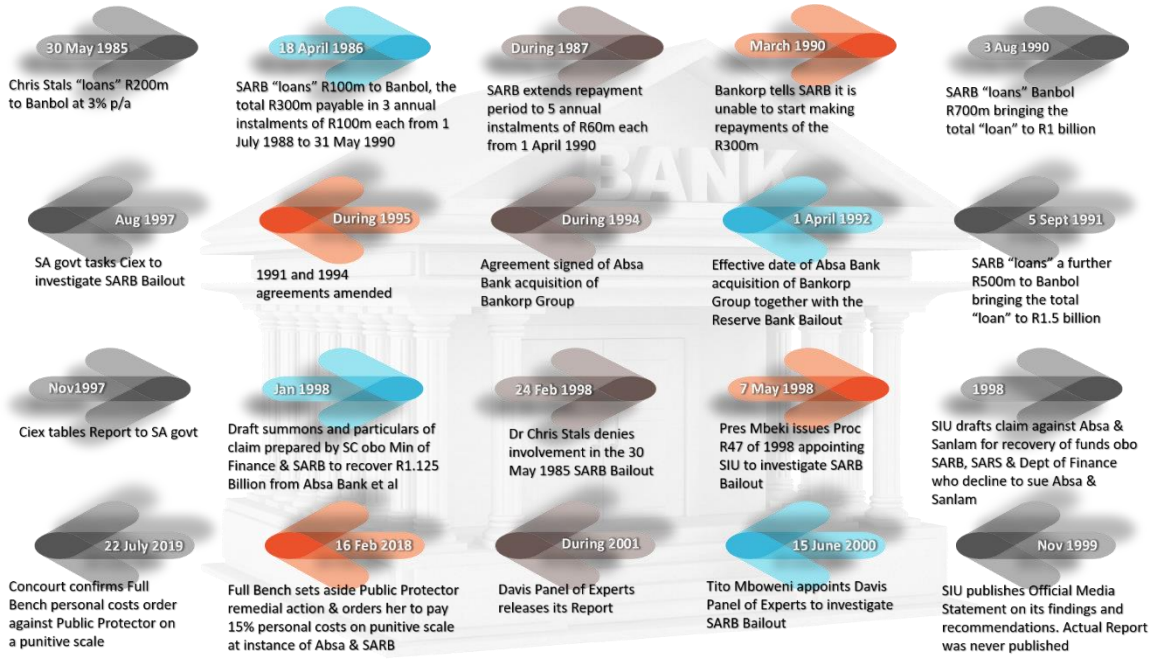
OPINION PIECE

# The Unfinished Story:
# The SA Reserve Bank Bailout of Bankorp Group and Absa Bank
# PART 1

## How it unfolded - The Timeline




## CAVEAT

The sources of much of the information contained in this paper are, except where the context indicates otherwise,

- the 2002 Report of the Davis Panel of Experts that was appointed by then governor of the SA Reserve Bank, Mr Tito Mboweni, on 15 June 2000 to investigate the Reserve Bank bailout of numerous banks, including Absa Bank, between 1985 and 1995
- a book titled *Dangerous Deceits: Julian Askin and the Tollgate Scandal* (1999), by Frank Welsh
- pleadings in various court cases involving an aspect of the Reserve Bank bailout that is the subject of this paper
- court judgments involving an aspect of this Reserve Bank bailout

For ease of digestion, I shall present the paper in two parts. This is Part 1 which deals with the background to the bailout and describes the terms of each transaction. Part 2, which will be published in due course, explores the findings and recommendations of the two investigations that were officially undertaken to probe the bailout. These are the investigation by the Special Investigating Unit led by Judge Willem Heath, on the one hand, and the Davis Panel of Experts led by Judge Dennis Davis, on the other.

Judge Willem Heath's investigation was established by President Thabo Mbeki on 7 May 1998 by Proclamation R47 of 1998, while Judge Dennis Davis' investigation was established by the governor of the SA Reserve Bank, Tito Mboweni, on 15 June 2000 following Judge Willem Heath's findings in relation to the same probe. Judge Willem Heath's Report has never been released, while the Davis Panel Report came out in 2002.

Part 2 will also touch on the findings and recommendations of the Public Protector on the same bailout, which she undertook in terms of the South African Constitution, read together with the Public Protector Act, and on which she released a Report on 19 June 2017.

## INTRODUCTION

In the week preceding the 2021 edition of Freedom Day in South Africa, a former freedom fighter and political prisoner, who later served as Premier of the richest province in South Africa, then in cabinet, and later became one of the first generation post-1994 black multi-millionaires, dropped what many consider a bombshell about theft of obscene amounts of money inside the SA Reserve Bank.

