

## **Corporate Governance & Transparency Standards Across the Supply Chain for Oil & Gas<sup>1</sup>**

We all agree that good governance plays a crucial role in optimising the petroleum sector's revenues and in achieving sustainable economic development for the producing country.

*“Good corporate governance helps to build an environment of **trust, transparency and accountability** necessary for fostering long-term investment, financial stability and business integrity, thereby supporting stronger growth and more inclusive societies”. (Angel Gurría – OECD General Secretary – G20/OECD Principles of Corporate Governance)<sup>2</sup>*

However, this process should start from the day a country decides to explore and extract this resource and should be applied to all stakeholders involved in the Supply Chain.

This is the reason why a set of mandatory corporate governance rules should be carefully designed by the industry's regulators and thoroughly implemented with the integration of transparent mechanisms and the adoption of sound processes to preserve the interests of all stakeholders in this sector's supply chain.

It is evident that when extracting and managing a natural resource, the stakes are much higher, especially for developing countries. A natural resource wealth tends to make governance rules harder to implement due to the increased vested and diverged interests in dealing with this lucrative sector.

Any governance system seeking to disrupt or control these interests will certainly face fierce resistance with a great risk of this system being either overturned or manipulated if those same standards and codes are not continuously monitored by trusted institutions, non-governmental independent agencies and ultimately by the civil society.

Stakeholders involved in the Good Governance Process include:

- **Local government/Regulatory Bodies**
- **Investors/Operators/Service Providers**
- **Citizens/Civil Society**

A wide range of corporate governance codes, standards and best practice guides were established and recommended for adoption by the government and private sector involved in the discovery, extraction, production and management process of a natural resource.

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<sup>2</sup> Organisation for Economic Co-operation and Development (OECD)- The updated Principles were launched at the meeting of G20 Finance Ministers and Central Bank Governors in Ankara on 4-5 September 2015.

Some of these policies and standards have primarily focused on anti-corruption and transparency such as the Extractive Industries Transparency Initiatives (EITI); while others like the International Finance Corporation (IFC) Performance Standards have dealt with the private sector's social and environmental responsibilities when working in this sector.

I will try in this presentation to outline the main **Corporate Governance Standards** that should be observed by private sector's parties involved in the Supply Chain of oil and gas in Lebanon.

When we talk about Corporate Governance, we must essentially talk about **Transparency** which is the only way to an increased and efficient **Accountability** in any public sector or private business activity.

The implementation of Good Governance in the oil and gas sector can be only achieved through improving Transparency standards that have to be observed by all key players in the supply chain, namely by governments, operating companies and all other service providers.

However, applying efficient transparency and accountability norms can be very challenging in countries with weak institutions and where there is a complete lack of corporate governance in state owned enterprises and in most SME's and family owned companies.

This is the case in Lebanon where vested and divergent interests are relatively strong and where the public trust in the country's state-owned institutions and private corporations is significantly weak.

In this context, the Lebanese Petroleum Authority (LPA) in its regulatory capacity should consider establishing a set of Corporate Governance Standards to be observed by all companies working in the petroleum sector. This is the approach adopted in other sectors, such as the banking sector where the Central Bank requires banks and financial institutions to adhere to a set of strict rules of corporate governance based on international best practice and Basel Committee Principles for Enhancing Corporate Governance.

Companies operating in the oil and gas sector should be required to develop their own corporate governance codes with period reporting to LPA on their corporate governance practices and their compliance with such codes.

Corporate governance standards are generally divided in two (2) categories:

- i. Internal Governance, represented by the Board of Directors who monitors the Company's management and enforces accountability by hiring, firing and compensating its executives; and
- ii. External Governance, represented by the Company's shareholders, lenders and regulators.

The main internationally recognized set of Corporate Governance Standards is the OECD Principles of Corporate Governance, which cover 5 essential areas in this process, namely:

1. Protection of Shareholders' Rights;
2. Equitable treatment of all Shareholders;
3. Recognition and protection of the exercise of the rights of other stakeholders;
4. Timely and accurate disclosure and transparency with respect to matters material to the Company's performance, ownership and governance, through annual audits.
5. A framework of corporate governance ensuring strategic guidance of the company and effective monitoring of its management by the board of directors as well as the Board's accountability to the company and its shareholders.

Corporate governance standards primarily support the process of equal, efficient and transparent exercise of the fundamental rights of shareholders, mainly:

- i. The right to supervise the way the company is managed,
- ii. The right to a share in the distribution of its net profit; and
- iii. The right to a share in its assets.

In addition to protecting shareholders' interests, Corporate Governance Standards are aimed at safeguarding the rights of all other stakeholders involved in the company's operation.

Therefore, corporate governance is better achieved through an active cooperation of the Company's governing bodies with all stakeholders in order to maintain its financial stability and its compliance with applicable laws.

