



**REFLECTIONS ON:
WHAT WENT WRONG
AT
TRUST AND ROYAL BANKS**

**BY
DR G GONO
GOVERNOR
RESERVE BANK OF ZIMBABWE**

3 MAY 2006

CONTENTS

1.	Background.....	2
2.	Does Banking Insolvency Matter? and What To Do About It?.....	3
3.	Summary of Reserve Bank and Curators' Findings In Trust Banking Corporation Limited and Royal Bank Zimbabwe Limited.....	7
4.	Does the Above Sound Familiar?.....	24

1 BACKGROUND

- 1.1 This booklet contains a no-holds barred personal reflection by the Governor on the important matters relating to the recently concluded issue of appeals by failed banks (Trust and Royal Banks)
- 1.2. In this write-up, I also take the opportunity to comment on another topical issue regarding Zimbabwe's relations with the International Monetary Fund (IMF), and the specifics of what transpired during the recent IMF Board meeting of the 8th of March, 2006.
- 1.3 This personal reflection seeks to discuss in concise detail the pertinent issues that have been raised by many stakeholders regarding the specifics of what exactly happened at the failed banks, and specifically at **Royal and Trust banks**.
- 1.4 I have chosen to focus on the two banks and reveal exactly what happened at these banks because the matters are now in the public domain.
- 1.5 Details of what transpired at all other failed financial institutions namely, Time Bank, Barbican, Intermarket, CFX, First National Building Society and others are being withheld because in some of the cases, the matters are sub-judice as there are pending court cases.
- 1.6 In other cases, as Governor, I feel that it is better to "let sleeping dogs lie" because the institutions concerned have made progress towards self-rehabilitation and thus publishing the gory details of what happened in their past lives would prejudice their eventual recovery. As Monetary Authorities we wish them a speedy recovery, rehabilitation and/or integration into the mainstream Financial Sector of our country.
- 1.7 It is hoped that these personal reflections will inform and prompt objective debate on the issues at hand, which should cultivate reasonable convergence of views on a progressive way forward.

2 DOES BANK INSOLVENCY MATTER? AND WHAT TO DO ABOUT IT¹

- 2.1 The Economic Development Institute of the World Bank (EDI) Finance, Industry and Energy Division published in a well-researched paper by ARISTOBULO de JUAN¹ which was as relevant in the late eighties and nineties as it is relevant today.
- 2.2 In the research, de Juan tried to deal with the controversial issue of Bank insolvency, its symptoms and causes, implications to the depositors, shareholders, fiscal and monetary authorities, the economy as a whole and what to do about it.
- 2.3 When I was a part-time lecturer for four (4) years on the MBA Programme at the University of Zimbabwe (1994 – 1997) in the field of Banking, Money and Capital Markets, I made Aristobulo de Juan's articles “**essential and compulsory**” reading if one was to pass my subject.
- 2.4 In the wake of what has befallen the Zimbabwean financial sector prior to current stability and in the wake of the findings of the Independent Panel of Experts that produced the Recommendations on the challenge by Trust and Royal Banks, I thought it instructive to share with the broader community of both the banking and non-banking members of society insights from de Juan's research.
- 2.5 de Juan begins by pointing out to the conventional wisdom which is that a healthy and sound macroeconomic environment is a necessary and essential condition for banks to do well. He however goes further to reveal the “impact of micro phenomena” on both the macro and institutional situations.

¹ In these brief notes of reflection, I draw from the vivid lessons espoused in de Juan Aristobulo 'Does Bank Insolvency Matter? And What to do About It?' *EDI Working Papers, Finance, Industry and Energy Division*,.

- 2.6 There is no doubt that Zimbabwe’s macro-economic situation has had a negative bearing on the health and soundness of banks but what role has the individual institutional frameworks played in the insolvency of individual banks?
- 2.7 The following issues come out of de Juan’s work and I quote extensively from the said research findings:
That while it is undeniable that “macroeconomic problems have always been identified as a major cause of widespread bank insolvency, experience in (bank) supervision and dealing with problem banks shows evidence that **mismanagement plays a major role in bank insolvency**. A context of poor bank supervision, as well as political interference with banks in the areas of lending and recovery also plays a significant role” de Juan points out.
- 2.8 In his paper under title, de Juan focused on the microeconomic causes of bank insolvency namely: **mismanagement, lack of (adequate) supervision and political pressure**. I shall focus on the issue of **mismanagement** only.