Reaction was swift, ranging from incredulity to scepticism to outright dismissal of the whole incident as a function of him having fallen victim to a financial scam. Even when he gave a media briefing of more than two hours' duration on his allegations, the South African media remained largely dismissive and, at best, sceptical.

But to South Africans who remember some of the dalliances that the South African Central Bank has had with alleged criminality in the past, Mr Tokyo Sexwale's allegations may not be altogether that far-fetched. His allegations triggered in me a memory of one of those Reserve Bank dalliances with alleged criminality: the unfinished story of the unlawful bailout by the Reserve Bank to banks that, on the evidence and on the findings of two Judge-led investigations, did not qualify for such bailout between 1985 and 1995. So, to dismiss Mr Sexwale's allegations without a probe would be a grave mistake and a disservice to the South African public.

Let me take you down Memory Lane.

## BACKGROUND TO THE SA RESERVE BANK BAILOUT CONTROVERSY

### Bankorp beginnings

The Bankorp Group began life as Central Acceptances Limited in 1968, with Senbank as a subsidiary. Over the next 10 years the Group grew rapidly, acquiring the Bank of Johannesburg, Federale Bank, Mercabank, Santam Bank, Sasbank and Trust Bank. Many of these banks had experienced operating difficulties. Trust Bank, the largest acquisition, had an aggressive lending policy, the effects of which had forced it to apply for and receive assistance from the SA Reserve Bank.

By 1986, Central Acceptances, by then the Bankorp Group, had become the third largest banking group in South Africa through organic growth. By that year the Group's subsidiaries included:

- Trust Bank, a commercial bank
- Santambank, a general bank
- Senbank, a merchant bank
- Mercabank, an investment and merchant bank

In addition, Bankorp held a 50% shareholding in Banbol (Pty) Ltd which it used since 1985 to channel the assistance package from the SA Reserve Bank. Banbol was owned jointly by Bankorp and Boland Bank Limited. Because both parties held a 50% shareholding in Banbol, it was not necessary to consolidate the financial statements of Banbol into the accounts of either one of the shareholders in terms of the prevailing accounting practice at the time. Therefore, routing the Reserve Bank's assistance package to Bankorp through Banbol contributed to the secrecy of the assistance package.

### Bankorp growth strategy

In the 1980s the Bankorp Group continued to expand rapidly. The mode of expansion changed from growth by acquisition to growth by aggressive lending. According to the Davis Panel, this drive for asset growth resulted in decline in the Group's asset quality and its eventual financial distress leading to the need for provision of assistance by the SA Reserve Bank. But, as we shall see, according to one former managing director, the SARB assistance was occasioned by something other than genuine financial distress.

Despite receiving Reserve Bank assistance, Bankorp grew its assets (excluding

contingencies and repurchase agreements) in real terms by 7.41% per year between 1985 and 1990. In this regard there appears to have been no monitoring of Bankorp management's conduct of the business by the SA Reserve Bank in terms of internationally accepted best practice of Central Banks in dealing with distressed banks.

The strategy of superior returns did not materialise and in its 30 June 1990 Annual Report, Bankorp reported a loss of R368.4 million, compared with a profit of R131.6 million the previous financial year. Again, it would seem that the SA Reserve Bank was not paying attention as required by internationally accepted best practice of Central Banks in dealing with distressed banks. Instead, it increased its financial assistance to Bankorp substantially.

By 1991 Bankorp was the smallest of the five major banking groups, but still substantially larger than the sixth largest banking group at the time (NBS Bank), which had assets amounting to R8.171 billion as at 31 December 1991.

**Concerns about Bankorp asset growth**

During the latter part of the 1980s the SA Reserve Bank voiced concern about the growth in credit extension by banks. Banks were urged to practise restraint in their financing of consumer goods and the provision of mortgage financing for luxury homes in particular.

The SA Reserve Bank addressed letters to Bankorp on at least two occasions in the late 1980s, expressing concern about the rapid growth in its asset book. On 6 July 1989 the SA Reserve Bank Governor (at that time Dr Gerhard de Kock) wrote to the Chief Executive of Bankorp (Dr CJ van Wyk), conveying the SA Reserve Bank's displeasure on the excessive rate of increase in credit extension by Bankorp in recent months. This letter also mentioned that banks had been requested at meetings held on 9 March 1989 and 5 May 1989 to exercise restraint in their rates of credit extension.

