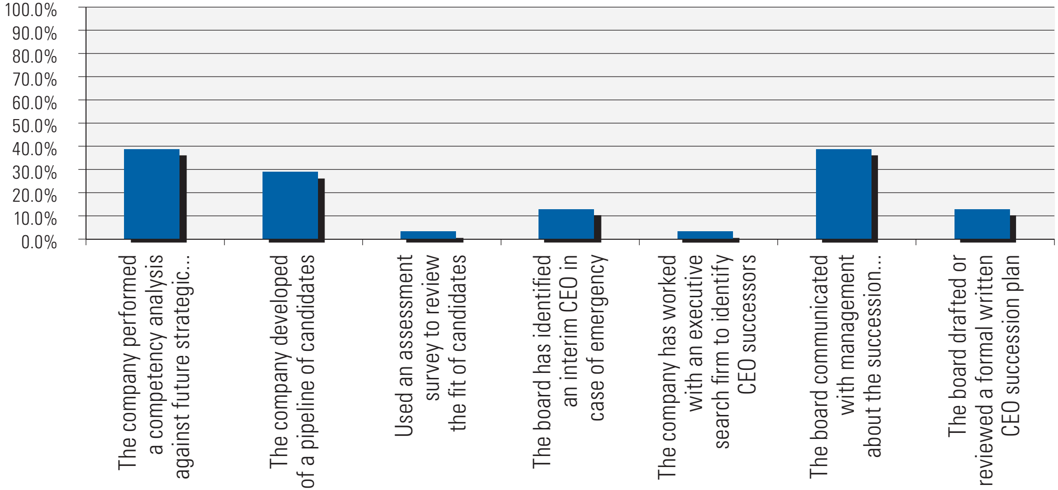


Figure 25. Succession planning

Do you feel that succession planning has been adequately addressed by your firm? Please select all that apply.



Shareholder rights

The OECD Principles for Corporate Governance recommend that shareholders have the right to secure methods of ownership registration, convey or transfer shares, obtain relevant and material information on the corporation on a timely and regular basis, participate and vote in general shareholder meetings, elect and remove members of the board and share in the profits of the corporation. Furthermore, shareholders should be sufficiently informed about and have the right to approve or participate in decisions concerning fundamental corporate changes (OECD, 2016).

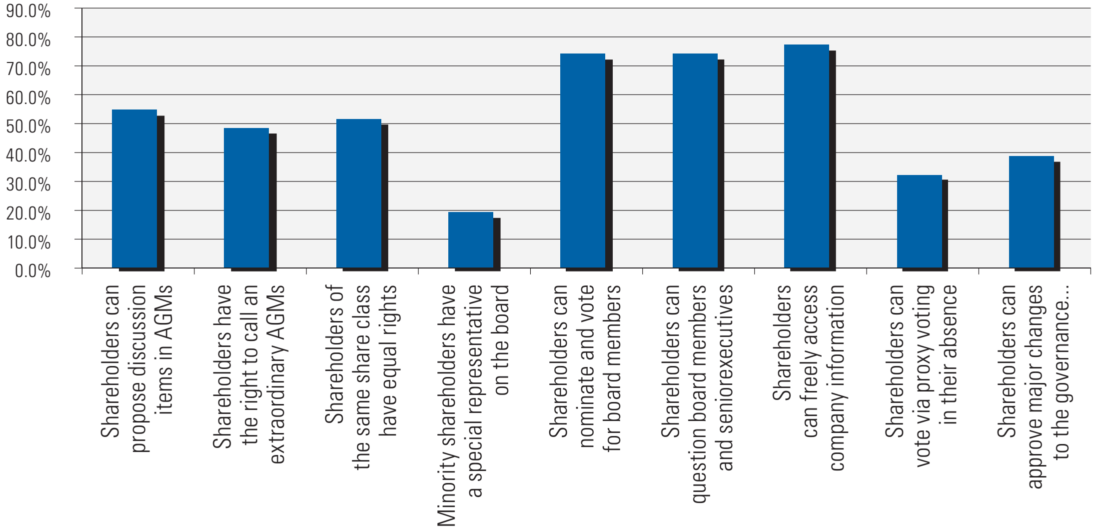
In principle, while all of these rights are broadly addressed by the Code de Commerce, this Law is rather dated and does not address shareholder rights comprehensively. For instance, cumulative voting and other mechanisms that facilitate the exercise of shareholder rights are not addressed by the existing legislation. In developed jurisdictions, it is common for the regulators to set specific deadlines for notification of AGMs and specific ownership thresholds for convening ordinary and extraordinary shareholder meetings.[12]

Survey responses highlight that the most often cited mechanism for shareholder protections include: the ability of shareholders to propose discussion items at AGMs (54%), question board members and senior management (74%) and access company information (77%). In order to the shareholders to propose discussion items, participate in AGMs and exercise their rights effectively, meeting notifications to shareholders should be clear and the percentage of shareholding to convene an AGM or an EGM should also be set. The percentage of shareholding needed to convene an ordinary or an extraordinary assembly is not specified in the Code of Commerce though the quorum for adopting decisions is addressed.