MISMANAGEMENT

- 2.9 de Juan cites mismanagement as an “**evil itself that may cause serious damage to a bank or banking system as a whole**”.
- 2.10 “**The most significant feature of mismanagement is the dynamics of deterioration that it introduces in banks through a behavioural process that is difficult to reverse with external policies and measures**” the article says.

- 2.11 The author points out to **four types of mismanagement** which we as Zimbabwean Monetary Authorities **have found prevalent** in all **the failed banks that tried to take the Central Bank to court.** (Time Bank is still entertaining the idea of taking us to court and/ or smear-campaigning the Governor and his team.)
- 2.12 The identified categories of mismanagement are: **technical mismanagement, cosmetic management, desperate management and fraud.**
- 2.13. “They (the four types of mismanagement) do not have to occur in a sequential manner but when technical mismanagement leads to losses or to the need for dividend reduction, it frequently **unleashes** cosmetic and desperate (forms of) management.”
- 2.14 “Fraud may be part of the dynamics that make good managers become bad managers. **Illiquidity comes at the end of the process.** In the meantime the bank in question may have lost its capital several times” points out de-Juan.
- 2.15 “Technical mismanagement may involve a whole variety of **inadequate policies and practices.** The most relevant ones are over extension, poor lending, lack of internal controls, and poor planning in the areas of business and management”
- 2.16 “Cosmetic management consists of hiding past and current losses to buy time and remain in control while looking and waiting for solutions. Typical procedures include evergreening loans or systematic rollover(s), capitalization of interest, and fictitious or unrealistic collateralization.”
- 2.17 “Desperate management refers to a situation where bankers see themselves in danger of having to declare a capital loss or having

to pay no dividends. At this stage”, writes de-Juan, “the banker, besides indulging in cosmetics, will look for business that may permit them to buy time and make up for the previous deterioration.”

2.18 “The main practices followed under these attitudes are **SPECULATION, PAYING ABOVE-MARKET** rates for deposits, and charging (very) high interest rates to borrowers” the research paper reveals.

2.19 “Fraud may have been one of the causes of losses for a bank at that stage. When illiquidity approaches and the banker feels that the end may be near (writing is on the wall), the banker may be tempted to **DIVERT MONEY** out of the bank.” (Sounds familiar!).

2.20 “Typical channels (for diverting or siphoning money out of the bank when the banker realizes the writing is clearly on the wall) are:

lending to companies and buying or selling companies that are owned by, or connected with the bank (bank officials, shareholders, related parties etc).”

2.21 “All these operations (loans) are properly (or improperly) materialized through fiduciaries (third parties), paper (or shelf companies), and other similar methods to escape supervision.”

2.22. As a university post-graduate lecturer about ten years ago, I didn’t think that I would come across these aspects in real life, which teachings I regarded as “just theory” then. But ALAS, I was so on to be confronted with all these evils of banking practice hardly three months into my new job as the Chief Superintendent (Governor) of Zimbabwe’s Financial Sector!

- 2.23 To the “word and letter” of de Juan’s research paper, done in the early 1990’s, **every aspect of that research has revealed itself in Zimbabwe’s banking industry.**
- 2.24 Of course there are other aspects of shortcomings to do with the Central Bank itself and the Ministry of Finance as was the set-up then.
- 2.25 Inadequate Supervision or Supervision without full Authority to institute immediate remedial measures against culprits, political or Ministerial interference against instant remedial measures and a lack of a strong prudential regulatory and legal framework coupled with inadequate understanding of issues by those who are expected to stand for or instill sound financial systems in their environments are other causes that promote the decay of uprightness, and good corporate governance in financial systems of countries.

IMPLICATIONS OF BANK INSOLVENCY

- 2.26 Implications of bank insolvency to individuals and the whole economy and what to do when faced with such a situation are all aspects this Governor used to teach his MBA students for four years. **(Pity one hasn’t got too much spare-time to go back to “Uni” and start such classes again.** The evidence now available would expose the duplicity of certain individuals, **one or two of whom passed through my** hands but did not have the stamina to complete their MBA course till today, ten years down the road.
- 2.27 As Governor, I am however ready, time permitting, to share my little academic and practical knowledge of turn-arounds with those interested in the near future.
- 2.28 For the time being, read the Justice Smith Appeals Panel report on Trust and Royal Bank cases.

