



## *Lebanon's compliance and constraints*

*By : Dr. Paul G. Morcos \**

Lebanese Banking Secrecy system, traditionally known in the world, aims at increasing the confidence in the banking sector and encouraging the flow of foreign funds; however, it is no more an absolute privilege for banks to enjoy, as they are subject to abide by the fighting Money Laundering and tax evasion Laws: the Special Investigation Commission - Lebanon's FIU that is - has the power to lift banking secrecy in case of illicit deposits or when accounts of suspected people involved in money laundering and terrorism financing are identified.

Lebanon has taken – and is still taking – to comply with regulatory requirements which include voting laws on lifting banking secrecy to fight money laundering, terrorist financing, and tax evasion.

The laws enacted considered topics on:

- o Fighting Money Laundering and Terrorist Financing<sup>1</sup>
- o Exchange of Tax Information<sup>2</sup>
- o Declaring the Cross-Border Transportation of Money<sup>3</sup>

In November 2015, the Lebanese Parliament adopted the required laws though article 75 of the Constitution stipulates that the Parliament

should immediately elect the President of the State – absent it has been two years now- as a result of which, it loses its legislative capacities and becomes a pure electoral body.

On the other hand, as some states or organizations might perceive Lebanon as a potential financial access point into the global system. The Lebanese financial institutions are being always alert to this threat, where they apply sound and rigid (KYCs) and Enhanced Due Diligence measures to identify PEPs, high risk clients and sanctions evasion schemes, or cases where layers are created for the purpose of hiding the ultimate beneficial owners as seen in Trusts.

In its circular number 126, the Central Bank of Lebanon – and here I quote – also “requires banks to be fully informed about the laws and regulations that govern correspondent banks abroad, and to transact business in accordance with such laws, regulations, and procedures adopted by international legal organizations or by the sovereign authorities in the correspondents’ home countries.”

The Central Bank, in conjunction with the Association of Banks and the Union of Arab Banks, is continuously focusing on the

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<sup>1</sup> Law No. 44, issued on 24-11-2015 – amending Law no. 318 of 2001 to include a wide range of predicate offences such as tax evasion as well as additional requirements

<sup>2</sup> Law No. 43, issued on 24-11-2015

<sup>3</sup> Law No. 42, issued on 24-11-2015



appropriate processes to assert that local banks are compliant with the international standards and to maintain Lebanon's standing as a safely sound and attractive banking location. The Laterals provide on-going training sessions, seminars, and conferences to support qualifying Lebanese banks' employees as far as AML/CFT matters are concerned.

Following these procedures – and maybe many others to come – the Financial Action Task Force (FATF) announced, in early 2016, that Lebanon meets all the necessary conditions for fighting money laundering.

Lebanon being a dollarized economy is highly influenced by the US legislations and sanctions programs. The Central Bank of Lebanon and the Lebanese banks, collectively, aim at not failing to comply with the regulatory requirements.

However, despite the fact that we do understand the US concerns which we highly consider, still, we believe that blacklisting Lebanese banks preferably be communicated and coordinated with the Lebanese Regulators prior to taking any regulatory actions.

Now to address the issue of politically exposed persons, PEPs pose a substantial legal and reputational risk to the financial and economic sectors. The world has witnessed quite a few PEP scandals involving heads of states, their family members, and close associates.

The no secret secret is that Lebanon is highly influenced by PEPs. Regulators, however, refuse (or the PEPs) allowing them abuse the Banking Secrecy Law. Accordingly, a set of related procedures was developed for banks to

adopt, in order to support increase the quality and effectiveness of their controls against this influence. These procedures include:

- Applying Enhanced Due Diligence to All PEPs, Foreign and Domestic.
- Requiring a Declaration of Beneficial Ownership.
- Requesting Asset and Income Disclosure as part of their KYC.
- Performing frequent periodic review of PEP Customers.

Most of the Lebanese banks, even, go beyond the legal definition of a PEP. They apply a broader scope of enhanced due diligence (EDD) measures than those required under either domestic legislation or regulation.

#### Constraints

Now to underline some important constraints that despite all the procedures Lebanon is taking to fight money laundering and terrorist financing, and its abiding by the international regulatory requirements, I believe we should seriously consider them, as they complicate – if not obstruct – the banking transactions that, in turn, negatively affect the Lebanese economy.

