

Transcript of the Press Conference on the Hercegovacka Bank

Participants:

Ambassador Donald Hays, Principal Deputy High Representative

Miss. Toby Robinson, Hercegovacka Bank Provisional Administrator

Mr. Johan Verheyden, Hercegovacka Bank PA Spokesperson

Mr. Verheyden: Good morning everyone and welcome to this press conference. Let me first introduce the people who have come with me to Mostar today: on my far right is Ambassador Hays, the Principal Deputy High Representative of the OHR; and Miss Robinson, the Provisional Administrator of the Hercegovacka Bank. Ambassador Hays will start this press conference today with a few remarks on the reason why the High Representative, Wolfgang Petritsch, installed the Provisional Administration, and Miss Robinson will inform you about her findings so far on the difficulties and the successes of the investigation, and about the future of both the Provisional Administration and the Bank itself. And, after the opening remarks, there will be time for your questions. I give the floor to Ambassador Hays.

Ambassador Hays: Good morning. I am always pleased to come to Mostar because it is much nicer here than it is in Sarajevo in terms of the weather, the sun and the setting. But, today's event is a sobering one. It is almost a year today when the High Representative decided that events unfolding with regard to the Bank required the installation of a Provisional Administrator. And it is useful to recall that at that time the High Representative stated that he was convinced that the interest of the public and the confidence and the credibility of the banking system in BiH in general and in the Hercegovacka Banka in particular required a Provisional Administrator to be installed. Now, for most of you – you probably will recall that there was an attempt on April 6 to enter the Bank and to do it in the way a Provisional Administrator normally takes over a bank. Because, this takes place frequently in Europe and in the US – as a matter of fact, it has taken place in this country on a number of occasions as well. But, on that occasion, crowds gathered around and drove the Provisional Administrator and those who were attempting to do orderly business out of this city. And it was only because of that violence and the damage and the destruction done that military force had to be used to come back later to gain entrance to the Bank and other branches. I have seen in the press over the last week or so comments that say “after a year, nobody has been convicted, there is no evidence of illegal activities, there have been no findings”. But, first and foremost, I will tell you that, while there was a massive attempt to destroy records and computer files, we have successfully uncovered all of the computer files going back to 1998. Over a million documents were seized and 600 000 computer files. And these have been analysed by professional bank examiners and forensic auditors. And what has come to light is a sad story of criminal activity. When this Bank was established, the intent stated was that it was to sponsor the economic well-being of the Croat community in this part of the Federation. But, in point of fact, the Bank quickly became an institution to further a political agenda of a small group of individuals. The information coming to light now, as a result of investigation, indicates that not only were they engaged in a political effort to undermine the Federation and the Constitution of this country, but they quickly became involved in diversion of funds, fictitious loans, embezzlement, tax evasion, fraud and self-enlargement. OHR's role is to follow the criminal activities of those who were involved in this banking scheme. We have established 4 investigative teams, we are integrating the members of the federal investigative branch of Special Police, the Tax Police along with professional law enforcement and experts on bank fraud from the IC. Currently, over 20 cases have been handed over to the Prosecutor for further examination and we foresee this continuing throughout the summer and into the fall as we get further access and further information from the files that we have at our disposal. Now, it is inappropriate for anyone to discuss the particularities of legal cases, criminal cases that are now under investigation, so neither Miss Robinson nor I will be able to discuss individual involved in these cases. But we can talk about the pattern of action which has come to light and which is the basis for these criminal charges. The sad fact is that the people who lost out in this Bank were the citizens that were the subject of the Bank's establishment in the first place. There is no doubt that the people who organised this scheme still have your money. So, with that I will turn over the discussion to the Provisional Administrator. Thank you.

Miss. Toby Robinson: Good morning. As Ambassador Hays has said, it has been one year since the Hercegovacka Bank has been placed under Provisional Administration. In that year, we faced many challenges but we have made a lot of progress. I think the most important message that I want to convey today is that failure of this Bank was imminent. The Bank faced serious liquidity problems, it had a portfolio of bad loans, much of its capital was fictitious and the loan losses far exceeded the ability of its capital to absorb those losses.