12 In the MENA region, these thresholds are commonly set at 5-10% of total outstanding shares. In OECD member countries, it is most commonly set at 5% and regulators have further specified deadlines by which the requested meeting must be held.

Figure 26. Shareholder Rights

The rights of the shareholders are protected through the following mechanisms.
Please select all that apply.



For shareholders to exercise their rights appropriately, they need to receive adequate disclosure. In most countries a large amount of information, both mandatory and voluntary, is compiled on publicly traded and large unlisted enterprises and subsequently disseminated to a broad range of users. Public disclosure is typically required, at a minimum, on an annual basis though most regulators require periodic disclosure on a semi-annual or quarterly basis for listed companies. Listed companies often make voluntary disclosure that goes beyond minimum disclosure requirements in response to market demand.

In Lebanon, disclosure requirements are addressed primarily through the Listing Requirements for public companies and through the BDL circulars for banks. The CMA requirements are most detailed addressing both annual and interim disclosure, including disclosure of specific material changes. Banks provide detailed reporting to the BCC based on a series of established templates. Banks and listed companies are required to adopt a corporate governance code and to report on key aspects of their governance, such as board structure and composition.

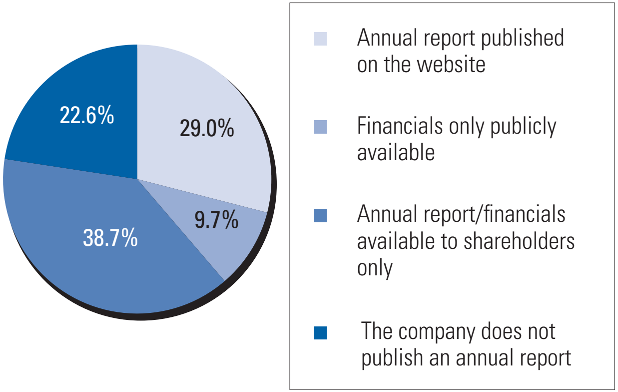
On the other hand, the requirements for unlisted joint stock companies remain quite rudimentary, requiring the balance sheets of companies to be published in the official gazette, along board composition and company auditors[13] (Article 101 of CC). Privately-held Lebanese companies – including large conglomerates - do not provide any public disclosure publicly and consider it as a source of risk. This is not merely a result of informality of the economy or practices relating to keeping "two sets" of books, but a concern that transparency may be damaging to company interests.

Indeed, 39% of surveyed companies make their annual report available only to shareholders, and only 29% publish them on their website. 23% of firms do not publish an annual report at all. As can be seen from the Figure 25, the most commonly reported item was board composition, while items such as risk factors and executive remuneration are generally not disclosed. Regulators might wish to consider measures to stimulate better disclosure by privately-held firms and shareholder access to disclosed documents.

13 All Lebanese SARL are required to have two external auditors.

Figure 27. Annual Report Publication

Does the company publish an annual report?



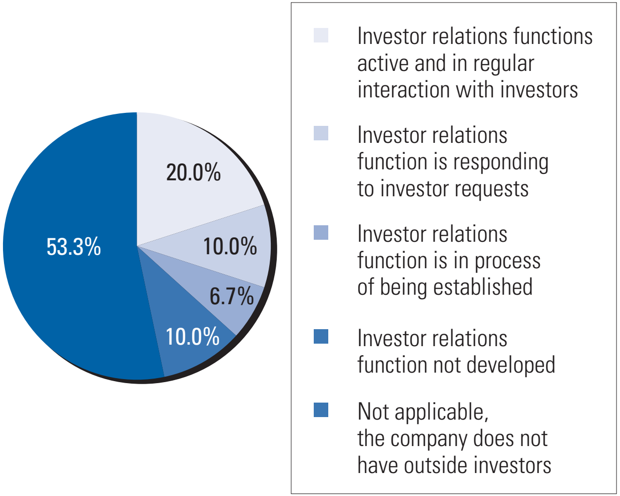
For a few large listed firms, the introduction of an investor relations (IR) function has marked a significant progress in the information provided to the shareholders and in the quality of dialogue between boards/executives and shareholders. Currently, the introduction of an investor relations function is not required either for banks or for listed companies. As a result, most Lebanese corporates, except those also traded in London, have no investor relations function. [14]

While 53% of respondents indicated that their company does not require investor relations since the company does not have outside investors, only 20% of firms noted that the investor relations function is active and is regular interaction with investors, and 7% commented that the function is in the process of being established. Some banks such as BLOM have an active investor relations function and the CEO seeks to meet with foreign investors to brief them on company developments.

