

# NARRATIVE REPORT ON LEBANON



## PART 1: NARRATIVE REPORT

Lebanon is ranked eleventh on the 2018 Financial Secrecy Index, based on a very high secrecy score of 72, and a low scale weighting for the size of its offshore financial services sector, at 0.5 percent of the world total.

### Introduction and background

Lebanon has historically had a large offshore financial sector, catering mostly to Arab countries and to the large and successful Lebanese diaspora there and further afield. The diaspora is so extensive that its members outnumber Lebanon’s own population by a significant margin, and the IMF ([p38](#)) identifies it, alongside banking secrecy, currency convertibility and high interest rates, as a cornerstone of a banking sector that is unusually large for a country of Lebanon’s income level.<sup>1</sup>

The Lebanese diaspora is estimated at anywhere between 5 million and 16 million-strong: larger than Lebanon’s total population of around four million (plus, now, one and more than a [million Syrian refugees](#)).<sup>2</sup> Many members of the diaspora are high-net worth individuals and [include](#) such world famous names as Carlos Slim, the Lebanese-Mexican telecoms tycoon who is the world’s richest man; Carlos Ghosn, the French-Lebanese-Brazilian boss of carmakers Renault and Nissan; and Nicholas Hayek, a Swiss-Lebanese who runs Swatch, the biggest maker of Swiss watches.<sup>3</sup>

Lebanon’s political and military troubles over recent decades have certainly disrupted the offshore financial sector, though has proved astonishingly resilient in the face of these shocks. Beirut’s offshore financial services sector has been growing at an average of [nearly 12 percent per year](#) since 2006,<sup>4</sup> with banking deposits estimated at [US\\$166 billion](#) at the end of 2016.<sup>5</sup> With banking assets equivalent to around 400 percent of GDP, Lebanon is more heavily dominated by its banking sector than most other financial centres around the world.<sup>6</sup>

While other offshore financial sectors have significantly curbed financial secrecy in recent years, Lebanon has sailed against the prevailing winds on global financial transparency and continues to make secrecy a core selling point.

### History of the Lebanese tax haven

#### Offshore pre-history

The earliest roots of Lebanon’s status as an offshore financial centre date back a century or so. Between the First and Second World Wars, many Lebanese [emigrated](#) to parts of the developing world, particularly to Latin America and to Africa – and especially to French African colonies.<sup>7</sup> This diaspora soon began to develop as a classic successful trading network, initially operating as middlemen between European colonials and indigenous locals. When decolonisation happened after the Second World War, Lebanese businesspeople became increasingly influential in many of these economies, tapping the diaspora’s large and often family-dominated international trading networks and expanding into

Rank: 11

Chart 1 - How Secretive?

72  
Secrecy Score

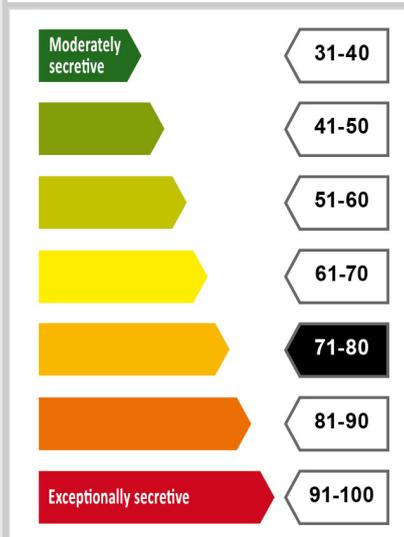
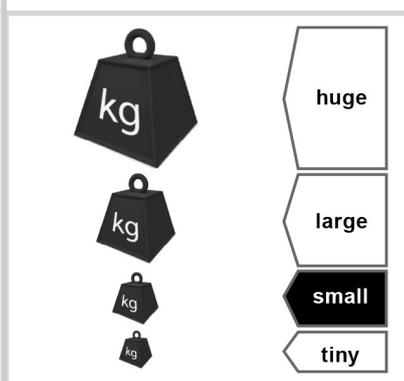


Chart 2 - How Big?