- 2.29 To demonstrate transparency, the RBZ has opened a data-room for the public to come and look into the details of how the management-shareholders of these two banks mismanaged the affairs of their Banks.
- 2.30 Furthermore, the Justice Smith Appeals Report together with these reflections have been posted on the Bank's website effective 3 May 2006. ([Ref; www.rbz.co.zw](http://www.rbz.co.zw))

3. SUMMARY OF RESERVE BANK & CURATORS' FINDINGS IN TRUST BANKING CORPORATION LIMITED AND ROYAL BANK ZIMBABWE LIMITED

- 3.1 In the interest of transparency and avoidance of doubt and speculation, the Reserve Bank hereby takes the unprecedented step in the history of the country's financial services industry, to spell out what exactly transpired in the case of Trust Banking Corporation and Royal Bank Zimbabwe and how the Reserve Bank had to inevitably step in the way it did in the National interest.

TRUST BANK CORPORATION LIMITED BACKGROUND

- 3.2 Trust Banking Corporation (Trust Bank) began operations in January 1996 as a merchant bank and converted its licence to a commercial bank in 2000.

Prior Examinations

- 3.3 Over the years, the bank was subjected to a number of on-site examinations which noted a number of deficiencies in asset quality, liquidity and internal controls, among others.
- 3.4 The October 2003 on-site examination determined that the banking institution was still exposed to high liquidity risk; poor accounting systems; was engaging in non-banking business via a wholly owned subsidiary, TMB Nominees; and was exposed to high reputation risk.
- 3.5 The bank's acute liquidity problems worsened in the second and

third quarters of the financial year ended December 2003. By December 2003, the bank was relying on Reserve Bank liquidity assistance, which amounted to about \$100 billion on a daily basis.

Investigation of Trust Bank

- 3.6 The Reserve Bank commissioned an independent investigation of Trust Bank Corporation, in terms of the Banking Act, in December 2003, which was led by Camelsa Chartered Accountants (Private) Limited, in order to get to the bottom of the bank's chronic liquidity problems.
- 3.7 The investigation confirmed a liquidity gap of \$110 billion as at 12 December 2003, against the bank's understated liquidity gap of \$70 billion. The disparity indicated that the bank was misrepresenting the gravity of the problem in order to continue accessing RBZ lender of last resort facilities under the pretext that the problems were of a temporary nature. (de Juan's "writing on the wall" statement!)

Major Causes of Liquidity Problems

- 3.8 The investigation attributed the bank's liquidity problems to a number of factors including the following (technical, cosmetic and fraudulent management):
 - a. Rapid expansion of the bank with no proper internal controls and early warning systems.
 - b. Poor management information systems which compromised the integrity of the bank's financial records.
 - c. Poor asset and liability management manifested through the

investment of short-term funds in illiquid assets which included, **furniture, real estate property, bricks, fridges, as well as shares on the Stock Exchange.** These transactions were being conducted via the holding company at a time the bank was already experiencing serious liquidity constraints.

d. The bank was, thus, operating outside the confines of the Banking Act and Regulations through engaging in non-banking activities via a wholly owned special purpose vehicle known as TMB Nominees.

3.9 The investigation revealed significant non-performing insider loans granted without formal loan agreements or facility letters, and/or proper due diligence as follows:- TMB Nominees (\$23.8 billion); Trust Holdings Limited (\$6.8 billion); and other insiders (\$17.6 billion).

3.10 The liquidity gap was compounded by massive withdrawals, speculation restricted maturity rollovers and insignificant deposits. As a result, the bank was compelled to attract new depositors at interest rates of up to 850% per annum when other banks were paying 500% for same. Some of the depositors were demanding security due to the bank's increased reputation risk.

3.11 Some banks and major wholesalers were no longer accepting cheques drawn on Trust Banking Corporation except on collection basis.

