

ROLE OF THE AUDIT COMMITTEES IN THE GOVERNANCE FRAMEWORK

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5 May 2015

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Agenda

- Audit Committee – definition and role
- BDL circular 118
- The role of the Audit Committee within foreign subsidiaries
- The role of the secretary to the Audit Committee
- The audit universe
- Competences and professionalism of the members of the committee
- The Compliance Unit
- Joint area with the Risk and Remuneration Committees

Audit Committee – definition and role

- The purpose of the Audit Committee is to **assist the Board** in its oversight of :
 - the fairness of the Bank’s financial statements and other relevant public disclosures;
 - the Bank’s compliance with legal and regulatory requirements relating to financial reporting;
 - the external auditors’ independence and qualifications;
 - the design and implementation of sufficient and effective P&P for internal control;
 - the independence and the performance of the internal audit function.
- A balance between strong communication and trust with the Internal Audit Unit and robust oversight is at the heart of the role of the Audit Committee.
- The Committee is responsible to report its activities or any other duty as assigned by the Board of Directors as stipulated in the Committee’s Charter.
- Audit Committee's functions are not intended to duplicate or substitute for the duties of the Board of Directors.

BDL circulars 118 -133

- Banque du Liban (“BDL”) issued circulars 118 & 133 to put forth the conditions of the establishment of Audit, Risk and Remuneration Committees within financial institutions in Lebanon.
- There are roughly 70 banks in Lebanon.
- For each financial institution, provisions of the circulars highlighted the need for :
 - 3 independent Board members, (Chairman of the committees);
 - Only One Board member can be simultaneously member of the Audit Committee and the Risk Committee (cross membership)
 - 4 to 5 non executive members(NE) or executive (E) (NE for Audit and Remuneration and E or NE for the Risk Committee)
- → In total, the population needed for the Audit, Risk and Compensation committees would be around 600 directors who should be skilled, knowledgeable with practical banking (operations) or financial experience. Lebanese banks can maybe elect / appoint international bankers as board or committees members to fill partially gaps and take advantages from their previous experiences.

How to train these members and what are the tools that the institutions should provide them to fulfill their positions ?

The Role of the Audit Committee (AC) within foreign units (2/2)

- One major question relating to the consolidated financial statements can be raised regarding the confirmation of the review by the subsidiary audit committee of the consolidated financial statements before the parent Audit Committee.
 - What about different standards applied in foreign entities ? The EA should give the assurance regarding a proper mapping of the local standards to IFRS?
- This interrelation between the parent bank and its subsidiaries is essential for the Audit Committee and the Board to approve the consolidated financial statements.

The Role of the Audit Committee (AC) within foreign units (1/2)

- Article 5 of BDL circular 118 states that the Audit Committee scope of work covers the bank in Lebanon and in its foreign units.

“The scope of the Audit Committee’s work shall cover the bank in Lebanon and all its branches and affiliates in Lebanon and abroad.”

- To what extent a Lebanese Audit Committee can request information from a bank incorporated in Switzerland ? What about banking secrecy law ?
- How clear communication channels between the Audit Committee of the parent bank and its subsidiaries should be established in order to allow the parent Audit Committee to properly fulfill its role ?

The Role of a Board Member Secretary of the Audit Committee

- Is there a role to be agreed upon for Board Member to act as a secretary of the audit committee ?
- Circular 118 does not assign any specific function to this role.
- The role of the secretary would consist in :
 - securing structured communication channels between the Committee and the Management;
 - following of the implementation of remedial measures proposed in the reports of the Unit, the control authorities and the external auditors,
 - preparing the agendas of the AC meetings with the Head of Internal unit before submitting it to the Chairman of the AC ;
 - delivering of supporting documents; and
 - summoning of meetings.

The audit universe

- The audit universe is broad and diversified and it requires practical banking (operations) and financial experience. The AC members qualifications and profiles should cover among others:
 - Laws (Banking Secrecy law, CMC, AML/CTC, Decree 1983, Decree 50)
 - BDL/ BCC Circulars and Memos : Corporate Governance (106), Internal Audit (77, B271), External Auditors (118), Compliance (128,83), Capital management and Solvency (119, B277, BM 5/2014), Credit (48, 58 , B276) , Investments and participations(23 ,81) , Risk Management (B242, B262) Electronic banking (69, 63)....
- I will not enumerate and categorize the 133 Basic circulars or the 281 BCC memos : the objective is to highlight the complexity and the diversity of the Audit Universe and the qualifications required for the AC members.

