Mobilizing the Private Sector for Corporate Governance
Dr. Nasser Saidi

This article is an excerpt from Dr. Nasser Saidi's speech at a recent focus group discussion on the state of corporate governance in Lebanon organized by CIPE, the Private Sector Task Force on Corporate Governance and the Lebanese Transparency Association. Dr. Saidi is former Minister of Economy and Trade, Minister of Industry, and First Vice Governor of the Central Bank of Lebanon.

The Arab region has been failing to attract foreign and local investment. In fact, the money that is flowing to this area is mainly directed at exploiting mineral resources, oil, and gas. As for financial investments, no individual or country seems to be interested in investing in either bonds, shares, or the equity markets. The region's share of world capital flows ranges between 1.5% and 2% only. On another level, the region is experiencing a rapid growth of its population, leading to burgeoning unemployment rates and a socio-economic and environmental disaster. In fact, within ten years, 60 million jobs must be created. Following the events of September 11th, 2001, the outward flow of capital generated from the Arab region was restricted. One would be fooled to believe that investments have increased in the region after September 11; however, the new financial barriers erected by the West are the reason why large Arab investors have poured their money into other Arab countries. Once the new barriers are relaxed or removed, I believe that the money will flow out.

Why are we not able to attract resources, while our own *raw* natural resources are being exploited and human resources are leaving? Corruption, waste, bribery and the lack of transparency add to the multitude of risks to investment in the region and hamper the fundamental socio-economic development and well being of its populations. On that basis, we should formulate an action plan for the implementation of a transparency scheme for corporate governance that defines the stakeholders, the resources devoted to the plan, and the tools planned to execute it.

On a practical level, however, we should be aware that small and medium enterprises (SME's) will have difficulty enforcing the principles & standards of corporate governance. For example, some 85% of Lebanese firms have fewer than ten employees and 90% of these firms are family-owned. The enforcement of corporate governance measures for SME's is rather costly. Thus, the question of how to reduce the cost of compliance and transparency must be addressed.

So, how do we advance corporate governance in the Arab world? It is important to get the stakeholders on board in order to find feasible and pragmatic ways to implement the sound principles of corporate governance. Let us be active with business groups –such as Chambers of Commerce & Industry- to induce them to *formally* adopt the principles of corporate good governance. Within the business groups, public discussions should be held on this issue. We should also reach out to academia, the media, and parliamentarians. Corporate governance implementation requires leadership and awareness.

One successful example for Lebanese firms to follow is the "Cadbury Report", (*for a copy of the report, contact CIPE at cipe@cipe.org*) wherein a code of business ethics within a family-run firm was put forward. Trust, honesty and reputation in business transactions are hallowed principles that have been around a thousand years; however, they have to be translated into the modern context of conducting business –such as in e-commerce- with businesses reminded regularly of such principles and creating an incentive-compatible framework so that achieving good corporate governance standards does not necessitate high costs. Convincing individual business people that good corporate governance pays off, even in an environment of pervasive bribery and corruption.

Laws, regulations and institutions must provide a supportive legal infrastructure for corporate governance. In particular, Commercial Law in Lebanon and most Arab countries needs to be reformed, in order to better streamline corporate governance principles within the laws. For example, commercial law does not separate ownership from control. However, one must be realistic; in the process of advocating reform and the modernization of corporate law, one must take account of the preponderance of family-owned businesses in the Arab countries, and be careful not to infringe on individual freedom to choose and dispose of wealth.

We also need to focus on corporate governance within public utilities and agencies. Given the importance of public production of goods and services in most Arab countries, governments must ensure that public sector entities are well managed in accord with private sector good governance principles. Further, if a policy of privatization is the order of the day, then having efficient and well supervised financial markets becomes essential. Financial markets are able to impose transparency, discipline and accountability, if privatized corporations are legally required to get listed on the stock exchange. Stock exchanges can play this role on condition that they are efficient and supervised by an independent capital market authority. Hence, in many cases, a modern capital markets law must be put into force.

In Lebanon, a draft law that privatizes the capital markets (the Beirut Stock Exchange) was prepared five years ago, but is still awaiting review on the shelves of the Ministry of Finance. The problem lies in the lack of public action and lobbying to push this draft law into realization. The Parliament needs to be involved. The missing link is the lack of lobbying initiatives. Good communication and effective lobbying can play an important role.

So what do we need to do? How do we advocate better corporate governance? One idea is to seek implementation of 12 key, internationally recognized, generic standards for sound financial systems[1] and to follow up on Lebanon's (and other Arab countries) compliance with these standards. The standards are organized under three broad areas: Macroeconomic Policy and Data Transparency; Institutional and Market Infrastructure, and Financial Regulation and Supervision.

1) Monetary and financial policy transparency—this standard is formulated in the form of a Code of Good Practices on Transparency in Monetary and Financial Policies, with the issuing body being the IMF.
    - Lebanon has achieved substantial progress in this area

[1] See the FSF - Financial Stability Forum: 12 Key Standards for Sound Financial Systems

2) Fiscal policy transparency—the standard is the Code of Good Practices in Fiscal Transparency; the issuing body is the IMF.
   - Lebanon is seeking to implement the Code.