14. The Middle East Investor Relations Association (MEIRA) has this year signed an MOU with the BSE to facilitate the establishment of investor investor units in listed companies.

Figure 28. Investor Relations Function

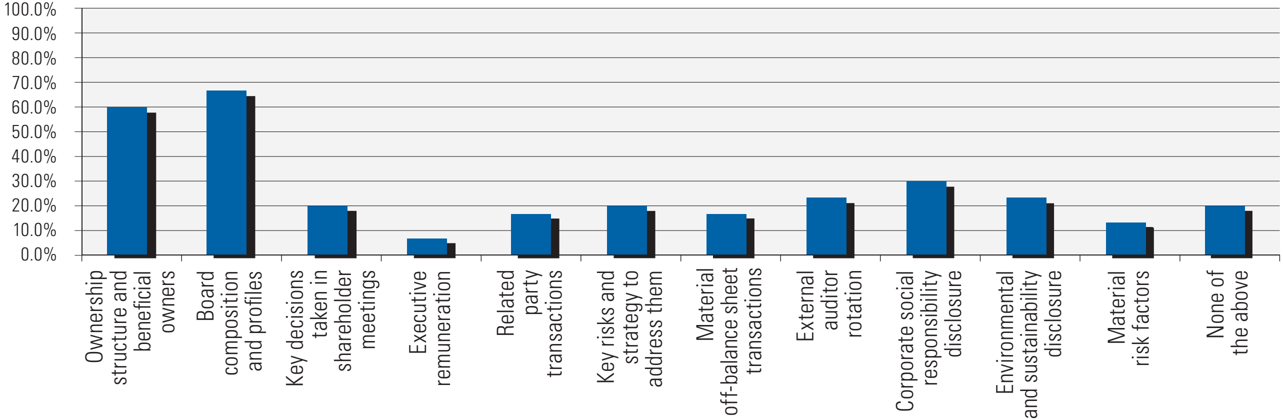
How well is the investor relations function developed?



Although in companies with an IR function, the quality of disclosure is considerably higher, it bears to note that the quality of corporate governance reports, even in the few companies which produce them leaves room for improvement. The concept of a corporate governance report is somewhat misunderstood: in a number of banks, including leading ones, it only includes details of board composition. Corporate governance reports rarely address the role and interactions of the board and executive with risk and strategy issues. In addition, specific information on compensation of directors, board evaluations results and measures to improve board efficiency is not disclosed. In fact, Lebanese banks provide more comprehensive reporting on their corporate social responsibility/philanthropic activities than on their governance.

Figure 29. Publicly Available Disclosure

Are disclosures regarding the following items made publicly available? Select all that apply.



Disclosure of specific items such as related party transactions (RPTs) merits further attention. Considering the concentrated ownership structure in Lebanon, disclosure on related party transactions should be provided to shareholders. While the approval of related party transactions is addressed in the Code of Commerce, and the Code of Money and Credit[1], they are not adequately disclosed and hence whether the approval mechanisms are implemented in unclear. It is a good practice that extraordinary RPTs are approved by the Audit Committee or an equivalent mechanism.[2]

The Code of Commerce (Article 158) and the Code of Money and Credit (Article 152) expressly forbid banks to provide credit to board members and require all RPTs between the company and its director to be pre-approved by the AGM. However, interviews with bank boards and executives highlight the importance of having regulations to address conflicts of interests of bank board members and executives. For instance, bank board members and executives have access to privileged client information and may benefit from it for personal gain.

1 Refer to Annex II for the specific provisions governing the approval of related party transactions in Lebanon.

2 For further information refer to the OECD Guide on Related Party Transactions in the MENA region, 2014.

CONCLUSIONS

The evolution of corporate governance regulations and standards in Lebanon has been gradual and piecemeal due to the limitations in the legal system, notably the Code of Commerce. The slow development of the equity markets has also stymied the development of a governance culture in regulated firms. In the banking sector, the regulatory approach adopted by the Central Bank has resulted in a gradual adoption of governance practices which are broadly similar with peers in the region.

The development of the equity market in Lebanon presents an opportunity to future improvements in corporate governance. The corporate governance framework introduced by the CMA can be further defined when the market develops as previewed by the Capital Markets Law. For instance, if companies in which banks have invested by virtue of Circular 331 are exited on the stock market, the exchange could see a pipeline of new issuers, in which case it may be relevant to differentiate governance standards between small and large issuers.

While a small number of banks in Lebanon are listed, banks are regulated primarily by the BDL though the periodic circulars which request that banks introduce additional governance functions. While this approach has had the impact of improving corporate governance in the banking sector, the sector may benefit from a consolidated code of governance, with some mandatory and some principle-based recommendations which could accommodate banking organisations of different size and complexity.

