

**BANQUE DU LIBAN**

**Intermediate Circular No 254  
Addressed to Banks and Financial Institutions**

Attached is a copy of Intermediate Decision No 10707 of April 21, 2011 amending Basic Decision No 7737 of December 15, 2000 (Internal Control in Banks) attached to Basic Circular No 77.

Beirut, April 21, 2011

The Governor of Banque du Liban

Riad Toufic Salamé

**BANQUE DU LIBAN****Intermediate Decision No 10707****Amending Basic Decision No 7737 of December 15, 2000**

**The Governor of Banque du Liban,**

**Pursuant to the Code of Money and Credit, particularly Articles 70 and 174 thereof,**

**Pursuant to Basic Decision No 7737 of December 15, 2000 and its amendments, relating to Internal Control in Banks, and**

**Pursuant to the Decision of the Central Council of Banque du Liban (BDL) taken in its meeting of April 13, 2011,**

**Decides the following:****Article 1:**

The title of Basic Decision No 7737 of December 15, 2000 is amended and shall become: “ Internal Control and Internal Audit in Banks and Financial Institutions”.

**Article 2:**

The numbering of Articles 8, 9 and 10 of Basic Decision No 7737 of December 15, 2000 is modified to become Articles 16, 17 and 18, respectively.

**Article 3**

Articles 1, 2, 3, 4, 5, 6 and 7 of Basic Decision No 7737 of December 15, 2000 are repealed and replaced as follows:

“Article 1: The following expressions shall mean:

- 1- Internal Control: the set of regulations, policies and procedures established in order to control the risks that the bank or financial institution faces or may face and therefore to protect their assets.
- 2- Internal Audit: an independent and objective assessment process of the work and activities carried out by the bank or financial institution’s departments and units, in order to enhance the effectiveness and efficiency of internal control and risk management.

Article 2:

The provisions of this Decision shall apply to:

- 1- All the departments, units, operations and activities of banks and financial institutions, including outsourced activities and operations.
- 2- All the branches and affiliates of banks and financial institutions in Lebanon and abroad, provided the provisions of Basic Decision No 9671 of August 16, 2007 on the relation between Lebanese banks and financial institutions and their affiliates abroad are respected.

**First: Internal Control**

Article 3:

The Senior Management must establish an internal control framework which is commensurate with the size of the bank or financial institution and the nature of the risks that any of them faces or may face; it must also update this framework when needed. This framework must be based, at least, on the following components:

- 1- Internal environment: to rely on a clear and documented organizational structure that respects the separation of duties and the non-conflict of interest; to adopt a human resources policy based on the principles of merit and qualification; and to disseminate a control culture among the bank or financial institution's staff.
- 2- Risks: to determine the risks that the bank or financial institution faces or may face and to classify these risks according to the possibility of controlling them and addressing them properly.
- 3- Internal control policies and procedures: to prepare documented internal control policies and procedures, based on the results of the risk determination and assessment process, provided these policies and procedures form an integral part of the mechanism adopted for executing any of the bank or financial institution's operation or activity.
- 4- Complementary systems: to ensure the systems required for implementing internal control, the most important being:
  - a- an accounting system that respects the laws and regulations in force and the IFRS
  - b- a system for risk assessment and follow-up
  - c- an archive system
  - d- a management information system
- 5- Continuous monitoring: to ensure a continuous monitoring in order to ascertain the implementation of policies and procedures and the systems' soundness and to address the reported deficiencies.

**Second: Internal Audit**

Article 4:

All banks and financial institutions must establish an internal audit unit (hereafter "the Unit") that meets the following conditions:

- 1- It must be entirely independent from the body entrusted with the bank's operations, have no executive responsibilities within the bank or financial institution, and be objective when fulfilling its duties
- 2- It must be granted full powers when carrying out audit operations

- 3- Its staff must be qualitatively and quantitatively commensurate with the bank or financial institution's size, the diversification of their activities and the nature of risks that any of them faces or may face.

Lebanese banks and financial institutions affiliated to other Lebanese banks may be authorized to have an internal audit Unit jointly with the parent company. This authorization is granted at BDL Central Council's discretion and based on the Banking Control Commission's opinion.