It is also worth mentioning that the OECD has published its Guidelines on Corporate Governance of State-Owned Enterprises to help governments assess and improve the way they exercise their ownership functions in state-owned enterprises. Good corporate governance of state-owned enterprises improves efficiency and transparency in the state-owned sector. This will result in considerable economic gains, and creates a level playing field for private and state-owned enterprises.

After a series of corporate scandals, most international corporations are now electing board of directors who are independent from management, with non-executive members and independent committees overseeing management, compensation and auditing matters.

The Lebanese legislator has finally embraced this change by introducing a new amendment to the Lebanese Commercial Law that allows for the separation of functions between a Chairman and a General Manager.

Moreover, the new amendment makes it now possible for a non-shareholder to become a board member of a Lebanese company, paving the way for companies to appoint independent directors who may be better positioned to monitor Board performance and to reduce situations of conflicts of interests between competing shareholders.

In addition to their obligations to comply with Lebanese Laws applicable to their activities, “*companies holding petroleum rights or petroleum operating rights, sub-contractors and entrepreneurs, operating non right holders*” are bound by special laws namely, Law No. 84 on the “Promotion of Transparency in the Petroleum Sector” (the “**Transparency Law**”).

Under the Transparency Law, “persons holding public political or employment positions in the country and their respective spouse, ascendants and descendants up to the first degree, and any of their partners or representatives are prohibited from, directly or indirectly, investing or holding certain decision positions in companies pre-qualified to participate in licensing rounds or holding petroleum rights (and any of their affiliates and/or mother companies), in companies qualified to have Petroleum Rights transferred to them, and their secondary entrepreneurs and sub-contractors”.

This prohibition applies for three (3) consecutive years after leaving their respective positions.

Article 7 of the Transparency Law prohibits offering or receiving benefits for the purpose of facilitating the prequalification, the obtention of a petroleum license or other types of privileges in Lebanon, leaking information classified as confidential, covering breaches in execution, or facilitating the contracting of secondary entrepreneurs with the Right Holders, and of sub-contractors with such entrepreneurs.

Companies Holding Petroleum Rights should also disclose with accuracy:

- i. their Beneficial Owners and any other information that shall be recorded in the petroleum register.
- ii. their share of the profit petroleum, the production data for each financial year and the procedures for the permanent stopping of the operations
- iii. any and all information related to the content of the permanent stopping scheme of their operation (except for confidential data) and the estimated costs of such permanent stopping of the operations.
- iv. the identity of workers in the sector as well as the ratio of Lebanese and foreign workers involved in the process.

The companies holding petroleum rights shall follow transparent procedures for recruitment, ensuring equal opportunities, diversity and selectiveness. The LPA shall ensure that right holder companies are properly implementing the recruitment scheme as approved by the LPA and shall provide the Parliament with quarterly reports in this regard.

Repetitive gross breaches of this Law by the companies holding petroleum rights, shall lead to the cancellation of the Petroleum Right or license by the Council of Ministers, at the recommendation of the Minister of Energy and Water based on the opinion of the LPA.

Companies involved in the Supply Chain should also adhere to and comply with other specific legal requirements namely:

**1. Law No. 83 dated the 10<sup>th</sup> of October 2018 on the "Protection of Whistle-blowers":**

- This Law protects any natural or legal person who denounces to the National Anti-Corruption Commission ("NACC") any past, present or future act or failure to act which he/she believes relates to the corruption of a public servant misusing his/her powers, position or job to obtain benefits or gains which are not legally due.
- Under Law 83/2018, a public servant includes, any person performing a public function or carrying out a public task, service or activity for a public institution, service or facility.
- The whistle-blower will be granted employment and physical protections.
- The denunciation shall not be considered as a breach of the person's duty of professional confidentiality, his/her identity shall be kept secret except with his/her prior approval or in the context and within the limitations necessary for his/her protection, and he/she shall be entitled to compensation in case of any damage (whether pertaining to his/her professional duties or to his/her personal life) resulting from pointing out corrupt behaviour, provided causation is evidenced between the damage and the disclosure.
- The NACC may request additional protective measures in case there is a serious threat on the whistle-blower's (or his/her family's) safety and may grant him/her compensations and benefits depending on the importance of the information.

**2. Decision No. 1472 dated the 4<sup>th</sup> of October 2018 on the "Mechanism for the Determination of Beneficial Owners" ("Decision 1472/2018"):**

- Pursuant to Decision 1472/2018, a "**Beneficial Owner**" is any natural person who ultimately owns or effectively controls, directly or indirectly, the activities of another natural or legal person on the Lebanese territory.
- Indirect ownership or control include the cases where such ownership or control has occurred by way of sequential acquisitions or other indirect means of control.
- Every legal person must determine the identity of the Beneficial Owners in the activity by determining the natural person behind:
  - i. any natural person owning, directly or indirectly, 20% or more of its capital;
  - ii. any natural person owning the majority vote or to right to take major decisions, including the appointment and dismissal of the members of its administrative or supervisory Board;
  - iii. any person occupying a position in the company's upper administration.