Bankorp was the only one of the five major banking groups at the time that did not adhere to the SA Reserve Bank's request for restraint. It was, therefore, requested in the letter to take immediate steps to curb credit extension. The letter concluded by saying that the co-operation of Bankorp is expected in the matter, particularly in view of the special assistance of the SA Reserve Bank to the Bankorp Group, without the Reserve Bank penalising the Group for its excessive credit extension.

After the appointment of a new Chairperson at Bankorp (Mr Derek Keys), the then Senior Deputy Governor of the Reserve Bank (Dr A S Jacobs) expressed concern about the management of the banks within the Group, including contraventions of exchange control regulations by Trust Bank. He noted the bank's aggressive credit growth; the questionable quality of its credit; the expansion of its balance sheet; and its **inability to comply with the requirements of the Banks Act since March 1989**.

That was on 13 November 1989. Within three years, and during the period of Absa Bank's acquisition of the Bankorp Group with its Reserve Bank assistance in place, Mr Derek Keys (formerly the Chairman of the Bankorp Group) was to become Minister of Finance from 1992 to late 1994.

What was the thinking behind that appointment at that time? Why did President Mandela retain Mr Keys after the 1994 elections in that cabinet portfolio only until September 1994?

I pause here to point out that the inability of a bank to comply with the requirements of the Banks Act is a disqualifying factor as regards registration and continued operation as a bank. That a Central Bank donated hundreds of millions more of public funds (as the SA Reserve Bank was to do in 1990 and 1991) to a private banking group that, by the Reserve Bank's own admission, should not even be

registered as a bank points, at the very least, to the Reserve Bank directors' abdication of their fiduciary duties.

**Bankorp financial difficulties and management response**

Bankorp's strategy of asset growth coincided with a period of restrictive monetary policy from 1987, with concomitant rising interest rates and, for the first time in a number of years, sustained positive real interest rates. In addition, the domestic economy suffered a severe recession during the period 1990 to 1992 (three years of negative economic growth).

Borrowers of funds were not accustomed to paying a **real** price for funds and a number of households and businesses ran into financial difficulty and were unable to repay lenders. The Bankorp Group was especially negatively affected by the financial difficulties experienced by its customers because of its aggressive lending strategy. As a result of its strategy of asset growth, the Group inevitably ended up with assets of a more dubious nature and suffered financial setbacks as its customers defaulted on commitments. By 1990 Bankorp told the SA Reserve Bank that only about 52% of its assets were profitable.

By that year the Bankorp Group reported that its strategy had been refocused from asset growth to one of containing such growth in favour of improving asset quality. By 30 June 1991 the Group's total assets, including assets relating to contingencies and reserves, had decreased by 8.5% to R31.841 billion.

Well, that seems to be the Bankorp version as narrated by the Davis Panel of Experts in its Report. But according to a former managing director of Trust Bank, Bankorp overstated its bad and doubtful debts at least five-fold. This, according to Frank Welsh, is what the former managing director told Judge Willem Heath's Special Investigating Unit:

**"When the 1990 lifeboat was being negotiated with the Reserve Bank every relevant person in Trust Bank had been asked to list their bad and doubtful debts. After they had done this they were asked to make the list much larger by Piet Liebenberg and Hennie van der Merwe, so that they 'could clean up the loan book'. In other words make over-estimates so that the bank could liquidate many clients who were not otherwise either candidates for liquidation or even particularly uncreditworthy. Liebenberg said, 'We're going to clean up our book.' The result was that the list submitted to the SARB was a multiple of *five times* that submitted by all the bank and credit managers throughout the group! This meant that the Bank went after clients who would never in normal circumstances have ever been pressed."**

If this evidence is true, it would seem to point to a fraudulent procurement of the Reserve Bank assistance by the Bankorp Group, and that fraudulent procurement permeates the entire duration of the bailout, including the benefits of it acquired by Absa Bank when it bought the Group with effect from 1 April 1992 subject to the assistance remaining in place. As far as I am aware, there is no statute of limitations, or prescription, for the recovery of public funds procured by fraudulent means from those who benefited from the fraud. And, again if the evidence is true, have the perpetrators identified in the evidence been criminally prosecuted? If not, why not? And who else knew about this alleged ruse and did nothing about it? What has the Reserve Bank done about such persons?

**THE BAILOUT TO BANKORP AND ABSA BANK**

Since 1985 there had been a number of transactions and agreements relating to bailouts from the Reserve Bank to Bankorp and, subsequently, to Absa Bank which acquired the Bankorp Group with effect from 1 April 1992 (although the agreement was signed in 1994). These the Davis Panel of

Experts classified into three sequential bailout packages, referred to below as **Package A** (1985 to 1990), **Package B** (1990 to 1992) and **Package C** (1992 to 1995).