3.12 The worsening liquidity problems culminated in a run on the bank in January 2004.

Liquidity Assistance

- 3.13 To avert a systemic crisis, the bank was granted liquidity assistance on condition of the bank restructuring its operations, management and the board.
- 3.14 With the full concurrence of the bank's Chairman, then Mr. T. Masaya, the former Managing Director Mr. W. Nyemba, Finance Director, Mr. N. Hlupo and the Executive Director, Mr. C. Goromonzi were asked to resign from the board and bank. This was because of the 'Trust' lost between executive and non-executive directors, some of whom, by their admissions, were not fully aware of exactly what was going on in the Bank.
- 3.15 As part of the liquidity support, the bank was issued with a **Corrective Order on 13 January 2004** and was supposed to comply with the following conditions:
 - 3.16 Conducting a review on the appropriateness and suitability of its current management and board structures;
 - 3.17 Enhancement of the board oversight of operations and strengthening of management information systems;
 - 3.18 Discontinuation of activities that amount to violation of the Banking Act and Regulations;
 - 3.19 Restrictions on payment of dividends, incurring any debt or capital expenditure without prior written approval from the Reserve Bank;
 - 3.20 Widening the scope of risk management systems, and desisting from introducing new products without prior approval from the Reserve Bank;

- 3.21 Disposal of fixed assets and non-interest bearing assets;
- 3.22 Submission of reports on a quarterly basis sharing the progress made in addressing the issues prescribed in the Corrective Order; and
- 3.23 Submission of a weekly return of liquidity risk to the Reserve Bank.

Appointment of a Supervisor

- 3.24 A full time supervisor was appointed on 20 January, 2004 to monitor the situation at Trust Bank on an on-going basis.
- 3.25 The supervisor and his team resided at the bank's headquarters and attended all the management meetings held at the bank. Their main mandate was to assist in turning around the fortunes of the institution including assisting in the bank's merger efforts.

Deteriorating Conditions

- 3.26 Despite restructuring the board and senior management, the bank remained in a critical condition. The damage that it had suffered already was too severe to recover from. Read de Juan's research on the illiquidity situation! The financial condition worsened due to huge funding costs and the resultant operating losses. There was no tangible progress on recapitalization.
- 3.27 Various merger initiatives, notably with MBCA and NedBank/Old Mutual from South Africa failed to crystallise **largely as a result of the huge capital deficit the institution was facing**. Against this background, it was quite apparent that market solutions had failed to address the deep rooted structural anomalies at the bank.

- 3.28 The bank's capital position deteriorated significantly by 42% from (\$801 billion) as at 30 June 2004 to (\$1.14 trillion) as at 31 July 2004. **The bank was thus factually and technically insolvent.**
- 3.29 The bank was not in a position to meet its statutory reserves obligations amounting to \$17.3 billion as at 16 August 2004.
- 3.30 Furthermore, the bank failed to remit to the Reserve Bank \$31.4 billion repaid by some beneficiaries of the Productive Sector Facility (PSF) as at 16 August 2004 due to its liquidity constraints. The bank was also failing to repay other loans it had received from banks such as CBZ Ltd, Stanbic Bank, Interfin, First Mutual Ltd, and others and to save these banks from systemic risk, the RBZ had to meet Trust Bank's obligations on a number of occasions. At one stage, First Mutual Society policy and deposit holders almost went on strike due to Trust's failure to meet its obligations from this institution.

Placement of the Bank under Curatorship

- 3.31 Due to the foregoing, the bank was factually insolvent and placed under curatorship on 23 September, 2004. The decision to place the bank under curatorship was taken after various measures that had been taken to resolve the liquidity and solvency challenges facing the institution failed to restore the bank into a sound condition.

Curator's Findings

- 3.32 The curator Mr. Peter Bailey of KPMG confirmed that the bank was factually insolvent, with a net liabilities position of \$1.4 trillion as at 31 October 2004. In his opinion, **there were no viable options to turn around the fortunes of the institution as the bank had**

a formidable net asset value of negative \$1.447 billion.

3.33 The curator recommended that the assets and liabilities of the bank would be taken over by ZABG and only a shell company would remain with a negative equity of \$1.4 trillion.

Non-Compliance

3.34 Trust Bank was charged of contravening Exchange Control regulations, specifically:

(b) Exchange Control (Exchange Rate) Directive 2002. It was noted that on 359 separate occasions, **Trust bank had violated Exchange Control Regulations.**

(b) Exchange Control Directive RC34 as read with Directive RC51: It was noted that on several occasions, the bank failed to sell 25% or 40% of its foreign currency receipts to the Reserve Bank. The aggregate amount not remitted to RBZ amounted to USD14, 801, 013.00

Forensic investigation report by BCA Consulting (Pvt) Ltd

3.35 The investigation team of Forensic auditors confirmed the earlier findings pertaining to the conduct of the institutions' directors and shareholders before the institution was placed under curatorship.