- The disclosure of the information relating to the Beneficial Owner must be made upon the declaration of commencement of work and in the yearly statements made in accordance with Article 38 of the Taxation Law. Such information must include, *inter alia*, the information on the identity of the Beneficial Owner, its tax number and percentage of ownership (Article 4 of Decision 1472/2018).
- Following the request of the Tax Administration, each of the Association of Certified Public Accountants, the Beirut and Tripoli Bar Associations and the Notary Public shall promptly provide the Ministry of Finance any document directly or indirectly related to Beneficial Owners.
- The Ministry of Finance shall ensure that the Tax Administration gets hold of such information. The latter shall audit the Beneficial Owners' compliance with the relevant laws and obligations and impose fines when necessary.

**3. Law No. 44 dated the 26<sup>th</sup> of November 2015 on "Fighting Money Laundering and Terrorism Financing" ("Law 44/2015"):**

- Law 44/2015 defines unlawful funds as all types of assets, including legal documents and papers evidencing ownership generated from the perpetration or attempt to perpetrate or participation in specific acts, among which:
  - i. the misuse of privileged information, the disclosure of secrets, the hindering of auctions sales and the unlawful competition;
  - ii. the corruption including bribery, diversion of influence, embezzlement, abuse of functions, abuse of power and illicit enrichment;
  - iii. environmental crimes;
  - iv. blackmail;
  - v. tax evasion.
- Money laundering is a standalone criminal offence constituted by any act aiming to:
  - i. hide or falsely justify the real source of funds known to be unlawful funds, by any mean; and
  - ii. transfer or move, exchange or invest funds with the purpose of hiding or diverting their unlawful source.
- Any natural or legal person responsible for money laundering shall be held liable and shall be punished by imprisonment for a period of three (3) to seven (7) years and by a fine not exceeding twice the amount laundered.
- An independent commission, with a legal personality shall be established at the Central Bank (the "Special Investigation Commission", "SIC"). The SIC is competent to receive all notifications, requests for support (even from foreign jurisdictions) and investigation procedures

regarding operations suspected to constitute crimes of money laundering and terrorism financing as defined under Law 44/2015. SIC may take appropriate measures which include provisional and temporary freezing of accounts and suspicious formalities.

**4. Law No. 55 dated the 27<sup>th</sup> of October 2016 on the "Exchange of Information for Tax Purposes" ("Law 55/2016"):**

- Law 55/2016 aims to implement and enforce any international convention pertaining to the exchange of information for tax purposes and the undertaking to provide the information requested under such convention, including the automatic exchange of information between Lebanon and any foreign country.
- The relevant administration assists the foreign country requesting the information in compliance with the provisions of the convention signed between them and in accordance with the terms of Law 55/2016.
- If the requested information is not covered by Lebanese Law on Banking Secrecy or by Article 151 of the Law on Money and Credit, the relevant administration provides the information directly to the requesting country. Otherwise, the SIC shall obtain the information and transfer it to the requesting foreign country, provided compliance with the convention signed with such foreign country, and notification of the party whose information is being processed, who will be entitled to oppose such sharing of information before the State Council (Fifth paragraph of Law 55/2016).
- The Ministry of Finance and the Central Bank of Lebanon shall, each within its authority, determine the administrations that are bound to provide the requested information, the information that should be provided, its extent, the standards for preciseness and the means to provide it (Clause (2) of Sixth paragraph of Law 55/2016).
- It should be noted that the Lebanese Government was authorized by the Parliament to ratify the Multilateral Convention on Mutual Assistance in tax Matters, and the Multilateral Competent Authority Agreement on Automatic Exchange on Financial Account Information Convention (Eighth paragraph of Law 55/2016).

On a final note, let me conclude by repeating what a Nobel Prize Laureate Mrs Rigoberta Menchu, wrote 18 years ago in the 2001 Global Corruption Report:

***“Without strong watchdog institutions, impunity becomes the very foundation upon which systems of corruption are built. And if impunity is not demolished, all efforts to bring an end to corruption are in vain.”***

My hope is that we would be able to build and foster a culture of **Transparency** and **Accountability** in the Lebanese Petroleum Sector and to set high standards of

**Corporate Governance** that should be adhered to and embraced by each stakeholder in the Supply Chain.

This goal can be better achieved through the effective engagement of the civil society in the petroleum sector's policy making and the involvement of competent and independent institutions in its monitoring process.