The vast majority or privately held companies continue to be controlled by families and have not advanced on the adoption of good governance standards. The eventual revision of the corporate law (Code de Commerce) can facilitate the adoption of basic governance requirements, at least for corporate entities of a certain size and indeed this route has been undertaken by other regulators in the region. A number of recommendations have been provided in this regard.

Other education-oriented initiatives aimed at helping private firms address succession planning challenges, separate family from corporate boards and facilitate the entry of new investors would benefit the sustainability of Lebanese companies. As highlighted by this report, succession planning will likely remain a key parameter driving the appetite of companies to introduce formal governance arrangements. Other company-specific factors such as the entry of new investors into capital or company diversification has also been highlighted as important forces.

The results of the survey and the benchmarking efforts undertaken for this report highlight a number of opportunities to upgrade the regulatory framework for privately held firms as well as for banks and listed companies. Over half of the respondents of the survey highlighted that the regulatory framework is currently insufficient, with less than 15% of respondents indicating that the regulatory requirements are appropriate to the economic context of Lebanon.

Notably, the establishment of a corporate governance code/guidelines was ranked as a top priority by survey respondents. In the recommendations section of this report, a number of areas where additional requirements may be imposed or where current regulatory framework can be revised are highlighted, recognising that some of these changes require revision of laws that necessitate Parliamentary approval. It is hoped that the adoption of these recommendations will pave the way to improving the sustainability and transparency of Lebanese companies.

ANNEX I. KEY GOVERNANCE PROVISIONS OF THE LEBANESE CODE OF COMMERCE

The management of the joint-stock company shall be entrusted to a Board of Directors consisting of three members, at least, and of twelve members, at most. Without prejudice to what could be provided by special legislation for certain joint-stock companies, the majority at least of the members of the Board of Directors must be of Lebanese nationality. The Board of Directors must appoint one of its members for the chairmanship (Article 144)

* * *

Their remuneration consists either of an annual stipend, or in tallies for attendance, or a percentage of the net profit, or a combination of these various advantages. The profit on which the Directors' percentage is based must comprise, in principle, only the net product of the exploitation which is the object of the company. Thus portfolio proceeds may not be included but exceptionally and by virtue of a special resolution of the general meeting renewed every year (Article 145)

* * *

The general meeting elects the members of the Board of Directors from among those shareholders who hold a minimum number of shares as fixed in the Articles (Article 147)

* * *

The Chairman of the Board of Directors shall discharge the duties of General Manager. The Chairman shall be at liberty to propose that the Board appoints a General Manager other than himself. However, such Manager shall discharge his duties on behalf of the Chairman and under his personal responsibility. (Article 153)

* * *

The Chairman of the Board of Directors may appoint a consultative committee made up of members of the Board or managers from outside the Board, or members of Board and managers (Article 153)

* * *

One can exercise more than four chairman's mandates, provided that General Managers are appointed in two out of the four companies that he chairs. No one can be Director in more than six companies, whose head office is in Lebanon. If a Director is over 70 years of age, he may not hold directorship in more than two companies. Is considered chairman or Director of a single company whoever is chairman or Director of several insurance companies operating under the same style. (Article 154)

* * *

The attendance or representation of at least half of the Directors is required for the validity of the Board's resolutions. A Director is forbidden to represent more than one other Director (Article 156)

* * *

The chairman of the Board of Directors and, eventually, the General Manager or the Managing Director in pursuance of sub-paragraph 4 of article 153, representing the company before Third Parties, assume the execution of the resolutions of the Board and the dispatch of the company's current business, such as may be determined by the Articles or usage, under the supervision of the Board of Directors.

* * *

The Board of Directors may, for a short and limited period, delegate certain of its powers to its chairman or to the Deputy General Manager, such delegation being subject to registration on the trade register (Article 157).

Any deal concluded between-the company and a Director is subject to the prior approval of the general meeting, whether such deal is transacted directly or through a middleman. Acts covering day-to-day operations between the company and its customers are exempted from this provision.

* * *

Equally submitted to this authorization is any transaction passed between the company and another establishment which would be owned by one of the Directors and in which the latter would be a joint partner, manager or director: The Director who should be in- one of these cases is required to advise the Board of Directors accordingly.