Typically, a bank takes deposits, it takes that money and it makes loans. In order for any bank to be successful, those loans must be repaid. If they are not repaid, depositor cannot be repaid. And in order to establish a bank, it must have a banking license. Operating a bank is a privilege, it is not a right. And when the regulator gives you that license, you agree to abide by all of the laws inside the banking practice. These laws are not just technicalities, they are there to protect the depositors. So, as I go through this, it may sound technical to you but remember: these laws are there to protect the depositors and, if a bank violates them, the depositors are at risk. The primary cause for the failure of this Bank was its preferential loans to the insiders. Approximately 2/3 of the commercial loan portfolio was made to shareholders, Oversight Board members, and related companies. In many cases, these loans had no collateral, if they did get collateral they did not perfect their legal interest. There was no expectation from these borrowers to repay the loans, selected individuals were not required to even pay the interest. We have numerous examples where the Bank just continued to add interest to the loans and the borrower never paid anything. A bank will not survive if it follows these practices.

In our review of the loan portfolio, most of the loans had law violations associated with them, these are substantive violations, not just technical issues. These are basic principles that every bank must follow or the bank will fail. It did not even follow its own internal practices and policies that it had set up, which is telling obviously albeit its need to obey the law. But, when you find a bank which sets up its own policies and it will not even follow its own guidelines, you have a problem.

When the Provisional Administration was installed a year ago, this Bank was illiquid. In the preceding 2 months, 21 million of the 29 million in citizens' savings was withdrawn. So, it was not just the High Representative of the International Community that had lost confidence in the Bank. The depositors had lost confidence, as well. Any time depositors lose confidence in a bank, it's catastrophic. I believe the former Management has made much of the fact that the large cash balances that the Bank had. When I say the Bank is illiquid, it is true the Bank had large cash balances, but that is only half of the equation. You must also look at how much the Bank needed to operate. And, regardless of how large those cash balances seem to you, if you have more withdrawals than you have cash, you are illiquid. And that is the situation this Bank faced. Because of the large concentration of Government funds that were in this Bank, it represented 50 % of the deposit base. Large amounts of those funds were to be withdrawn within a matter of days. The bank would have been unable to meet those withdrawal requests.

So, where do we go from here? We are nearing completion of our assessment of the Bank. Perhaps I should step back.

In accordance with the Banking Law, a Provisional Administrator must first assess the condition of the bank, and then make a recommendation as to the final resolution for the bank. We are nearing completion of that portion of my responsibilities. As I am sure you remember from previous press statements, there are 3 options for this Bank. And this is not unique for this Bank, this goes to any bank under Provisional Administration.

Rehabilitation is always the first option a Provisional Administrator will look at. It is always the best option if it can be done. If that is impossible, you look at the sale of the bank. And the last alternative is liquidation. Right now, I do not know which of these alternatives will be the final conclusion of this Bank. That decision will be made very soon, I think. As Ambassador Hays said, the investigation phase will continue for some months and that is not unusual in these cases.

So, in summary, I just wish to reiterate something Ambassador Hays said: this Bank was started with very noble goals in mind. Unfortunately, a few criminal hijacked it and, as a result, almost 40 000 depositors in this Bank will be the ones who lose: that includes citizens, legal entities, all the municipal and cantonal governments in Herzegovina, hospitals, school, medical clinics and the federation Government – which is, of course, the citizens' money, including the Croat Government. These were Federation's money's designated for these cantons. So they now cannot provide you all the services that you would expect from them. There is substantial evidence on criminal activity and that will be pursued over the next few months. I think all of us would agree that the people responsible should be held accountable. And I am looking forward to finalising the issues regarding this Bank and, hopefully, we can resolve these as quickly as possible.

Ambassador Hays: Let me just wrap up this portion of the press conference just by saying that this Bank, whatever the formal purpose for establishing it, intent of the organisers, at least initially, was to establish control of the economy, of the Croat portion of economy, of the Federation. And they went about their business the same way any other organised crime family would do. They used extortion, loan sharking, false companies, the manipulation of Oversight Boards and the rapid transfer of money which we call "kiting", they paid off government officials, police and the military, and they all got their personal cut. And when they saw their house of cards crumbling, they took the cash and moved to the way from the Bank so that you could not get it back. So, our goal right now, as International Community, is to bring the people responsible to the court of justice. Thank you.

Mr. Verheyden: O.K. Questions? If I may just ask that you state your name and the medium. Since there are a lot of you, please note that we do not have that much time – if we could limit this to one question and one follow-up question.

Questions:

Zoran Kresic, Vecernji list: I am interested to know if you have found or traced down at least a single Kuna from the amount of 54 million Kunas that Croatia sent through the Hercegovacka banka and that are allegedly missing? Also, I have talked to former director Karlovic today. He claims that the Bank was liquid on the day it was closed down and that it had 40 million Marks at its disposal, meaning more than it was needed.