I should disclose that I have not seen any of these agreements. It is doubtful that they are publicly available for scrutiny. For that reason, I cannot verify the accuracy of what is recorded in the Davis Panel Report, both in relation to dates and the contents of the agreements. I therefore assume that the **facts** recorded in the Davis Panel Report are correct because I have no independent means of verifying them. Having said that, I have no reason to believe that a Panel of Experts, led by a High Court Judge, would deliberately misrepresent the contents of agreements involving the Central Bank in what is arguably one of the starkest manifestations of commercial criminality in South Africa. In any event, some of these facts are corroborated in books that I have read over the years, including *Dangerous Deceits: Julian Askin and the Tollgate Scandal* (1999) by Frank Welsh.

The Davis Panel of Experts comprised the following persons:

- The Hon Mr Justice DM Davis, Judge of the High Court of South Africa (Cape of Good Hope Provincial Division) as Chairperson
- Prof L Harris, Director: Centre for Financial and Management Studies at SOAS, University of London
- Mr PC Hayward, Financial Sector Advisor at the Monetary and Exchange Affairs Department, International Monetary Fund, who served on the Panel in a private capacity
- Mr RM Kgosana, Chairperson of KMMT Inc Chartered Accountants
- Mr RK Store, Chairperson of Deloitte and Touche Chartered Accountants
- Ms S Zilwa, Chairperson of Nkonki Sizwe Ntsaluba Chartered Accountants.

Let us now consider each of the bailout packages in turn.

**Bailout Package A**

In April 1985 Bankorp approached the SA Reserve Bank with a request to provide the bank with financial assistance of R300 million in order to assist it in difficulties it said it encountered pursuant to certain bad investments and other non-performing assets that it had acquired with the takeover of Trust Bank in 1977 and Mercabank in 1984.

The first set of agreements started when the Reserve Bank, in a letter dated **30 May 1985** and, on the face of it, signed by Dr Chris Stals, granted assistance to Banbol of R200 million at an interest rate of 3% per year to assist Bankorp. Repayment of the assistance had to commence as quickly as possible and be completed before 31 May 1990. A further condition was that Sanlam (at the time the ultimate majority shareholder in Bankorp) had to cede government bonds to the SA Reserve Bank as security for the assistance.

It appears – from **draft** Particulars of Claim prepared in January 1998 by Adv E Bertelsmann SC of the Pretoria Bar on behalf of the Minister of Finance (as first plaintiff) and the SA Reserve Bank (as second plaintiff) against Absa Bank – that this was an oral agreement. The letter of 30 May 1985 may have served only to convey the granting of the financial assistance. A copy of that letter is reproduced as *"Appendix D"* in Frank Welsh's book, *Dangerous Deceits: Julian Askin and the Tollgate Scandal* (1999), at page 361.

Yet, by 24 February 1998 Dr Stals was to claim that he was **"not involved in the initial decisions in April 1985 or in 1986, when the original decision was taken to provide assistance to the Bankorp Group"**.

Question: Why did Dr Stals deny his involvement in the April 1985 assistance to the Bankorp Group in the face of the existence of documentary evidence to the contrary? If his denial is to be believed, who would have wanted to frame him by forging his signature, and why? Dr Gerhard de Kock was governor of

the SA Reserve Bank in April 1985. Why not frame him?

The second agreement within the **Bailout Package A** came on **18 April 1986** when the SA Reserve Bank agreed to increase its assistance package to Banbol by a further R100 million to give further assistance to Bankorp. This financial assistance was structured broadly on the same terms and conditions as the assistance granted in May 1985. It was agreed that the total sum of R300 million (that is, the May 1985 advance of R200 million and the April 1986 advance of R100 million) would be repaid in three equal instalments of R100 million each per year, payable from 1 July 1988 until the full amount of the assistance had been repaid on or before 31 May 1990. So, effectively, the repayment terms of the May 1985 advance were amended by those of the April 1986 advance.

But the repayments did not happen as agreed. Instead, during 1987, the Bankorp Group introduced a major rationalisation programme. In order to lend support to the programme, the SA Reserve Bank agreed to amend the terms and conditions for the financial assistance by extending the repayment period from three years to five, and the commencement date for repayment from 1 July 1988 to 1 April 1990. The instalments then reduced from R100 million to R60 million per year, payable over five years commencing on 1 April 1990. The other terms and conditions remained unchanged. It is not clear whether the interest that accrued to the SA Reserve Bank for the 21- month extension was factored into the new repayment arrangement.