Lebanon accounts for less than 1 per cent of the global market for offshore financial services, making it a small player compared with other secrecy jurisdictions.

The ranking is based on a combination of its secrecy score and scale weighting.

Full data on Lebanon is available here: [www.financialsecrecyindex.com/database](http://www.financialsecrecyindex.com/database)

To find out more about the Financial Secrecy Index, please visit [www.financialsecrecyindex.com](http://www.financialsecrecyindex.com).

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diamond mining and other lucrative sectors. These networks remain substantially in place today and are a 'patriotic' cornerstone of Lebanon's surprisingly resilient offshore banking sector.

Lebanon itself became a trading nation of note after the creation of Israel in 1948: a change that saw Beirut supplant Israel's commercial port of Haifa as the trade capital of the Middle East.

### A trading *entrepôt* becomes a financial hub

The original architect of Lebanon's financial centre was a Palestinian Lebanese banker, Yousef Beidas, who set up the now notorious Intra Bank in 1951. The bank has been described as:

“. . . one of the Middle East's greatest financial success stories and later one of its most disastrous financial collapses.”

Beidas' influence helped cement in Beirut a factor that is common to all tax havens: as one analyst put it, Lebanon

“was committed, to an unusual degree, to a flexible, free wheeling form of *laissez faire* capitalism.”<sup>8</sup>

Two other factors combined to give the sector a kick-start. The first was Lebanon's banking secrecy law, passed in 1956 under Beidas' strong influence. The second was the Suez crisis of 1956, which according to financial historian Tom Naylor (p34) frightened many Egyptian investors and helped Beirut displace Cairo as the beachhead for European business into that region.<sup>9</sup>

From then on, Beirut increasingly sought to position itself as both a commercial and a financial *entrepôt* for the region, much as Dubai has done more recently.

By the time Beidas' Intra Bank collapsed in 1966, its influence was huge: its holding company controlled the Port Authority, Middle East Airlines, the Casino du Liban – the world's largest – the main radio station, and more besides. The bank's scale of activities and its far-reaching political clout created a Lebanese variant of the financially '[captured state](#)' that we have encountered in every secrecy jurisdiction we have analysed (for the nearest comparable example, see our [Dubai report](#)). Naylor notes of Intra Bank's demise:

“Although the bank's rise and subsequent fall could be ascribed at least partly to 'political' factors, the situation should have highlighted the dangers inherent in financial

institutions relying on hot and homeless money for funding their lending and investment.”

### OPEC brings a flood of petrodollars

The OPEC oil price hikes of the 1970s brought economic crisis to western economies, but the Arab world saw the opposite effect, with huge oil windfalls tumbling into Arab treasuries. Beirut, like Dubai, was a major beneficiary.

However, Lebanon was beset with its own political turmoil, including a vicious civil war which erupted in 1975. Yet such was the resilience of its financial sector, and of the Lebanese diaspora, that the sector continued to survive and even flourish, to many outsiders' astonishment.

In the same way that the potential for conflict was a factor in turning Switzerland into a secrecy jurisdiction, Lebanon's financial centre seems to have turned adversity into a strength, by creating structures to deal with it. In Lebanon's case the main mechanism was that banks were set up and maintained with large capital buffers. Yet this obscures a more human story, as an account in the American Political Science Review<sup>10</sup> describes it:

“The regime survived in no small measure because of the commitment, and indeed heroism, of the Lebanese central and commercial bankers and their employees, who dodged bullets, paid off rival militias, and managed to keep their doors open for all but a few months of a 10-year nightmare. [...]

Not even the law of the jungle prevailed, so dense and overgrown was its underbrush of class, regional, and international, as well as sectarian, conflicts.”

The same account cites further factors: Lebanon's large and appreciating gold reserves, the resilience of Lebanon's export economy, as well as local bankers' strong networks of mutual trust, enabling them to roll over loans indefinitely and prevent large-scale collective bankruptcies. Astonishingly, bank deposits reportedly doubled between 1975 and 1980, amid episodes of fighting in the streets.