* * *

The Board of Directors and the supervisory commissioner submit - separately -to the general meeting a report on the transactions to be concluded, and the general meeting shall take its decision in the light of these two reports. Transactions so authorized may not be incriminated except in the event of concealment. (Article 158)

* * *

Directors must establish, at the end of the first semester of every financial year, a summary statement of the liabilities and assets, and, at the end of the year, a stock-taking, a balance sheet, and a Profit and Loss Account (Article 161)

* * *

Directors are, on the other hand, responsible to shareholders for their mismanagement. As a general rule, the Directors' liability for mismanagement is not extended in relation to Third Parties. However, in the event of insolvency or juridical liquidation of the company, demonstrating insufficient assets, the commercial Court may, either on the request of the Receiver or judicial Liquidator, or that of the Public Prosecutor's office, or even officially, decide that the company's debts shall be borne, up to an amount it shall determine, by the Directors and all other persons vested with a management or supervisory mandate, with or without joint (liability). In order to clear their responsibility, they must produce proof that in their management of the company's business they have exercised the diligence of a salaried proxy. (Article 167)

* * *

Shareholders who cannot attend a meeting may have themselves represented by proxies, who must themselves be shareholders, except as regards the legal representatives of shareholders deprived of legal capacity (Article 181)

* * *

An office shall be set up, composed of at least a chairman and a secretary (Article 183)

* * *

Any shareholder, whatever the type of shares he holds, and even though he possesses only the provisional voucher, may cast his vote (Article 185)

* * *

Without prejudice to the double voting power which is the privilege of holders of registered shares for at least two years beforehand, as was explained above, each shareholder has as many votes as the shares he holds or represents, without limitation thereon, unless such limitation is formally provided by the Articles, and on condition it is identical for all shares, irrespective of the category to which they belong (Article 186)

* * *

The shareholder is precluded from voting in his personal name or as proxy, whenever the matter concerns vesting him with a specific advantage or that the meeting is required to take a decision in respect of a dispute between himself and the company (Article 187)

* * *

Subject to the nullity of subsequent deliberations, any shareholder, any debenture-holder may have access at the head office to stock-taking, the Balance Sheet, the Profit and Loss Account, the list of shareholders, the report of the Board of Directors, the report of the supervisory commissioners, the consolidated Profit and Loss Account and the consolidated Balance Sheet if any exists, and to the report of the supervisory commissioners on these consolidated Account and Balance Sheet, within the-fifteen clear days preceding the annual meeting. Directors are required to complete the list of shareholders as and when stocks to Bearer are deposited (Article 197)

* * *

The ordinary meeting is to be composed of a number of shareholders representing one-third at least of the company's capital. If such quorum is not obtained, a second meeting shall be convened, and it deliberates validly, whatever portion of the capital is represented (Article 198)

* * *

Regarding the resolutions involving modification of the company's object or form, quorum must not be less than three-quarters of the company's capital (Article 202).

ANNEX II. REGULATION OF RELATED PARTY TRANSACTIONS

Any deal concluded between the company and its director is subject to the prior approval of the general meeting, whether such deal is transacted directly or through a middleman. Acts covering day-to-day operations between the company and its customers are exempted from this provision. Equally submitted to this authorization is any transaction passed between the company and another establishment which would be owned by one of the directors and in which the latter would be a joint partner, manager or director. The director who should be in one of these cases is required to advise the Board of Directors accordingly.

The Board of Directors and the supervisory commissioner submit to the general meeting a report on the transactions to be concluded, and the general meeting shall take its decision in the light of these two reports. Transactions so authorized may not be reversed except in the event of concealment. Authorization must be renewed every year if it concerns transactions involving long-term consecutive commitments.

Directors are forbidden, except when they are juridical persons, to obtain in their favour from the company, in any manner whatsoever, an open current account, a guarantee or an endorsement of trade Bills made out to the order of third Parties. Such prohibition does not apply to banks if the aforementioned acts constitute normal operations within the scope of these banks.

In addition, banks are forbidden to carry on a trade, an industry or any activity whatsoever which is alien to the banking profession; enter into association, in whatever form, with industrial, commercial, agricultural enterprises or others, in compliance with the provisions of article 153; grant credits, in any form whatsoever, to their supervisory commissioners, to the Central Board and to the Central Bank's personnel of all grades, as well as to the family members of such persons; grant, either directly or Indirectly, credits to members of its Board of Directors or to persons in charge of its management, to its principal shareholders and to relatives of such persons without compliance to the following conditions.

Credits shall be the object of a prior authority, in principle, from the shareholders general meeting which would specify at least the maximum level of credits that could be granted to each person, while it would be the duty of the Board of Directors and of the Supervisory Commissioners to advise the shareholders ordinary annual meeting of the grant conditions governing such credits and of the way such conditions shall be met;

b) The granting of every credit must be the object of an express permission of the Boards of Directors specifying the amount and the terms.

c) Credits shall be covered by collateral security or by bank guarantee from a finance establishment duly registered in Lebanon and acceptable to the Supervisory Commission. Such credits shall not exceed, in the aggregate, 25 per cent of the bank's own funds.

e) Any bank may grant these credits to members of its Board of Directors, to persons in charge of its management and to its principal shareholders, irrespective of the conditions stated in this article, within a margin of 6 per cent of its own funds and the maximum level referred to in the preceding subsection.

f) It shall be the duty of the Banking Control Commission to appreciate to what extent the provisions of this article shall apply to specific accounts and risks.