So, since the first financial assistance of R200 million in May 1985, and the second assistance of R100 million in addition thereto in April 1986, Bankorp had failed to make any repayment of the funds to the SA Reserve Bank by 1987. Instead, the date by which the total R300 million should have been repaid (31 May 1990) was virtually turned into the date for payment of the first instalment (1 April 1990).

But that did not happen either. According to the Davis Panel Report, in March 1990 Bankorp informed the SA Reserve Bank that Bankorp was not in a financial position to commence repayments. I pause here to point out that in South African law, this constitutes (and constituted at that time) an act of insolvency in terms of s 8(g) of the Insolvency Act, 1936. It is (and was) a serious breach of fiduciary duties by directors and officers of Bankorp, on the one hand, and the directors and officers of the SA Reserve Bank, on the other, to allow Bankorp to continue trading when it was insolvent. Instead, the SA Reserve Bank increased the financial assistance by another R700 million in August 1990, and by yet another additional R500 million in September 1991, bringing the total assistance to Bankorp to R1.5 billion. I discuss these two additional assistance payments as **Bailout Package B** below.

Instead of advancing additional assistance of R1.2 billion to a banking group that was by its own admission insolvent, the SA Reserve Bank should have triggered the winding-up provisions in s 346(1)(b) of the old Companies Act, 1973 by invoking s 344(f) and s 417, s 424 to s 426 of that Act. In fact, in a letter dated 6 July 1998, the then Registrar of Banks told the Manager: Investigations at the Special Investigating Unit (Mr SJ Barkhuizen) that:

> **"the SARB decided to limit its financial assistance to banks to liquidity assistance against the collateral of securities that would qualify as collateral for loans granted through the discount window. When appropriate collateral for liquidity assistance is not available and whenever the SARB has reason to suspect that a bank is insolvent, it is the SARB's policy to place the bank under curatorship.**
> **Financial assistance beyond secured liquidity assistance will be considered only whenever a decision to assist a bank is taken by the Government. Such assistance, subject to the provisions of the Reserve Bank Act, will be provided**

**on terms to be decided jointly by the Government and the SARB."**

Question: if it was the SA Reserve Bank's **policy** to place a bank under curatorship whenever the Reserve Bank had **"reason to suspect"** that a bank is insolvent, why did it not place the Bankorp Group under curatorship in 1990? After all, the Bankorp Group itself told the Reserve Bank that it was unable to make repayments, an act of insolvency. What is more, the Senior Deputy Governor of the Reserve Bank (Dr A S Jacobs) had on 13 November 1989 written to Bankorp's Chairman (Derek Keys) expressing concern about the Group's inability to comply with the requirements of the Banks Act since March 1989. Why, then, did the Reserve Bank pump more public money (R1.2 billion more) into a bank that did not meet the requirements for remaining registered as a bank?

There is more. Was the financial assistance by the SA Reserve Bank to Bankorp after March 1990 (when Bankorp told the Reserve Bank that it was unable to make repayments of the R300 million advance) a decision taken by the Government at a time when Bankorp was insolvent? On what liquidity bases did Absa Bank need Reserve Bank assistance in 1992? As discussed later, neither the Davis Panel of Experts nor the statutory Special Investigating Unit led by Judge Willem Heath, found any basis for this assistance. And was it mere coincidence that the Chairman of Bankorp (Derek Keys) was appointed Minister of Finance in 1992 and by President Nelson Mandela in 1994?

## Bailout Package B

As intimated above, despite Bankorp informing the SA Reserve Bank in March 1990 that it was insolvent, and the Reserve Bank itself expressing concern in November 1989 to the Group's inability to comply with the requirements of remaining registered as a bank, the SA Reserve Bank nonetheless made further advances to it of R700 million in August 1990 and a further R500 million in September 1991. In fact, Frank Welsh writes that on 17 August 1998 Marinus Daling (former Sanlam and Bankorp director) told Judge Willem Heath in an interview that **"Trust Bank had been insolvent at the time of the 1990 lifeboat"**.

It gets worse.