The civil war lasted until 1991 and although there was some inevitable damage to the financial sector during this period it rebounded again quickly in the 1990s, helped not only by the fact that Lebanon never defaulted on its debts during the war, but

also by the constant flow of remittances from the powerful Lebanese diaspora which, at 21 percent of GDP in 2007, was among the highest rates in the world ([pp4-5](#)).<sup>11</sup>

Lebanon's political turmoil adds another unusual twist to the tale of its offshore centre: its strategic position in regional (and global geopolitics) means that some powerful countries such as the United States have a strong interest to avoid Lebanon becoming a financial failure, and this provides a confidence-boosting backstop for certain hardy investors. As the IMF [noted in 2008](#):

“Lebanon, at present, benefits first and foremost from a perceived implicit guarantee from donors, but also from its reputation in credit markets and a unique investor base.”<sup>12</sup>

The banking system largely shrugged off the global financial crisis of 2008 onwards, with deposit inflows continuing [to grow](#) at 20 percent annually.<sup>13</sup>

### **The Lebanese offshore centre today: backstopped by secrecy**

Official statistics suggest that non-residents account for only a small share of Lebanese deposits, but informed observers do not take this classification seriously<sup>14</sup>. The same [2008 IMF report noted](#) that:

“Banks fund their positions from deposits, which reached 267 percent of GDP in 2006, a large part of which held by non-residents. [...] The Lebanese Diaspora (most of whom have a Lebanese address) is the largest group of depositors. This Diaspora includes a significant share of high net worth individuals, many doing business in countries with underdeveloped banking systems. Depositors from other Arab countries reportedly hail mostly from Syria, West Bank and Gaza, Iraq, Jordan, Saudi Arabia, Kuwait, and UAE.”

The existence of the “offshore” diaspora as a source of banking sector profits (although deposits have slowed since 2014 – [see p8 of this IMF report](#))<sup>15</sup> is complemented, of course, by financial secrecy. Over half a century after the introduction of Lebanon's banking secrecy law, it remains a cornerstone of the financial centre. While there is some exaggeration in one offshore practitioner's [boast](#) that Lebanon's banking secrecy is “the strongest in the world,” it does offer a range of secrecy facilities, and its secrecy

score of 72 on this year's Financial Secrecy Index – largely unchanged from 2015 – places it among the worst in the world.

Lebanon has only taken limited steps to come into line with international standards on transparency: it created a new money-laundering law in 2001, the year of the major terrorist attacks on the United States; and in 2011 it imposed certain new restrictions on banks related to terrorist financing and money laundering, with a view, [according to the Banque du Liban circular announcing it](#), to mitigating “reputational risk to which banks and financial institutions might be exposed and to protecting the utmost national interest.”

The pattern appears to be that Lebanon has made some concessions when it comes to the narrow categories of terrorist financing, partly on account of its need to preserve the goodwill of the United States, and in particular because of its unstable geopolitical situation. Yet when it comes to foreign tax evasion and other less politically sensitive crimes, Lebanon appears to be offering the continuation of secrecy as a unique selling point. Indeed, François Bassil, President of the Association of Banks in Lebanon, [said in 2015](#):

“Lebanon has no intention to abandon the banking secrecy law, although Switzerland and other countries may remove this law eventually.”<sup>16</sup>

Lebanon's strong focus on financial secrecy has naturally made the country a hotbed of illicit activity. According to a [2015 report](#) by the U.S. State Department's International Narcotics Control Strategy (INCSR):

“Lebanon faces significant money laundering and terrorism financing challenges [...] media reports suggest that a number of Lebanese abroad are involved in underground finance and trade-based money laundering (TBML) activities. Laundered proceeds come primarily from foreign criminal activity and organized crime, and from Hizballah, which the United States has designated as a terrorist organization, though the Government of Lebanon does not recognize this designation. [...] Lebanese expatriates in Africa and South America have established financial systems outside the formal financial sector, and some are reportedly involved in TBML schemes. Lebanese diamond brokers and purchasing agents

are reportedly part of an international network of traders who participate in underground activities including the trafficking of conflict diamonds, diamond trade fraud (circumventing the Kimberley Process<sup>17</sup>), and TBML.”