3) Data dissemination—the standards are the Special Data Dissemination Standard (SDDS)/General Data Dissemination System (GDDS), (both issued by the IMF).
   - Lebanon has now entered the GDDS and the Central Bank, with assistance from international institutions (IMF, World Bank) is establishing the Lebanese Statistics Portal (LebStat), which will provide a statistics gateway, a single-access point to available economic, social, financial and real sector data.

4) Insolvency and Bankruptcy Procedures
   - The World Bank is assisting the Lebanese government in drafting modern insolvency and bankruptcy laws. Principles of bankruptcy are essential for the viability of corporate governance.

5) Principles of Corporate Governance.
   - The standard defined by the OECD awaits formal adoption in Lebanon by relevant institutions such as Chambers of Commerce, business & professional associations.

6) Accounting—the standard is the International Accounting Standards, issued by the IASB
   - Lebanon recognizes the IAS, but there is no mandatory implementation by business or effective enforcement.

7) Auditing—the standard is enforcing the International Standards on Auditing, issued by the IFAC
   - Lebanon recognizes the ISA, but there is no compliance mechanism for the auditing and related professions.

8) Payment and Settlement—the standards are the Core Principles for Systemically Important Payment Systems and the Recommendations for Securities Settlement Systems, issued respectively by the BIS-CPSS and the BIS-IOSCO
   - Lebanon has, with the assistance of the IMF, modernized its payments media and systems, bringing them into compliance with BIS Core Principles and related recommendations. "If the payment systems are not safe, sound, and efficient, firms would not be able to conduct business properly," said Dr. Saidi.

9) Market integrity—the standard is establishing the 40 Recommendations of the Financial Action Task Force (FATF) and the Eight Special Recommendations Against Terrorist Financing, issued by the FATF.
   - Lebanon has issued and enforces a modern Anti-Money Laundering Law (No. 318, April, 2001).

10) Banking supervision
   - Lebanon is at the forefront among emerging economies in the application of the Core Principles for Effective Banking Supervision issued by the BIS and related measures,

such as the creation credit and audit committees, general audit, and independent surveillance reporting that are directly accountable to the board of directors. It has a well-managed, professional and independent Banking Control Commission.

11) Securities regulation—the standard is the implementation of the Objectives and Principles of Securities Regulation, issued by the IOSCO.
    - Lebanon cannot effectively enforce principles and regulations in this key area, until the government establishes an independent capital market authority with the relevant mandate.

12) Insurance supervision—the standard being the Insurance Core Principles (ICP), issued by the IAIS
    - An independent Insurance Control Commission has been established as a result of passage of a Law (in 1999) leading to extensive reform of the insurance industry in Lebanon. However, policy measures have yet to be taken to implement the ICP.

Advocates of good corporate governance in Lebanon and the Arab countries should lobby and seek the adoption and implementation of the above-mentioned key standards for sound financial systems. A program should be set-up to of monitor and report on advancement in implementing the standards on a regular basis, and observe how Lebanon and the Arab countries are progressing in opening their financial markets, and improving their economic competitiveness in the global economy.

Lebanon has recently signed the Association Agreement with the European Union, which sets a framework and benchmarks for the modernization and improvement of rules, regulations, laws and institutions in Lebanon. Adopting this ‘acquis communautaire’, as the European Accession countries are discovering, would also be welfare improving in Lebanon, leading to substantial efficiency gains in economic organization and activity. Lebanon would clearly benefit from harmonizing its laws and regulations with those of the EU, which also removes any domestic foot-dragging and excuses for not reforming the economic, financial, commercial, and legal systems. Similarly, in the process of negotiating entry into the World Trade Organization, the Lebanese government stands to benefit from streamlining procedures and ‘red tape’ and introducing and/or modernizing some 17 different laws and regulatory regimes.

We should also support the widespread, comprehensive introduction of ***e-government*** in Lebanon, as an important tool for administrative reform, reduced cost of delivery of government goods and services and of government procurement, and to help in removing much of the corruption and bribery that are rampant in the private and public sectors.

The main message here is that groups advocating corporate governance reform in Lebanon should formulate an action plan and mobilize themselves, with the assistance of the media and local civil society organizations. Seeking implementation of the core standards for sound financial systems should be part of the action plan. We also should focus on the economic incentives to self-motivate, drive companies to adopt corporate governance principles, and not attempt to impose these principles on them. A combination of economic incentives, self-regulation and enforcement of laws and regulations may be needed for corporate governance to flourish. But it all starts with the private sector being pro-actively *engaged* in the development of the corporate governance environment. A private sector task force promoting corporate governance or business associations developing codes of corporate governance for its members are promising starting points. The stakes are high: better corporate and public governance improves the investment environment and leads to better institutions and higher, sustainable economic growth.