

As Lebanon's central bank audit crumbles, the worst is yet to come

Houshig Kaymakamian, Al Arabiya English Wednesday 02 December 2020

Lebanon's controversial central bank forensic audit fell apart last week, signaling that the worst may be ahead for the crisis-stricken country.

[Alvarez & Marsal](#), the company contracted by the Lebanese state to carry out the forensic audit of the central bank, also known as Banque du Liban, said it withdrew from the agreement two months after it was signed as it had not received the information from the central bank necessary to carry out its task, and it was not confident it would.

Lebanon is in the midst of an economic and financial crisis, the worst since the end of the civil war in 1990. The local currency has seen more than 80 percent of its value against the dollar slashed, sending more than half the population into poverty as inflation rates sky-rocket.

A forensic audit is a prerequisite for desperately needed international financial aid to flow into the country, specifically from the US and France and in order to re-kindle frozen negotiations with the International Monetary Fund for a bailout.

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The company's withdrawal came as a surprise to Lebanese officials, as the outgoing Finance Minister Ghazi Wazni had announced a three-month extension on the contract earlier in November, promising that the requested information would be secured.

"Set up to fail"

"I think it [the contract] was set up to fail by design, and it speaks to the flagrant lack of political willingness in the country to investigate the [central bank]," Nafez Zouk, lead economist and emerging markets strategist at Oxford Economics told Al Arabiya English.

“Not enough of the groundwork was laid out in preparation for this contract to be successful,” he said.

A leaked document by Forbes showed that the central bank had refrained from answering more than half the questions asked by Alvarez & Marsal. Central bank Governor Riad Salameh has cited the banking secrecy law in Lebanon – a law fewer than 10 countries in the world still adopt – as blocking the central bank’s ability to provide needed information to the auditing firm.

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However some questions had nothing to do with banking secrecy, such as ones on the governance structure and the inner-workings of central bank, which signaled an explicit lack of willingness to cooperate on the bank’s part.

“The banking secrecy law is not the real obstacle for the forensic audit,” Paul Morcos, a lawyer and renowned legal consultant told Al Arabiya English.

Caretaker Prime Minister Hassan Diab and his outgoing Justice Minister Marie-Claude Najm have both accused Salameh of obstructing the audit.

Morcos said that the real obstacle standing in the way of the forensic audit was, and is, that there is no will to facilitate it by a lot of the political players in the country.

“Yes the banking secrecy might be seen as being a technical obstacle, but this is very easy to overcome,” he said.

The legal expert explained that the banking secrecy law could either be amended by Parliament, or the institutions and beneficiaries could simply be asked to lift it for the purpose of the forensic audit and provide their authorization.

An anti-government protester shouts slogans while wearing a mask with the colors of the Lebanese flag in Beirut, Lebanon, Thursday, July 2, 2020. (AP)

Further, the central bank was a third-party to the contract signed between the New York-based consultancy and the Lebanese state.

“So basically you are asking the entities being audited to supply the information voluntarily; clearly that’s a flaw in the contract,” Zouk said.

“Why would the [central bank] willingly supply information that could potentially incriminate it if it is not compelled to do so by legislation?” he added, highlighting the importance of legislative action to support the contract so that central bank doesn’t have “any excuses to hide behind.”

What were they looking for?

Morcos also pointed out that the scope of the contract was very broad, with no clear indication of what the auditors would be looking for.

“What are we looking for? Is it embezzlement, is it fraud, is it money-laundering, financial engineering, misused loans? If they don’t put clear targets for this mission then they won’t have clear outcomes,” he said.

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Morcos wasn’t sure if information gathered in the event of a successful forensic audit would be credible, sufficient and constitute grounds for legal prosecutions.

Lebanon’s banking system for years resembled what experts have dubbed a “Ponzi scheme” that has bolstered the banking system by offering unreasonably high interest rates. And over the past few years, Salameh has carried out unorthodox financial engineering schemes that has over the past years boosted foreign currency reserves.

Even French President Emmanuel Macron in a speech in September likened Lebanon’s banking system to a Ponzi scheme.

But with Lebanon facing acute dollar liquidity issues for a year, Lebanese banks have been forced to impose illegal capital controls on foreign

currency transfers and withdrawals, and the façade has come crashing down, making an audit the first step in righting years of wrongs.

Reputation at risk, dwindling chances of aid

The failure of the first forensic audit contract has further tarnished Lebanon's already damaged reputation.

"The international community will not take us seriously [anymore]," Morcos said.

However Lebanon's reputation is not the only thing at stake.

Former Lebanese Prime Minister Saad Hariri addresses the media on Aug. 18, 2020. (AP)

"There is also a reputational risk for the companies [the government] want[s] to attract," Zouk noted.

With a big global firm pulling out from a contract with the Lebanese state, other giants could hesitate to entangle themselves with the troubled country.

"Now we need to prove even more that we're willing to give any next auditor unfettered access to information," Zouk said.

However, Morcos said that Lebanon should not lose more time and funds by assigning a new company if political will to carry out the audit will not materialize.

Zouk warned that the chances of international aid were dwindling.

"We know what we need to do to unlock the aid but nobody is doing it," he added.

Protecting an increasingly small pie

Without the audit, Lebanon is back at square one. President Michel Aoun this week sent a letter to Parliament underlining the importance of the forensic audit of the central bank to prevent the country from being perceived as a "rogue" state by the international community.

Members of Parliament on Friday gathered to discuss the audit and concluded the session with a decision – which is not binding – that stipulated that the central bank and all state institutions should undergo a forensic audit. They also agreed that banking secrecy would be waived, but it was not made clear how this new audit, now extending to all state institutions would be carried out.

Morcos said that the decision should have been called a “recommendation” since it has no legal weight. He reiterated that Parliament should have issued a law amending banking secrecy, which they did not.

Salameh told TV station Al-Hadath Tuesday night that he would provide access to government accounts to auditors, but reiterated that revealing the contents of bank accounts would require a change in legislation.

“I don’t think there will be a third contract because in all likelihood if **[Prime Minister-designate Saad] Hariri** is to head a new government, he won’t push for a forensic audit,” Zouk said.

Lebanon is marred with decades-old corruption and mismanagement by the entire political class that ultimately has led to the current state of collapse.

“The ruling elite is now in a position where it is fighting for its own survival as it is facing an existential threat because the rest of the society has woken up to their failure and failed system,” he said.

“They’re trying to protect share of an increasingly smaller pie, I guess for them it’s better than nothing and they get to stay in power a bit longer.”

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