3.36 The team **further confirmed that Trust Bank suffered financial prejudice as a result of actions of the former executive directors and noted the following additional wrongful conduct of the former directors of Trust Bank:**

- (a) There was a net debit of EUR 346,556.00 to the Commerz account in the month August 2004 which can not be accounted for. When the directors of Trust Bank resigned, signatories to Commerz Bank account were not changed.
- (b) Significant foreign currency amounts were debited to Trust Bank's nostro accounts yet there are no corresponding credits in the bank's ledger. **The total of ZAR 1,445,921.64, BWP 27, 201.57, EURO 706, 059.69 and USD 703,476.50 could not be accounted for** and yet, as we speak, the same Trust Bank former owner-managers have set up a new financial outfit in South Africa from where they are carrying on business unhindered.
- (c) Some of the amounts referred to above were transferred from Trust Bank's First Rand account to former Trust Bank directors as follows: ZAR 107,531.60 to Mr. Nyemba and ZAR 45,277.20 to Mr. Goromonzi.
- (d) On 27 August 2003, Trust Bank paid Euro 253,000.00 from Trust Bank nostro account, through Commerz Bank on behalf of First Mutual. The payment was in respect of cost of equity in FML purchased by Trust Holdings Limited in FML. This transaction was recorded as an asset in the books of Trust Bank yet FML is not a subsidiary of Trust Bank.

3.37 A Trust Bank cheque of \$961, 180 261.00 was made payable to NDH. The proceeds were distributed by NDH amongst former Trust Bank directors apparently on Mr. Nyemba's instructions partly as follows:

- (a) The sum of \$106,293,987.68 was paid to Luapa Holdings. Mr. Goromonzi is a director of Luapa Holdings (Pvt) Ltd.

(b) The sum of \$214,992,809.13 was paid to Wilta (Pvt). Mr. Nyemba is a director of Wilta.

- 3.38 Amounts of \$84,446,950.94 and \$800,000,000.00 were paid from Trust Bank to Uzben Enterprises and Transtobac companies in which Mr. Nhlupo was a director and shareholder.
- 3.39 An amount of \$800,000,000.00 was paid from Trust Bank to Transtobac a company in which Mr. Dhliwayo was a director.
- 3.40 The investigators were unable to communicate with the former directors who are now based in South Africa. There was therefore need for more efforts to be made in order to seek clarification on why the various payments were made and the fictitious assets created.

Specification

- 3.41 The Reserve Bank, on the strength of the reports before it, requested the Minister of Justice on 12 April 2005 to specify three of the former directors of Trust Bank namely, W. Nyemba, C. Goromonzi and N. Hlupo and their companies. This was meant to ensure that they would not dispose of their property or increase their indebtedness to the detriment of the creditors and facilitate further investigation into the activities of the directors.

Incorporation of Bank's Assets into Zimbabwe Allied Banking Group (ZABG)

- 3.42 In line with the Troubled Banks Resolution Framework, the bank's outstanding TBF loans were duly converted to equity. Over and above these, deposits and sundry creditors above \$5 million were also converted to equity.

- 3.43 After conversion, existing shareholders' interest was written off against accumulated loss and therefore they no longer had interest after conversion of TBF and other liabilities into shares in ZABG.

Court Action by Trust Bank Corporation

- 3.44 Trust Holdings Limited, the sole shareholder, lodged an application to the High Court, seeking to bar the amalgamation of the bank into ZABG. The main basis of the application was that RBZ and the curator were not empowered by the Banking Act [Chapter 24:20] to incorporate the bank into Zimbabwe Allied Banking Group (ZABG). The application was dismissed with costs by the High Court on 8 March, 2005.
- 3.45 A further appeal to the Supreme Court was dismissed with no order as to costs on 5 September 2005. The court ruled that appellants should have appealed to the Reserve Bank against the curator's decision to sell the assets. The rest of the story is the subject of the Justice Smith Appeals Panel Report which is now public.

ROYAL BANK ZIMBABWE LIMITED

- 3.46 Royal Bank Zimbabwe Limited was established in 2002 and commenced commercial banking operations on 8 May 2002. The major shareholder included Messrs Jeffrey Mzwimbi and Durajadi Simba. Investigations by the Reserve Bank and the Curator revealed that the two officials were **instrumental in running down the institution.**

Profile of Mr. Jeffrey Mzwimbi

- 3.47 Mr. Mzwimbi started his professional career in 1977 and was instrumental in setting up of United Merchant Bank in March 1995 where he was a Managing Director Designate.
- 3.48 **UMB later collapsed in April 1998 due to serious managerial shortcomings and poor corporate governance practices as evidenced by poor risk management practices, fraudulent and unethical banking practices.** Messrs Mzwimbi and Simba's involvement in running the affairs of United Merchant Bank (UMB) casts serious doubt on their fit and proper status.