“Exchange houses are reportedly used to facilitate money laundering and terrorism financing, including by Hizballah. Although offshore banking and trust and insurance companies are not permitted in Lebanon, the government has enacted regulations regarding the activities of offshore companies and transactions conducted outside Lebanon or in the Lebanese Customs Free Zone. Offshore companies can issue bearer shares.”<sup>18</sup>

A 2012 [report on Lebanon](#) by the OECD Global Forum pointed to a litany of serious shortcomings.<sup>19</sup> It noted:

“Lebanese authorities do not have access to information held by banks, fiduciary institutions and other institutions within the financial industry, for tax purposes. Although the Lebanese competent authority can exchange any information already in its possession, it is unclear whether it has powers to access information for exchange purposes when the information is not required for its own tax purposes.”

“Due to strict bank secrecy obligations, the Ministry [of Finance] cannot access information regarding transactions and the identity of customers of banks and other entities within the financial sector, including fiduciaries under a Lebanese fiduciary contract. Moreover, the scope of the professional secrecy safeguards appears to be broader than the professional secrecy protected under the international standard.”

“Bearer shares and to-order shares may be issued by joint stock companies and partnerships limited by shares, and adequate mechanisms to ensure that the owners of such shares can be identified are not in place. Lebanese law does not ensure that information identifying the settlors, trustees and beneficiaries of foreign trusts with a Lebanese trustee is available, in particular when the trustee is acting outside the financial industry and thus not subject to AML obligations.”

Since the last Financial Secrecy Index there have been some changes. The State Department’s [2017 INCSR report](#) notes that ‘Lebanese authorities have revoked licenses and increased regulatory requirements for exchange houses that facilitate money laundering,’ and that the anti-money laundering regulations have been widened to include notaries, lawyers and accountants.<sup>20</sup> Lebanon remains on its list of jurisdictions of primary money laundering concern, though, and the report describes the role of Lebanese financial institutions in laundering and moving criminal proceeds through West Africa and back into Lebanon.

Lebanon [joined the OECD’s Common Report Standard](#) in May 2017,<sup>21</sup> in time to begin exchanging information in 2018 and as at 21 December, 2017 forty one bilateral agreements were activated. It has not joined the BEPS Inclusive Framework whose core standards include a form of country-by-country reporting, and it has not made any moves to collect information on beneficial ownership of companies. Legal ownership information is compromised by the continued circulation of bearer shares, and in 2016 the OECD’s Global Forum noted ongoing problems with accessing information in order to exchange it [\(p34\)](#):

“Under the procedure for accessing bank information, a prior notification is made in writing to the person under investigation. There are no exceptions to this notification of the account-holder prior to exchange of information, for example for cases where the information requested is of a very urgent nature, or where prior notification is likely to undermine the chance of success of the investigation in the requesting jurisdiction.”<sup>22</sup>

In common with many other secrecy jurisdictions, Lebanon combines its secrecy offering with significant tax exemptions for non-residents, [including](#) on profits, on stamp duties on contracts, inheritance taxes, corporate income taxes, dividend distributions, capital gains, interest, and more.<sup>23</sup>

The combination of tax exemptions and secrecy offerings make Lebanon a ‘classic’ tax haven or secrecy jurisdiction, rather narrowly focused, with relatively few financial sector alternatives to fall back on if it were to row back on secrecy. This relative lack of alternatives will make reform of the sector quite hard, not least because of path dependence issues; offshore bankers do not have many skills that can be readily transferred to other, more productive, occupations.