Miss. Toby Robinson: I will address the last question first. The Bank did have approximately 40 million Marks. However, not all of that was available to pay out depositors. As Mr. Karlovic should know, a portion of that is at the Central Bank and is held there as reserves and the Bank may not withdraw it. Other portions of that cash were in foreign correspondent bank accounts. In one instance, there was 4 million in a Croatian bank to secure guarantees and letters of credit for inside companies, the shareholders of the Bank. So, of that 40 million, the Bank did not have nearly that much available to pay its normal withdrawals to depositors. So, I think that is a very misleading number and if we compare that with the amount of money that was about to be withdrawn by the MIO, by the Federation Ministry of Finance, the Bank could not have funded all those withdrawals.

Well, for the record, in 1999 alone, 1.1 billion Kuna went from the Croatian Government through this Bank – a minimum of 1.1 billion Kuna. So, we are not talking about 54 million. And we are looking at every Kuna that came from Croatia. There was approximately that much that came in in 2000 and pretty close to that in 1998. That is Croatian Government's money that came to this country to pay soldiers' salaries, pensions, aid for fallen soldiers' families. I think we can all agree those were very noble recipients worthy of it. At the same time, we have the same constituents – they did not get paid. So something is wrong because the money came through this Bank, it did arrive from Croatia. And that is one of the areas that we are investigating with the cooperation of the Croatian Government. As you can imagine, there are millions of transactions involved and we will follow it until we know what happened to it. If it takes a month or 6 months, that's how long it takes. But, on the other hand, I am not going to sit here and accuse Mr. Karlovic or anyone else of inappropriate behaviour regarding that money. It is not right to accuse someone in the media when they have no opportunity to defend themselves. So let me make it clear: we are investigating the Croatian money, I am not going to make any allegations regarding it and once the investigation is complete, we will know.

Mirsad Behram, RTVMO: It has remained unclear at least to me – I do not know about my colleagues. From what you and Ambassador Hays have been saying, especially if we take into consideration what was said and written over this 1 year: in what ways have all these criminal activities been linked to politics. Ambassador Hays has said these activities were an attempt to undermine the FBiH Constitution. Can you tell us in what ways were politicians involved in all of this?

Ambassador Hays: We have recently spoken to senior politicians in the Government. They have indicated to us that they were well aware of the power share agreement between the previous administration which allowed parties to divide up the spoils of the Federation. It was in this context that the individuals that set up this bank were able to construct a Bank that would control the majority of business as operated in the Croat community. And then, once they control the businesses, they could tax the businesses. Once that happened, they then turned to drawing in municipal, cantonal and federal funds into the Bank. The Bank quickly became equivalent to a Treasury

for these people to manage what they considered the Croat community. It was clear that the intention was to make this region autonomous within the Federation under their control. And if you reflect on the events leading up to April 6th, it was clear, at least to those in the IC and in the Federation, that things were about to take place and with regard to developing an autonomous region. Now, while this is something of great concern to both the Federation, the state and the IC because it is destabilising and therefore anti-Dayton, the OHR and the IC is focused on the criminal activity that took place in this Bank and not on the political activity. Because, in the process of their activities, those who were in this enterprise defrauded the public and the clients of this Bank of millions of KM while enriching themselves. And they never thought a moment about what they were doing.

Amela Rebac, Studio 88: Newspapers reported on the meeting between Federation officials and Miss Robinson, so I would like to ask about the amount of 17 million KM which is practically a debt to the retired people. There was a law-suit mentioned in this context by Mr. Grabovac.

Miss. Toby Robinson: I am not familiar with Mr. Grabovac's statement. I think the 17 million is the Ministry of Finance.

Amela Rebac, Studio 88: Yes, the money was here, in the Hercegovacka banka.

Miss. Toby Robinson: Yes, it is. That and much more. I think the 17 million goes to various agencies within the Government but is under the control the Ministry of Finance. I think the Minister was attempting to transfer that money just prior to April 6. As I understand, the Federation obviously desperately needs the money. But I am not familiar with the (not audible) what Minister Grabovac is referring to a criminal charges related to the 17 million. So I cannot – you can address that directly.

Ambassador Hays: We met with the Minister, the Prime Minister and others over the past several days. At that meeting, we discussed in detail the status of the bank, the decisions that had to be made. They outlined their concerns with regard to funds that had been deposited and that have not been available to them. And over the course of the next week, we will be meeting with the Central Bank and bank regulators to get a better picture on how we should move forward with regard to the Bank. But, we did not speak about the specifics of any criminal activity, charges, nor did they ask us with regard to individuals and criminal charges.

Emil Karamatic, BHR1: Listening to you now and by analysing what you have said, my question would be: are you truly concerned about common citizens or the Federation.