Profile of Mr. Dujaradi Simba

- 3.49 Mr. Simba's professional career saw him working as a senior executive in a number of failed institutions such as United Merchant Bank, Universal Merchant Bank and lately Royal Bank.
- 3.50 Onsite examinations carried out by the Reserve Bank in 1998 on United Merchant Bank revealed that the bank was exposed to serious insider lending, extremely poor pre-lending practices and very weak credit administration. Similar problems were later discovered at Royal Bank.

Mr. Simba's Appointment

- 3.51 The Reserve Bank turned down the proposal to appoint Mr. Simba as an Executive Director at the licensing stage due to his glaring lack of prerequisite academic and professional qualifications as well as his questionable integrity.

3.52 However, as the overall decision rested with the then Registrar in the Ministry of Finance, he was finally allowed to take the position of Head of Business Development.

Factors leading to the collapse of Royal Bank

Siphoning of Depositor Funds...

3.53 Mr Mzwimbi spearheaded a cartel of bank management within the institution to selectively award contracts amounting to (\$21.6 billion) for the supply of various goods and services to the companies in which they had interests, or with whom they had relationships.

3.54 Some of these companies are (Gemtree Investments [Mzwimbi and Pemhiwa], Elytra Investments [Mzwimbi and Pemhiwa], Covenant Investments [D. & W. Simba – brothers], Panalla Investments [D. & T. Simba – spouses].

First Mutual Saga...

3.55 Royal Bank abused depositors funds amounting to \$17.1 billion to purchase shares in First Mutual on behalf of First Mutual senior management and Royal Bank directors.

3.56 This transaction later exposed the bank to liquidity and reputation risk. First Mutual Limited took Royal Bank to Court for \$60 billion and petitioned for liquidation of the bank.

Finsreal saga...

- 3.57 The bank was also involved in a legal dispute with Finsreal Asset Management Company which alleged that the directors of Royal Bank had passed fictitious entries on their account in the bank's books.
- 3.58 An investigation report by Ernst & Young indicates that the bank unlawfully used depositor's funds to create the impression that the bank's capital hand increased from \$108 million to \$500 million. The purported increase in capital was facilitated by the transfer, on 17 January 2003, of depositor's funds amounting to \$500 million to Finsreal Asset Management as a short-term investment. Subsequent to an early termination of the investment, the shareholders applied the proceeds, via numerous Finsreal cheques, to create a false impression of adequate capitalization of the bank. This was in violation of good corporate governance practices.

Poor Risk Management and Corporate Governance Practices

- 3.59 The bank advanced significant, unsecured loans to insiders in violation of sound risk management and corporate governance practices.
- 3.60 Some of the beneficiary insider companies included Gemtre Investments (Private) Limited, Elytra Investments (Private) Limited, Covenant Investments (Private) Limited and Panalla Investments (Private) Limited as noted above.
- 3.61 The shareholders recapitalised the bank using depositor's funds

in contravention of the Banking Act and the Company's Act.

- 3.62 The bank failed to pay statutory reserves amounting to \$28 billion as it was having serious liquidity positions as evidenced by accommodation facilities from RBZ amounting to \$77.6 billion as at 30 June 2004.

Use of Depositor Funds for Capital Expenditure...

- 3.63 The bank used depositor's funds to finance capital expenditure such as branch acquisitions. This implies that the expansion was funded by depositors instead of shareholders.

Ignored Early Warning Signs...

- 3.64 The bank ignored the early signs of the impending liquidity crisis. The directors ignored the following signs:
- (a) The bank was suspended from the clearing system on a number of occasions due to failure to meet its obligations to other financial institutions.
 - (b) Inability to meet maturities when they fell due.
 - (c) Inability to cover daily positions and a widening maturity gap.
 - (d) Disputes with First Mutual life over the \$60 billion debt obligation.

Supervisory Action by the RBZ

- 3.65 Following the April 2004 examination, it was established that the bank was factually and technically insolvent to the tune of \$140 billion.