A further meeting was held on 1 August 1990 between the SA Reserve Bank, Bankorp and Bankorp's controlling shareholder in which Sanlam housed its strategic investments, Sankorp. The SA Reserve Bank was represented by Dr Chris Stals (Governor), Dr JA Lombard (Senior Deputy Governor), Dr BP Groenewald (Deputy Governor), Dr JH van Greuning (Registrar of Banks), and Mr SS Walters as secretary. Bankorp and Sankorp were represented by Mr Marinus Daling (Chairperson of Sankorp), Mr PJ Liebenberg (Chief Executive of Bankorp), Mr HJ van der Merwe, Mr PJ Strydom and Mr AS du Plessis. At that 1 August 1990 meeting, it was explained that the financial position of Bankorp had deteriorated to the extent that the SA Reserve Bank was **"confronted"** with a situation where Bankorp no longer met the requirements of the Banks Act. Mr Liebenberg (Bankorp Chief Executive) explained that:

- Bankorp had made no operating profit during the 1989/90 financial year
- excessive asset growth during the year had led to a situation where only 52% of total assets of some R35 billion of the Bankorp Group was profitable
- intangible assets were included in the balance sheet
- Bankorp had been unable to resolve its historical financial problems
- provision would have to be made for the writing off of bad and doubtful debts to an estimated amount of R1 billion.

The Bankorp Chief Executive (Mr PJ Liebenberg) also mentioned that by placing R1 billion worth of weak assets and doubtful debts in a risk portfolio, the balance of the asset portfolio could be expected to show a profit.

As a result of Bankorp's financial position, Bankorp and Sankorp requested the SA Reserve Bank to increase the existing loan of R300 million by a further amount of R750 million.

Question: where was Kobus Roetz – the former Trust Bank managing director who had told Judge Willem Heath of the SIU that the Bankorp bad and doubtful debt book submitted to the Reserve Bank in order to secure the assistance **"was a multiple of *five times***" the real number – when this happened? It appears that the Davis Panel of Experts had no regard to that evidence. Nowhere in its Report does it even refer to it. What other crucial evidence did the Davis Panel of Experts miss or disregard?

Well, two days after that meeting, **on 3 August 1990**, an oral agreement was concluded between the SA Reserve Bank and Bankorp in terms of which the Reserve Bank provided a package of aid to Bankorp (again via Banbol). This was the first of two advances under the **Bailout Package B** arrangement. The material terms of the agreement included the following:

- The R300 million assistance (**Package A**) that was already in place at the time remained in existence.
- A further amount of R700 million would be provided and Bankorp had to invest R400 million of the total amount of R1 billion with the SA Reserve Bank in cash and the other R600 million in government bonds for a period of five years.
- Both the R400 million cash component and the R600 million government bonds component would be invested at a yield of 16% per year. These investments served as collateral for the assistance. So, as Frank Welsh points out, **"the security said to be taken was no security, but part of the loan itself"**.
- As the assistance of R1 billion incurred an interest charge of 1% per year, a margin of 15% per year accrued to Bankorp, which would be for its benefit and against which the bad debts in question would be written off over the five-year period.
- Bankorp's cash dividends were limited to minority shareholders for as long as the facility continued. Sankorp was required to invest its share of the dividends in new capital in Bankorp. I pause here to point out that these "minority shareholders" are nowhere identified in the Davis Panel Report. However, it would seem from other material that I have consulted that they may have included the Rupert family's interest (See, for example, *Dangerous Deceits: Julian Askin and the Tollgate Scandal* (1999), Chapter Seven *"Safety at Sea"*, page 194, by Frank Welsh: **"Anton Rupert, whose interests held a controlling interest in 25 per cent of Absa shares, was on the board of the Reserve Bank when the 'Lifeboat' was launched"**). Question: why did the Reserve Bank have on its board a person who had a controlling interest in a bank regulated by the Reserve Bank?
- In addition, the agreement provided that certain conditions would be applied in the administration of Bankorp. These included the closing of 70 of its branches by 31 December 1990, the reduction of its staff by approximately 3,000 before 31 December 1990, a reduction in total assets by R5 billion by 30 June 1991, and periodic reporting to the SA Reserve Bank on the extent of bad and doubtful debts.

The Chief Executive of Bankorp was also required to hold quarterly review discussions with the Bank Supervision Department of the Reserve Bank.

It is not clear whether any of these conditions were fulfilled. But, if what happened on 5 September 1991 is any indication, it would appear not. I could find no evidence that these conditions were enforced by the SA Reserve Bank.

The second advance in the **Bailout Package B** arrangement came on **5 September 1991**. On that date, Bankorp CEO (acting on behalf of Bankorp), Dr Chris Stals (acting on behalf of the SA Reserve Bank), and Mr Marinus Daling

(acting on behalf of Sankorp), concluded an agreement which amended the conditions of the 3 August 1990 agreement discussed above. The reason for this amendment was said to have been that it transpired that Bankorp's bad and doubtful debts had then amounted to R1.635 billion. Again, the evidence of Kobus Roetz about inflated bad and doubtful debt numbers looms large. Was this number real or manufactured?