Awareness sessions and Seminars

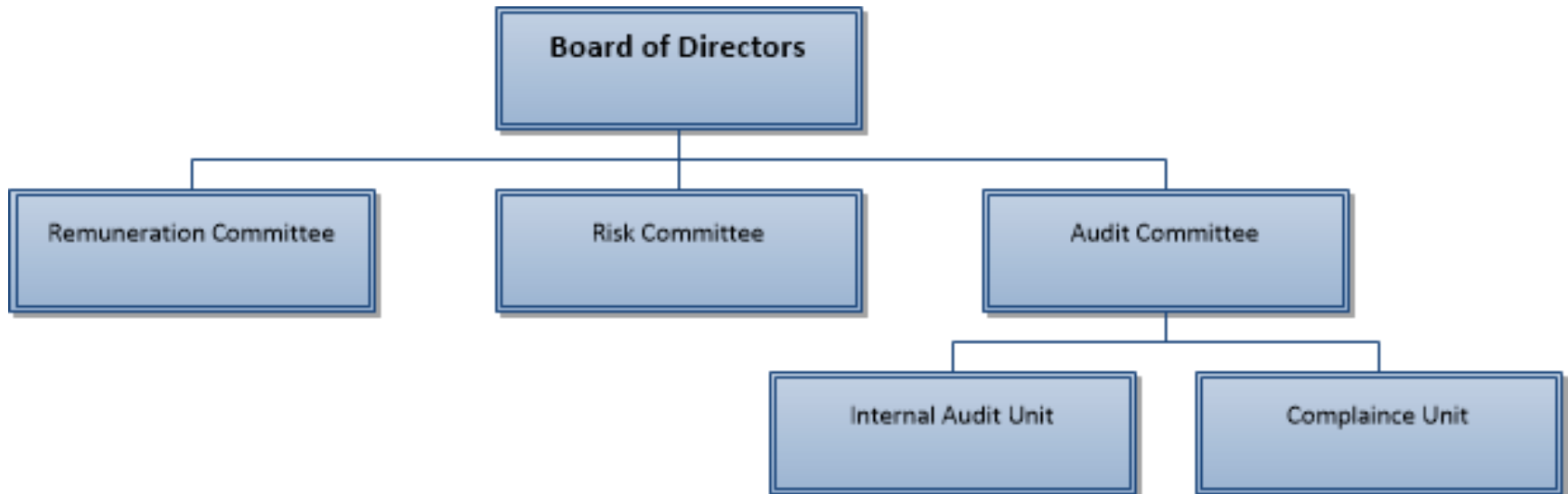
- I would like to highlight the importance of continuous education programs to Board and Board committees members to bring them up to speed on rapid changes in regulation in general and banking in specific: ABL is currently planning a three days seminar for that purpose.
- Seminars' topics should not be broad. Need for focused topics.
- Suggestion: BDL and ABL to prepare an online manual summarizing by topic the relevant circulars and decrees. Update this manual periodically based on the new requirements and regulations issued by BDL and BCC.

The compliance unit (1/2)

- BDL Basic Decision No 11323 was issued on 12 January 2013 relating to the establishment of a Compliance Department.
- Some banks decided to entrust to the audit committee to oversee the compliance function while maintaining a Chinese wall between the Audit and Compliance departments.
- This choice was triggered by the willingness of the banks to facilitate the supervisory role of the Board of Directors even if the circular was not explicit about this matter (“only reports to the Board BDL circulars 128 and 83”).
- This option is important due to the sensitivity of AML and CFT issues in particular avoiding any breach of an embargo or a sanctions set by the US Treasury, OFAC, EU, UN or non compliance with FATCA requirements.

The Compliance Unit (2/2)

Organization Chart of the Committees



Joint areas with the Risk and Remuneration Committees

- Common areas exist between the committees however, issues/ topics are treated differently. Each committee has a focused scope :

Topics	Risk Committee	Remuneration Committee	Audit Committee
ICAP	Discuss in details the assumption, results and makes recommendation to the Board		Review the procedure but do not discuss the content.
Remuneration	The Remuneration Committee shall coordinate closely with the Risk Management Committee, upon assessing the remunerations and their related risks and upon reviewing the Remuneration Policy, in order to ensure its efficiency and adequacy to "effective performance".		

- In order to facilitate the coordination between the different committees, it is recommended to have one common member (cross membership) at least between the Remuneration, the Risk and the Audit committee .