Where diverging viewpoints arise between the Banks Control Commission and the board of the bank concerned, the matter shall be referred for adjudication to the Central Bank's Board. The decision of the Central Bank's Board in this respect shall be considered as final and no means of administrative or judicial review shall be accepted.

Source: Code of Money Credit, Article 152, Code of Commerce, Article 158.

ANNEX III. BENCHMARKING OF KEY CORPORATE GOVERNANCE REQUIREMENTS

The following table provides a benchmarking of the Lebanese corporate governance requirements against select MENA jurisdictions. Considering the Lebanon has two main corporate governance regimes (for banks and for listed companies), both have been included for the purposes of the benchmarking.

Indicator	Lebanon (2016)	Egypt (2016)	Qatar (2009)	Saudi Arabia (2017)	Bahrain (2010)
Key source of corporate governance rules	Listing requirements, BDL Circulars, Code de Commerce	Comply-or-explain corporate governance code, listing rules, company law	Comply-or-explain corporate governance code, company law	CoE and mandatory provisions, company law	Comply-or-explain corporate governance code, company law
Size of the board	Specified for all joint stock companies as per the CC: 3-12 members Specified for listed companies (future IPOs): 3-12 members	Minimum 3, no maximum	Not specified	3-11	Less than 15
Requirements to have CEO/ Chairman separation	No, posts joined as per Commercial Code	Yes	Yes	Yes	Yes

Indicator	Lebanon (2016)	Egypt (2016)	Qatar (2009)	Saudi Arabia (2017)	Bahrain (2010)
Number of non-executive directors	Specified for listed companies only (majority) Recommended for banks, no specific proportion	Majority	Majority	Majority	Majority
Number of independent directors	Listed companies: at least one third or 2 whichever is greater Banks : 3 required	One third	At least 1 independent	Not less than 2 or one third of members whichever is greater	At least 3, including the Chair
Term of appointment of board members	3 years as per the CC, 5 years for the first mandate	Not specified	Not specified	3 years, may be reappointed	3 years, may be reappointed
Frequency of board meetings	Banks :4 times annually Listed companies: 4 times annually	Minimum 4 annually	Minimum 6 annually	Minimum 4 annually	Not specified
Board meetings' attendance requirements	Quorum set at least 1/3 of the company capital 4 board meetings annually for banks and listed companies	4 times annually (companies law)	Not specified	50% and no less than 3	Not specified

Indicator	Lebanon (2016)	Egypt (2016)	Qatar (2009)	Saudi Arabia (2017)	Bahrain (2010)
Limit on concurrent board appointments	For all companies: 6 boards 4 mandates for board Chairs unless GMs are appointed in some of these (splitting CEO/ Chair duties)	No (except for banks)	No	5	3 directorships in public companies
Conflict of interest provisions	Banks: in BDL circulars Listed companies: Listing Regulations and Market Conduct Regulations	Yes	Yes	Yes	Yes
Existence of board committees	Banks: Audit Committee, Risk Committee, Remuneration Committee. Listed Companies: Finance and Audit, Nomination and Governance	Audit committee (listing rules) Remuneration, corporate governance, risk and investment committees comply or explain	Audit, nomination and remuneration	Audit, remuneration, nomination and risk	Corporate governance, audit, remuneration and nomination

Indicator	Lebanon (2016)	Egypt (2016)	Qatar (2009)	Saudi Arabia (2017)	Bahrain (2010)
Composition of committees	Banks: Risk Committee - at least 3 board members, independent Chair; Remuneration Committee - at least 3 non-executive board members, independent Chair Listed companies: Finance and Audit Committee with at least 3 independent/non-executive members; Nomination and Governance Committee of at least 3 members and non-executive Chairman Each committee to have at least 1 independent and 1 non-executive director	Audit committee: at 3 board non-executive board members. No rules on nomination and remuneration. 3 non-executive of which 2 independent, voluntary recommendation	Chair to be independent and to include at least 3 non-executive board members	Remuneration and Nomination Committees all non-executive and at least 1 independent member. Risk Committee majority non-executive.	Corporate governance at least 3 independent members; Remuneration Committee only non- executive and majority independent, Chair independent
Audit Committee	Banks: Audit Committee at least 3 non-exec board members, independent Chair Listed Companies: at least 3 members majority non- executive or independent	Audit committee: at 3 board non-executive board members, listing rules	Chair to be independent and to include at least 3 non-executive board members	Audit: no less than 3, no executives, one financial specialist	3 members, Chairman independent, specific financial literacy requirements