Whatever the case, it seems that the Reserve Bank did not ask that question as its directors acquiesced in a further capital injection into Bankorp. A further amount of R500 million (bringing the total assistance to R1.5 billion) was provided by the Reserve Bank to Bankorp (via Banbol). This amount would be utilised to buy additional government bonds in the amount of R500 million. In terms of this further agreement, Bankorp was to cede all its rights and titles in these additional bonds as security for the further capital amount of assistance to it by the Reserve Bank, over and above the "security" for the earlier assistance described above. Again, bonds purchased with public funds advanced as a "loan" by the Reserve Bank were purportedly used as "security" for that same "loan".

Before this agreement was concluded, the financial assistance package was discussed with the Minister of Finance (Mr BJ du Plessis) at a meeting on 31 July 1991, attended by Dr Stals (Governor), Dr CJ de Swardt (Deputy Governor) and Adv MCJ van Rensburg (Assistant General Manager of the Reserve Bank).

When viewed in its totality the package yielded a net interest margin of 15% per year and generated a benefit to the Bankorp Group of R225 million per year for the five-year period 1991 to 1995, amounting to R1.125 billion in total.

This entire financial assistance which was provided to Bankorp in terms of the agreement (**Package A** and **Package B**) was to be applied towards the writing off by Bankorp of an identified set of bad or doubtful debts as at 30 June 1991, with any further losses to be met from sources other than the Reserve Bank.

The agreement contained a repayment provision in favour of the SA Reserve Bank which would have been triggered if the bad debts written off did not reach the agreed figure, **but there was no other provision for any repayment by Bankorp of any or all of the total net interest income which accrued to it during the period of operation of the agreement.** In other words, Bankorp was not required to repay the R1.125 billion that it stood to earn, using Reserve Bank funds, over a five-year period.

This assistance was subject to a further condition that the Bankorp majority shareholder (Sankorp/Sanlam) would have to provide the means to cover a substantial part of the total assistance required by Bankorp, that is, the difference between the debts of R1.635 billion (real or imagined) and the Reserve Bank's assistance amounting to R1.125 billion.

Again, I have not seen these agreements. They do not seem to be publicly available. Thus, I am unable to verify the accuracy of what the Davis Panel Report records both as regards the dates and detail of the contents of these agreements. I assume that the facts recorded by the Davis Panel in its Report are correct in this regard.

**Bailout Package C – Absa enters the scene**

According to the Davis Panel Report, the acquisition of Bankorp by Absa Bank became effective as at 1 April 1992. The acquisition was conditional upon the financial assistance from the SA Reserve Bank, arranged under **Bailout Package B** prior to the takeover, remaining in place. In other words, Absa Bank was to receive the future stream of net interest income previously arranged for Bankorp. As a result of this takeover, the September 1991 agreement was renegotiated between 1992 and 1994.

A new agreement was concluded **in 1994** with retrospective effect to 1 April 1992. This agreement was similar to the previous agreement (**Bailout Package B**), except that:

- Absa Bank replaced Bankorp as the beneficiary. (Ms Maria Ramos, Chief Executive of Absa Bank at the time of Absa Bank's review application to set aside the Public Protector's Report before the Pretoria Full Bench, confirmed this in her founding affidavit.)
- The requirement that Sankorp had to reinvest all dividends was abandoned.
- Bankorp was allowed to substitute a new statement of bad and doubtful debts as at 31 March 1992 (details of which had been audited) for the unaudited list of bad and doubtful debts as at 30 June 1991 in its reporting to the Reserve Bank. (Is this a reflection of the Reserve Bank having discovered the inflated bad debt numbers as alleged by Kobus Roetz? If so, what did it do about it, if anything? What did the Bankorp and Reserve Bank auditors know about this and when did they get to know about it?)
- The debts of debtors which had been classified as bad or doubtful as at the beginning of June 1990 could, depending on the financial position of the debtors, be increased or decreased in the actual write-off of bad debts against the amounts of financial assistance provided by the Reserve Bank, with the proviso that in the case of any debtor a debt written off may not exceed the amount of total indebtedness to Bankorp as at 31 March 1992.
- Absa Bank's external auditors were required in each financial year during the tenure of the 1991 agreement to audit amounts written off in order to ensure that such write-offs conformed to the stipulated conditions.