## Endnotes

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- 5 <http://www.abl.org.lb/subPage.aspx?pageid=7337>; 27.01.2018.
- 6 As the IMF put it in July 2014 (p34): “With assets of about 400 percent of GDP, Lebanon is among the top international banking centers, after the Bahamas, Hong Kong, and the United Kingdom.” P38 of this report suggests a number of possible reasons for the size of the Lebanese banking sector relative to GDP, of which the first is bank secrecy, and the second is loyalty from the diaspora. <http://www.imf.org/external/pubs/ft/scr/2014/cr14238.pdf>; 27.01.2018.
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- 10 [Prisoners’ Financial Dilemmas: A Consociational Future for Lebanon?](#), Clement Henry Moore, American Political Science Review, Vol. 81, No. 1, March 1987.
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- 13 <http://www.imf.org/en/News/Articles/2015/09/28/04/53/socar081109a>; 27.01.2018.
- 14 As the IMF notes, The classification of resident and non-resident deposits is essentially based on whether the holder of the deposit lists a Lebanese address, which is generally not a useful metric for establishing residence, particularly given the size of the Lebanese diaspora.
- 15 <https://www.imf.org/external/pubs/ft/wp/2008/wp0817.pdf>; 27.01.2018.
- 16 <https://www.albawaba.com/business/replacing-switzerland-why-lebanon-isnt-keeping-its-banking-secret-676936>; 27.01.2018.
- 17 As the FATF notes in a 2013 report: “The Kimberly Process (KP) is a voluntary export/import control regime, supported by the United Nations, and focussed on stopping the illicit trade in rough diamonds to finance armed conflict (i.e., the use of rough diamonds as an alternate currency used mainly to by weapons). It is not an international legally enforceable agreement, and its compliance flows from the national implementation legislation in participating countries. From an AML/CFT perspective what is important to note here is that the [Kimberly Process Certification Scheme (KPCS)] does not deal with ML or with TF activities and is limited to rough diamonds only. Thus polished diamonds are not covered by the KPCS as it is assumed that all polished diamonds come from KP Certificated rough diamonds.” (p24) Further, “when a shipment of rough diamonds is accompanied by a KP certificate, this may give legitimacy to the shipment to customs officials and bank employees.” (p61)

“According to the KPCS the KPC that come with imported diamonds are kept in a country and not sent with the following export of the diamonds. The rough diamonds that leave the country for export receive a new certificate issued by the responsible authority in the exporting country. This legitimate procedure may be exploited by criminals and is one of the major vulnerabilities of the KPCS whereby the actual origin of the rough diamonds is often concealed and practically impossible to retrieve by moving the rough diamonds through trade centres for the purpose of issuing a new KPC.” (p57)

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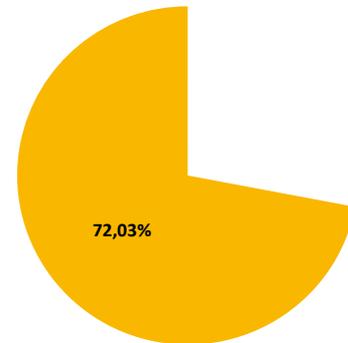
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## PART 2: LEBANON'S SECRECY SCORE



### Lebanon - Secrecy Score



### Lebanon KFSI-Assessment Secrecy Scores



### Notes and Sources

The ranking is based on a combination of its secrecy score and scale weighting (click [here](#) to see our full methodology).

The secrecy score of 72 per cent has been computed as the average score of 20 Key Financial Secrecy Indicators (KFSI), listed on the left. Each KFSI is explained in more detail by clicking on the name of the indicators.

A grey tick indicates full compliance with the relevant indicator, meaning least secrecy; red indicates non-compliance (most secrecy); colours in between partial compliance.

This paper draws on data sources including regulatory reports, legislation, regulation and news available as of 30.09.2017.

Full data on Lebanon is available here: [www.financialsecrecyindex.com/database](http://www.financialsecrecyindex.com/database).

To find out more about the Financial Secrecy Index, please visit [www.financialsecrecyindex.com](http://www.financialsecrecyindex.com).