Indicator	Lebanon (2016)	Egypt (2016)	Qatar (2009)	Saudi Arabia (2017)	Bahrain (2010)
Frequency of Audit Committee meetings	Banks: on a quarterly basis with in presence of 3 board members Listed companies: no	Quarterly reports to the board, listing rules. Quarterly meetings, voluntary	Not specified	Not specified	4 times annually
Company Secretary	Banks: no Listed companies: no	Yes	Yes, qualifications outlined	Yes, to be selected among board members or a third party	Yes
Board remuneration	Not specified but must be disclosed for banks and listed companies	Board fees cannot exceed 10% of the dividend, to be approved by the AGM	Not specified	Lump sum, attendance allowance or percentage of profits allowed, limit not set	Not specified
Corporate governance report	Yes, for banks and for listed comp-anies	Yes, board members report required	Yes, including CV of each board member	Yes	Yes, detailed composition specified by the regulator

Source: GOVERN Research, 2017.

ANNEX IV. BENCHMARKING: CORPORATE GOVERNANCE DISCLOSURE BY SELECT BANKS

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Corporate Governance website	Separate dedicated page on the website	Separate dedicated page on the website	Separate dedicated page on the website	Separate dedicated page on the website	Separate dedicated page on the website
Shareholder transparency	Comprehensive disclosure of the ownership framework; some shareholders not disclosed	Comprehensive disclosure of the ownership framework; disclosure of ownership by families as opposed to individual investors	Disclosure of ownership structure down to 1% shareholders in the corporate governance code, not regularly updated	Disclosure of ownership down to 2% of shareholders and individual attributions; reporting not up to date	Ownership not disclosed
Corporate governance guidelines	Guidelines drafted in 2006	Guidelines drafted in 2006 and updated in 2016 Bank strives to adhere to IFC and OECD Principles	Yes, corporate governance guidelines/board charter issued in 2007; last updated in 2011	Not reported	Yes, corporate governance guidelines, last updated in 2014

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Corporate governance report	Precise composition of the report included in the corporate governance guidelines	Yes, part of the annual report but not comprehensive	Yes part of the annual report but not comprehensive	Not reported	Part of the annual report
Size of the board	Maximum 12 as per the guidelines. In addition, non-voting honorary directors can be appointed	3-12 as per the guidelines, the ideally should not fall below 6. In addition, non-voting honorary directors can be appointed	12 board members	12 members	9 members
CEO/ Chairman separation	No, posts are explicitly joined however Vice Chairman appointed to chair board meetings in absence of Chair	No, but there are two Chairmen: one of the BLOM Group and one of BLOM Bank SAL	No, posts are joined though Chairman can delegate some of this authorities	No, though a Deputy Chairman who is also the General Manager has been appointed (same family)	Yes, the post of an Executive General Manager (EGM) was created to carry out many of the executive responsibilities vested in the GM
Presence of non-executive directors	Half as per the corporate governance guidelines	Majority of the boards independent and/or non-executive Some weaknesses in the definition of non-executive directors	Sufficient number of non-executive directors Current board 9 non-executives	Majority non-executive as per the bank's definition	7 non-executive

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Presence of independent directors	At least a third as per the corporate governance report; definition of an independent director more comprehensive than BDL's definition	Definition of independent directors not comprehensive; independent directors vote annually to elect a lead director	Current board 7 independent directors; definition of independent directors not robust	Not reported	4 directors; definition of an independent director unclear
Concurrent appointments	Maximum 4 outside Bank Audi, 75 years old limit	Chair of the board cannot hold the same role in more than 4 companies, under the condition that GM in 2 of these (as per the BDL regulations)	No limitations on concurrent appointments except those specified in the Code of Commerce. No multiple mandates in companies in the same sector, unless with an authorization of the AGM	Not reported	Not reported
Frequency of board meetings	At least 6 times per year of which at least twice in Lebanon	At least 4 times, of which at least twice in Lebanon	At least 4 times, of which at least twice in Lebanon	4 times per year (during 2015)	Not reported
Board meetings attendance	Not reported	Reported in the annual report and on the website. Attendances ranges from 64-100 percent.	Not reported	Not reported	Not reported

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Quorum for board meetings	50%+1	50%+1 except for extraordinary general assemblies; in some committees (i.e. Governance Committee) quorum is decided by the Corporate Secretary of the Committee at each meeting	Majority	Not reported	Not reported
Document distribution before board meeting	A week or minimum 48 hours if required	First bank in Lebanon to have appointed an independent Lead Director	Specific deadline not specified, but documents can be amended up to 48 hrs in advance	Not reported	Not reported
Board evaluation	Annually according to a methodology set by the board	Annual performance evaluations to be organised by the Company Secretary. Self-evaluation by the board and board evaluation of the Chairman	A self-evaluation after each meeting as well as an annual self- assessment of the board as a whole and individual members	Not reported	Not reported
Specific criteria for appointment of board members	Yes	No	No	No	Not reported