Miss. Toby Robinson: My first responsibility is to the depositors of this Bank – it's not to the shareholders or anyone else. It's to the depositors. The most difficult part of this job is facing those depositors and telling them I cannot give them their money back. And they have every right to expect that. In December or November, the High Representative amended the Banking Law so that we could pay out the citizens' deposits of 5000 and under. That affected all banks under Provisional Administration, not just this one. And I cannot tell you what a positive change that is. Other banks in this country under Provisional Administration go for 2 or 3 years and they cannot pay even 50 Marks.

Following this Decision, in December we paid out over 9000 citizens I think and we made every effort to pay it out before Christmas and we were successful. At the same time, we have set up procedures so that any depositors, citizen depositors, who could not be there during that period can contact the branches who will make arrangements to pay them even today. So, as Ambassador Hays said, we are exploring ways to try to alleviate, to reduce the hardship on the remaining depositors. However, under the banking Law, the Minister of Finance is treated like any legal entity. I am personally.... If we can look at the way to reduce the hardship on them, it is for all depositors. We should not treat the Minister of Finance differently, that is my opinion. So, we are looking at options that would affect all depositors, not just the Minister of Finance. So, to answer your question – I am concerned about all depositors, the Ministry of Finance is one of them. But I am concerned about all of them.

Alija Behram, Radio Free Europe: You have mentioned the 3 options as to the Bank's future: rehabilitation, sale, liquidation. Which one do you find most likely?

Miss. Toby Robinson: I wouldn't speculate at this point. I have tried to keep all 3 options open, which is difficult. But because liquidation is so catastrophic, it is the worst option, but sometimes it is the only option, so I have tried to keep the option of rehabilitation open as well as a sale to another institution or investors. We need to come to a final resolution on the Bank, so we are going to have to make some difficult decisions, but at this point I would not

speculate as to which of the 3 options we will chose.

Ambassador Hays: Can I interject here? The question with regard to the future of the Bank will not be resolved by the Provisional Administrator. It will be managed by the Central Bank and the banking regulators. And, in fact, this Bank and those who were involved in it and were involved in massive criminal activities will pay a role in that decision. Thank you.

(end of tape)

Alija Behram, Radio Free Europe: ...we are facing more or less bankruptcy in the region, there are many strikes: judges are on strike, firemen, teachers and health workers also, there is a general financial collapse in the canton, the government does not function. Do you see a link between these events, the events regarding the Hercegovacka banka, and the collapse we face in Herzegovina and Mostar today? My question to Ambassador Hays is the following: are there politicians from the current leading positions of the current structures of authority in the state and who are possibly involved in this scandal?

Ambassador Hays: First of all, I will not indulge in speculation as to whether or not criminal indictments will be drawn against any particular individual. But clearly, the names of individuals who set up the Bank are well known to you and those individuals were fully knowledgeable about the actions of the Bank. With regard to the economic situation in the Federation, certainly, when the 3rd largest bank fails – as this Bank has- it does not have a positive effect on the economic situation. But there are many other factors playing in to the economic situation that we face today in BiH. And the solution is to open up the market economy for job generation, for both domestic and international investment, and to liberate economic activities that normally take place in a free market economy.

Miss. Toby Robinson: I would like to add something to that. Clearly, when a bank is in such a situation, it does have an impact on the economy. And, because of the size and scope of this Bank's activities, it has more of an impact than normal. But, I would encourage you to interview some of the borrowers of this Bank because, in our negotiation on trying to get loan repayments, I have taken great care that we sit down and work with the borrower and establish a repayment plan that he can live with, and not forcing into bankruptcy. And I think that will help the borrower and it helps the bank as well, the depositors. So we are well aware of the impact and we are doing everything we can to minimise that.

Marko Markovic, Dnevni list: In her opening statement, Miss Robinson mentioned an issue I would like to raise. Is there a way to collect debts from large borrowers, beneficiaries of loans that were not secured as the Bank did not have sufficient guarantees to repay these debts, through a court procedure so that the Bank can be saved?

Ambassador Hays: Let me just put the types of issues in stark contrast. There are 2 types of loans about what you are speaking. One is the loan to a business or an entrepreneur who is overextended, in which case, if that individual or that company is unwilling to work with the Provisional Administrator to find a way to repay the loan, then the court is the appropriate venue to get the money back. But, by and large, the largest loans that were given out were given out to front companies managed by people who owned the Bank. And they were not running any companies and there is only criminal charges waiting for them. Thank you.

Marko Markovic, Dnevni list: One more question....

Mr. Verheyden: I am sorry, but we do not have more time. Thank you very much.