- 3.66 Numerous negotiations were held with potential investors who included Kingdom Bank, Nedbank of South Africa, Investec Limited (South Africa), Tetrad Group (Zimbabwe), Loita Capital of South Africa, to no avail in view of the huge capital deficit.
- 3.67 Due diligence exercises conducted by the above prospective investors also unearthed serious corporate governance deficiencies.
- 3.68 At the time of the April 2004 examination, the board had 10 directors of which only two qualified as independent directors as the rest had ownership interest in the bank.

Curatorship...

- 3.69 Following the deficiencies noted above and the impending liquidation on the institution at the instigation of First Mutual lawsuits the institution was placed under curatorship on 4 August 2004.

Curator's Findings...

- 3.70 The Curator's investigations confirmed the RBZ's findings that the institution failed due to non-performing of inside loans, abuse of foreign currency, poor governance and risk management and insurmountable liquidity problems.
- 3.71 Given the magnitude of the problems and failure to find market solutions, the curator recommended that the bank's assets be sold to ZABG.

Specifications...

- 3.72 The curator recommended that the specification of Messrs Durajadi Simba and Jeffrey Mzwimbi in terms of the Prevention of Corruption Act [Chapter 9: 16].

3.73 The Investigator appointed by the Minister on 1 April 2005 has since unearthed numerous deficiencies including dealing in foreign currency on the parallel market as outlined below.

Misuse of Foreign Currency Resources...

3.74 Contrary to good corporate governance practices, Messrs Mzwimbi and Simba were the only directors who managed the foreign currency positions in the bank.

3.75 A special investigation report on foreign currency dealings by Royal Bank revealed that Messrs Mzwimbi and Simba intentionally disregarded the national laws and regulations governing the foreign currency transactions in Zimbabwe.

3.76 It was established that PGI purchased 70% shareholding in Zimtile from Jones Holdings Limited for USD1,550,000 in 2003. Royal Bank caused the purchase price of USD1,550,000 to be exported to Beresford Trustees. The former also caused USD50, 0000 to be exported to PG Zambia. The purchase price was transferred in batches over a 5-month period. The funds involved were sourced on the parallel market.

3.77 Royal Bank also transferred USD400,000 on behalf of First Mutual Reinsurance Limited without Exchange Control approval.

3.78 Mr. J. Mzwimbi purchased property in 2002 and the purchase price composed of Z\$63 million and USD100,000. The foreign currency component was done in violation of Exchange Control regulations.

3.79 Some companies had Foreign Currency Accounts (FCA) and current accounts with Royal Bank Zimbabwe Limited. Royal Bank liquidated foreign currency amounts from the FCA to current

accounts at parallel market rates.

- 3.80 Royal Bank facilitated transfers from people in the Diaspora to relatives and friends in Zimbabwe. The Bank created an external obligation payable in Zimbabwe, while the foreign currency was not remitted to Zimbabwe.
- 3.81 The bank also bought foreign currency using parallel market rates from employees and the general public.

Poor Board Oversight

The investigator concluded that the Royal Bank board failed in their fiduciary of:

- (a) Protecting depositor's funds;
- (b) Safeguarding the bank's assets;
- (c) Maintaining reliable financial records through a sound internal control system;
- (d) Showing financial statements that fairly present the affairs of the bank;
- (e) Compliance with applicable laws and regulations; and
- (f) Behaving responsibly towards shareholders

4 DOES THE ABOVE SOUND FAMILIAR?

- 4.1 It would be useful if Zimbabweans desisted from forever personalising issues whenever or wherever they are caught with their “fingers in the till”, so to speak.
- 4.2 The personal attacks that have been directed at the Curators by the very same people who have caused untold anguish to many innocent depositors is simply unacceptable in a progressive society.
- 4.3 Also, various stakeholders in our country must put aside personal interests in favour of National preferences. The extent to which money has allegedly changed hands simply to buy allegiances, protection and to entrench make-believe conspiracy theories in the minds of certain innocent but powerful forces and opinion-makers, is unbelievable!
- 4.4 In the end, it is the Regulator, the enforcer of the law, who is put on trial and not the perpetrator of the crime, in the first place. The level of hatred that has been sown in certain circles against the Central Bank by these culprits is unbelievable. We must as Zimbabweans learn to grow up and move on!



**DR G GONO
GOVERNOR
RESERVE BANK OF ZIMBABWE**

3 MAY 2006