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Director education	Orientation and continuous education	Orientation and continuous education	Orientation and continuous education	Not addressed	Orientation and continuous education
Capacity for external consultation by the board	Yes, noted explicitly in the corporate governance guidelines	Yes, noted explicitly in the corporate governance guidelines	Yes, noted explicitly in the corporate governance guidelines	Not addressed	Not addressed
Board committees	Audit, Risk Governance and Remuneration, Executive Committees .Each committee to have a charter.	Audit, Risk Management Strategy and Corporate Governance, Nomination and Remuneration Committee, Compliance Committees	Risk, Compliance, Anti-Money-Laundering and Combating the Financing of Terrorism, Human Resources, Compensation, Remuneration, Nomination and Corporate Governance, Audit Committees	Corporate Governance, Risk Management, Audit, Remuneration Committees	Audit Committee, Risk, Credit, Remuneration Committee (not indicated on the website but in the annual report)

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Committee Composition	Not addressed by corporate governance guidelines	Not addressed by corporate governance guidelines but in each committee charter publicly available online. Audit Committee minimum 3 non-executive directors (total Committee size not specified). Risk management min 3 of which 2 non-executive, Chair independent. Governance committee at least 3 non-executive members, who should be at least half of the committee and independent Chair. Nomination Committee all non-executive and independent Chair. Compliance Committee to be comprised of at least 3 board members, Chair independent	Mostly independent directors according to the website, each committee comprised of 3 members. Only one member can be a member of both Audit and Risk committees; Audit and Risk Cannot be chaired by the same director	Charters for each committees established but not publicly available, hence committee composition not available	Audit Committee composed of non-executive and independent members, chaired by an independent director. According to the annual report, led by independent chair, one exec and one non-executive. Risk Committee composition not defined except to be chaired by an independent director. Credit Committee to be composed of 4 members. Remuneration and Audit Committee chaired by independent directors. Committee membership unclear from the website

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Frequency of Committee meetings	Not specified in the Corporate Governance Guidelines	Audit, Risk and Compliance committees 4 times a year, at least 2 in Lebanon. Corporate Governance Committee and Remuneration Committee at least 2 times per year	Not addressed	All but the Remuneration Committee meet 4 times a year. Remuneration Committee meets twice a year	Not addressed
Company Secretary	Yes	Yes, the Head of the Group Internal Audit is the secretary of the Audit Committee. Chief Risk Officer is Secretary of the Risk Committee. Head of Compliance is the Corporate Secretary of the Compliance Committee	Yes	Not addressed	Not addressed

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Board remuneration	Not disclosed. Every director should to hold at least one year's remuneration in Audi stock until they retire. Directors should disclose on an annual basis the number of Audi shares they own and the number of shares they acquired and sold during the preceding 12 months to the Corporate Secretary	Not disclosed. Each board member must hold at least 500 shares. Direct and indirect share ownership by board members available from the website	Attendance fees only	Not addressed	Not addressed
Investor relations function	Yes, only online contact form	Yes, comprehensive website with a dedicated contact person	No specific contact provided on the website, last investor presentation over a year old	None, not applicable as the bank is closely held	None, not applicable as the bank is closely held
Risk management (CRO, etc).	Yes, reporting to the board	Yes, reporting to the board Also, a whistleblowing function introduced	Risk management function described in broad terms	Not addressed	Risk management function described in broad terms

Criteria	Bank Audi	BLOM Bank	Byblos Bank	Fransabank	Bank Med
Auditor rotation	Not explicitly addressed in external filings, discussions reveal a rotation of senior partner	Every 3 years, however rotation of audit partner without changing firms is considered sufficient	Not addressed	Not addressed	Not addressed
Other	Annual board retreat. Produces annual CSR Report. Corporate governance code addresses primarily board composition, responsibilities and effectiveness. Does not address shareholder rights. Governance guidelines address the content of the Annual CG Report in a detailed fashioned beyond board composition)	Existing shareholders have a preferential right to subscribe to capital increases proportionate to their ownership. Shareholders can vote by proxy. Extraordinary meetings can be called by shareholders owning 20% of shares by contacting the auditor, same applies for placing items for AGMs. Extensive provisions on RPTs in the governance guidelines	Related party transactions addressed quite comprehensively in the governance manual	The annual report is only available in Arabic. Significant disclosure on CSR activities	Related Party Transaction and Conflict of Interest Policy adopted bank wide. The bank addresses corporate governance through detailed policies established at the level of its international subsidiaries. An International Committee established to follow up on corporate governance in business units

Source : GOVERN Research, 2017 based on the publicly available information provided by the select banks.

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