#### - First are the Gulf Sanctions on the Lebanese Economy

As we all know, the GCC – led by the Kingdom of Saudi Arabia – are, recently, taking further steps to penalize Lebanon economically in retaliation for the growing political power of Hezbollah. In February, Saudi Arabia stated that it had suspended a \$3 billion military aid for the Lebanese Armed Forces.

Additional financial penalties might be effected. Some funds transfers from Saudi

Arabia to Lebanon are being banned. I believe, we should not underestimate its impact not only on the Lebanese banking sector but also on the overall Lebanese economy, keeping in mind that Lebanon depends heavily on the Arab investments and remittances from Lebanese diaspora in the Gulf.

We should not fail to mention, here, the recently raised talks about GCC countries considering pulling their deposits from the Central Bank of Lebanon and reducing their other investments in the country. Withdrawals from the Central Bank would probably contribute in putting Lebanon's credit rating at risk as any further declines would make sovereign borrowing more difficult – if not impossible.

#### - The second constraint I would like to speak about is the US Sanctions (HIFPA)

In December 2015, President Obama signed the Hezbollah International Financing Prevention Act of 2015 (HIFPA) that seeks to drastically cut back Hezbollah's ability to conduct business and utilize the international banking system.

This Act further pressures the Lebanese banks as the law throws responsibility on them for not deliberately facilitating and carrying out financial transactions for Hezbollah.

The Lebanese financial sector needs now to be extremely cautious in this regard as far as deposits and loans are concerned; additional strictness in applying KYC and Enhanced Due Diligence procedures will be required keeping that we are not maybe considering the difficulties accompanied with the implementation process as Hezbollah plays

a significant role in Lebanon given its medical, educational and social institutions that spread amongst the Shiite community, also the complexities of identifying relatives and associates besides the political supporters.

The Lebanese Banks would neither want to risk nor to jeopardize their business relationships with their US correspondents; lately, they are bearing the burden of increased queries and investigations due to HIFPA.

An assurance from the U.S. government that it is Hezbollah who is being targeted, and not the Lebanese banks or Lebanon, will relief banks from their concerns.

In addition, the extent of information shared by the US Financial Intelligence with Lebanese counterparts is not clear so far.

#### - Third comes the constraint resulting from the Syrian Refugees issue

The official Syrian refugee population in Lebanon, according to the U.N. refugee agency, UNHCR, reached over 1.1 million in 2015. Set aside the social responsibility, unemployment rate in Lebanon is massively increasing as Syrian refugees are competing with the Lebanese laborers through carrying, out non-skilled labor at significantly lower wages, which in turn is making job creation a rigorous problem on the economy.

#### - The fourth important constraint is ISIS

Counter-ISIS financing is a new challenge that both the Lebanese and the international banking sectors are equally encountering. The Lebanese financial sector, collectively, is creating multiple lines of defense that aim to forbid ISIS from having access to their products and services. This is achieved by





including as main pillars in their compliance programs not only the local AML requirements but also the international standards set by FATF, Basel Committee, Wolfsberg Group and many others international organizations such as the World Bank and the International Monetary Fund (IMF).

While applying an effective AML/CFT regime, still, the Arab and Lebanese Banks are facing major challenges, especially that funds that are sent to individual ISIS fighters. According to U.S. government information, as of December 31, 2014, at least 19,000 foreign Jihadists from more than 90 countries have left their home countries to travel to Syria and Iraq to join ISIS.<sup>4</sup>

Taking all this into account and considering all the givens in Lebanon and the surrounding region, we wish the United States would more be aware of the geographic battlefield against ISIS that is being undergone at the Lebanese-Syrian cross borders.

Finally, a couple of questions I would like to raise here:

- a. What could be the radical measures the United States could take to curb ISIS' oil "business"?
- b. What are the chances to provide the Lebanese authorities with ISIS black lists knowing that the US security agencies now probably possess the names of foreign fighters?



<sup>4</sup> <http://www.fatf-gafi.org/media/fatf/documents/reports/Financing-of-the-terrorist-organisation-ISIL.pdf>