Again, I have not seen a copy of this 1994 agreement. I rely entirely on what the Davis Panel of Experts records in its Report.

The second agreement under **Bailout Package C** came in **1995** when a further agreement was concluded which amended the 1991 and 1994 agreements. The reason apparently given for this was that part of the government bonds that served as "security" for the Reserve Bank's assistance to Bankorp/Absa Bank would mature before the termination of the 1994 agreement. Accordingly, the Reserve Bank purchased the government bonds from Absa Bank and required Absa Bank to deposit the proceeds of R1.1 billion with it, and to cede the deposit to the Reserve Bank as security for the loan extended to Absa Bank. Absa Bank would earn interest on the deposit at a rate exactly equal to the rate of interest it would have received on the government bonds. This agreement terminated on 23 October 1995 when the accumulated total of financial assistance generated in terms of **Bailout Package B** and **Bailout Package C** amounted to R1.125 billion.

I have not seen documentary evidence of any of this. The Davis Panel Report provides no evidence for this conclusion. I have also not seen any of the agreements referred to above (including the 3 August 1990 agreement, the 1994 agreement and the 1995 agreement). I rely on what the Davis Panel of Experts records in its Report and have no reason to believe that it would deliberately misrepresent the contents of these agreements.

That, then, is the background to the Reserve Bank bailout controversy. The Davis Panel of Experts (which I discuss later) found that it did not comply with international best practice for central bank rescue of distressed banks.

But what are these best practice standards? Let us end this Part 1 with a discussion of these.

## INTERNATIONALLY ACCEPTED PRINCIPLES OF BEST PRACTICE

The Davis Panel of Experts distinguishes among three types of Central Bank interventions. These are

- **Liquidity support:** operations designed to provide liquidity to a bank which faces a liquidity problem but is solvent (a typical operation being a short-term loan against good quality collateral)
- **Solvency support:** operations to re-capitalise a bank that faces a solvency crisis that is capable of being resolved, and profitable trading restored on a sustainable basis (which might involve a grant of public funds through the Central Bank or other agency to protect retail depositors in the process)
- **Insolvency intervention:** operations to assist the orderly liquidation or sale of an insolvent bank (which, too, might involve a grant of public funds through the Central Bank or other agency to protect retail depositors in the process).

The Bankorp/Absa Bank assistance was none of these.

The Reserve Bank has – since its then governor (Dr Chris Stals) gave a lengthy lecture of uninterrupted evidence at the Tollgate enquiry – claimed that the Bankorp/Absa Bank assistance constituted the performance by the Reserve Bank of its function as a **"lender-of-last-resort"**.

The Davis Panel of Experts says the commonly accepted features of a **"lender-of-last-resort"** operation – usually afforded when, for example, a bank depositors' run on a bank is potentially contagious – are the following:

- Liquid funds are provided **against good collateral**
- The finance is provided for a defined **(short) period**
- The finance is usually provided at a **high interest rate**
- The funds are provided only to banks believed to be **solvent** but facing temporary difficulties and are made available to all such banks that apply for them
- Classic lender-of-last-resort operations are designed to provide banks with immediate liquidity in the form of cash, temporarily shortening the maturity structure of bank assets in order to enable banks **to meet depositors' demands** to convert liquid liabilities to cash.

According to the Davis Panel, the assistance to Bankorp/Absa Bank **did not** meet the generally accepted best standards of central banks as **"lender-of-last-resort"** for the following reasons:

- The assistance was not for a short term (it continued for 10 years)
- The interest rate charged (at 1% per year) was not high
- There was no requirement for management restructuring
- No cost was imposed on management (such as dilution of equity)
- The assistance was a simulated transaction, not a short-term loan
- The Reserve Bank took no equity stake or other form of compensation
- From 1992 Absa Bank received a grant (Package C) for which it did not qualify since it was not suffering liquidity or solvency problems
- Bankorp and Absa shareholders benefited from the assistance, not the depositors.

The Davis Panel sums this all up in two sentences:

> **"Dr Stals has also argued that the form of assistance was consistent with the practice and principles of central banks elsewhere. The Panel finds that the packages were not in line with contemporary or subsequent international best practice."**

In PART 2 I shall discuss the findings and recommendations of the Special Investigating Unit led by Judge Willem Heath, those of the Davis Panel of Experts led by Judge Dennis Davis, and those of the Public Protector. I shall offer my own view on the soundness of these findings and recommendations, and provide what in my view ought to be done in order to recover the money from those who benefited at the cost of many deserving causes in South Africa, like healthcare, housing and quality education, all of which are rights that are enshrined in the South African Constitution.