Article 5:

Banks and financial institutions are prohibited from outsourcing the internal audit in whole or in part to any external specialized firm.

Banks or financial institutions whose status is inconsistent with the provisions of this Article are granted a time limit ending on December 31, 2011 to regularize their situation accordingly.

Article 6:

The Board of Directors shall appoint the Unit Head and determine his/her compensation.

Each bank or financial institution must communicate the name of the incumbent Unit Head and his/her curriculum vitae to the Banking Control Commission, as well as any subsequent change with its motives.

Article 7:

The primary duties of the Unit shall be, for indicative purposes but not restrictively:

- 1- To assess the effectiveness of internal control
- 2- To review the effectiveness of risk assessment, management and reduction methods
- 3- To review the accuracy of accounting entries and financial statements and reports, including those required by Banque du Liban and the Banking Control Commission
- 4- To verify compliance with laws in force and regulations issued by Banque du Liban and the Banking Control Commission, in the absence of an independent Legal Compliance Unit in charge of this verification. However, if the latter exists, then the Unit shall be in charge of verifying the effectiveness of the mechanism and procedures adopted by the independent Legal Compliance Unit to control compliance with laws and regulations
- 5- To review the efficiency and effectiveness of the work performed by the Compliance Unit established pursuant to the provisions of Basic Decision No 7818 of May 18, 2001, regarding the procedures for fighting money laundering and terrorism financing.
- 6- To assess the efficiency of the Corporate Governance systems and their complementary policies and procedures; to ascertain, at all the bank's levels,

compliance therewith by all the services, units and branches; to prioritize their implementation when the bank expands abroad and when the bank undertakes acquisition and merger operations.

Article 8:

The Unit must comply with the following:

- 1- To prepare its own Internal Audit Charter that guarantees its autonomy and determines its full audit powers.
- 2- To submit the operations and activities of the bank or financial institution to a comprehensive audit within a specified time limit or Audit Cycle, provided this cycle does not exceed a two-year period.
- 3- To execute the audit tasks based on an Annual Audit Plan established after a thorough study of the risks that the bank or the financial institution faces or may face.

Article 9:

The Unit Head must submit a quarterly report to the Audit Committee concerning the audit, assessment and follow-up tasks performed by the Unit during the previous quarter, and he/she must also promptly communicate to the Audit Committee any important remarks.

Article 10:

The bank or financial institution shall put all the reports prepared by the Unit, as soon as they are requested, at the Banking Control Commission and the external auditors' disposal.

**Third: Miscellaneous Provisions**

Article 11:

The Board of Directors shall approve the policies of the bank or financial institution and shall be particularly in charge of the following tasks:

- To supervise and follow-up accurately the Senior Management's work, in order to ascertain that it fulfills its duties by ensuring an effective and proper internal control.
- To guarantee the constant effectiveness of internal audit.

The Audit Committee specified in Basic Decision No 9956 of July 21, 2008 shall assist the Board of Directors in its supervisory and controlling role regarding internal control and internal audit, provided the Audit Committee complies with the regulatory texts issued by Banque du Liban and the Banking Control Commission.

Article 12:

Foreign banks' branches operating in Lebanon must communicate to the Banking Control Commission the name of the supervisory body in charge of fulfilling the internal control and internal audit duties of the Board of Directors and the Audit Committee, as specified in this Decision and in all other regulatory texts issued by Banque du Liban and the Banking Control Commission.

Article 13:

In case a financial institution has no Audit Committee, then the Board of Directors shall fulfill the internal control and internal audit duties of this Committee, as specified in this

Decision and in all other regulatory texts issued by Banque du Liban and the Banking Control Commission.

Article 14:

External auditors must prepare an annual report regarding compliance by banks or financial institutions with the provisions of this Decision.

Article 15:

The Banking Control Commission shall issue, when needed, implementation regulations for this Decision.”

**Article 4**

This Decision shall enter into force upon its issuance.

**Article 5:**

This Decision shall be published in the Official Gazette.

Beirut, April 21, 2011

The Governor of Banque du Liban

Riad Toufic Salamé