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Congress Wants Four Largest Banks to Surrender Rescue Funds

by LADB Staff  
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The Mexican Congress is engaged in a tug of war with four of the country's largest banks over irregular payments received from the now-defunct savings-protection fund (Fondo Bancario de Proteccion al Ahorro, FOBAPROA). FOBAPROA was created to avert a crisis in the financial system that resulted from the peso devaluation of 1994 (see SourceMex, 1995-03-08 and 1995-03-15). The fund ceased to exist in December 1998 after Congress replaced it with a new agency, the Instituto de Proteccion al Ahorro Bancario, IPAB). IPAB assumed all of the FOBAPROA debts (see SourceMex, 1998-12-16).

IPAB and the Congress want to conduct a new audit of the bad loans assumed by the government during the bank-rescue operation of 1995 to determine if these loans were proper. The legislation that created IPAB mandates the agency to audit all assets acquired during the 1995 bailout. The agency is hoping to conduct three lines of investigation: an evaluation of the efforts of banks to recover overdue loans; a review of the eligibility of assets transferred to FOBAPROA; and a confirmation of the existence of loans.

The IPAB proposal for a new audit followed a report by the Auditoria Superior de la Federacion (ASF), which said FOBAPROA improperly disbursed 50 billion pesos (US$4.63 billion) to Mexico's four largest banks Banamex, BBVA-Bancomer, Bital, and Banorte. The allocations were inappropriate because they covered loans that were fraudulent or otherwise improper, auditors said.

ASF director Arturo Gonzalez de Aragon later added another 20 billion pesos (US$1.85 billion), bringing the total that banks would be required to pay to 70 billion pesos (6.48 billion). The four banks control 70% of Mexico's bank deposits. Legislators are seeking the new audit because they believe it could reveal further instances where bankers loaned money to their wealthy friends and then passed on the losses to the government.

Sanctions sought

In his report, Gonzalez de Aragon also called for sanctions against the government officials responsible for the FOBAPROA decisions because they acted beyond their powers. Among these officials are Comision Nacional Bancaria y de Valores (CNBV) director Jonathan Davis and ex-finance secretary Guillermo Ortiz, now the chief governor of the Banco de Mexico. The report by the ASF, which answers to the Congress, is significant because it proposes that the government reduce the amount of taxpayer money that will be allocated to the banks under the 1995 agreement that created FOBAPROA.

Since FOBAPROA was replaced by IPAB, the zero-coupon bonds received by the banks have to be exchanged for the equivalent of about US$20 million in new securities before they mature in
2005 and 2006. Even though FOBAPROA no longer exists, the government's bank-rescue program remains a political hot potato because of perceptions that the main beneficiaries were wealthy bankers. The center-left Partido de la Revolucion Democratica (PRD) went as far as to accuse the former governing Partido Revolucionario Institucional (PRI) of creating the program to benefit its supporters at the expense of society (see SourceMex, 2000-02-02, and 2001-08-05).

There was some evidence that at least one banker used FOBAPROA to help fund the presidential campaign of PRI candidate Ernesto Zedillo in 1994 (see SourceMex, 1999-06-09).

**Court decision halts new audit**

The release of the ASF report prompted Congress to issue a resolution supporting the IPAB request for the new review of all the loans received by the four banks. The banks, in turn, filed an injunction against such a review, noting that a special audit conducted in 1999 already examined all the loans carefully. That review was conducted by independent Canadian auditor Michael Mackey (see SourceMex, 1999-07-14).

In a decision handed down in August, an appellate court in Mexico City (Juez Noveno de Distrito en Materia Administrativa) granted the injunction sought by the banks. The decision by Appellate Court Judge Alvaro Tovilla Leon means that IPAB cannot proceed with the audit until a district court issues a ruling, which could take as much as one year. President Vicente Fox's administration has offered a cautious endorsement of the proposal to conduct further reviews of the finances.

Finance Secretary Francisco Gil Diaz, in a letter to critics led by Mexico City's PRD Mayor Andres Manuel Lopez Obrador, said the Fox government would act "in defense of the people and take whatever steps are necessary to recover what rightfully belongs to them." The Secretaria de Hacienda y Credito Publico (SHCP) is seeking to negotiate a compromise between banks, Congress, and IPAB.

IPAB is said to have been displeased with the administration's support for only a limited investigation of the loans. Some sources close to the administration say top IPAB officials had threatened to resign this past May if the government had decided to allow a diluted investigation. The administration's weak endorsement of the audit plan is only one source of tension with the legislative branch regarding the FOBAPROA controversy.

As a parallel action, the SHCP filed a "constitutional controversy" with Mexico highest court (Suprema Corte de Justicia de la Nacion, SCJN), accusing the Congress of usurping a function reserved for the executive. The SCJN, in a decision handed down in mid-August, deferred a decision on whether the matter was a violation of the Constitution but also ruled that the ASF and therefore the Congress had exceeded its powers by ordering a reduction in FOBAPROA payments to the banks.

The Fox administration's mixed position regarding the FOBAPROA controversy has created divisions within the PAN. A majority of PAN legislators, including legislative floor leader Francisco Barrio Terrazas and influential Sen. Javier Corral, have endorsed the right of Congress to call for a new audit. "All political forces in Congress recognize the federal audit committee as the appropriate
agency for the review and supervision of all operations conducted by FOBAPROA," said Corral. This stance has put PAN legislators in direct conflict with Senate leader Diego Fernandez de Cevallos and party president Luis Felipe Bravo Mena. The PAN president failed in an attempt in late July to halt a resolution by the party’s congressional delegation supporting the ASF plan.

Fernandez de Cevallos denied accusations that he was siding with the banks. "I am not against the resolution put forth by my colleagues," said the powerful PAN senator. "I disagree with the format of the document that was presented."

The PAN support for the audit paved the way for the full Congress to issue its own resolution calling for the banks to submit to a new audit and to surrender the FOBAPROA payments. "This is a message to the banks, asking them to be more receptive," said PRI Deputy Felipe Solis. "The resolution also has a high political value, since all parties voted in favor."

Leaders of the PRD in the Chamber of Deputies and the Senate said a coalition of parties will continue to consult with the Fox administration to get a full commitment from the president to recovering the FOBAPROA funds. "If the president decides to engage in an open and constructive dialogue with the legislature, we will succeed [in recovering the funds]," said Pablo Gomez, PRD floor leader in the Chamber of Deputies. "If he maintains a distance from the Congress, then he may have many problems."

**Analysts say compromise likely**

Some analysts said the position of the banks has been strengthened by the two court rulings, which could force the federal government, Congress, and the four financial institutions to forge some sort of compromise. "Our base case is that the banks will absorb some loss, but that this will be small," said analyst Paul Tucker of Merrill Lynch. "The matter is highly political, and the politicians will seek a token victory at least."

At a press conference in late August, bank executives Othon Ruiz Montemayor of Banorte, Ricardo Guajardo Touche of BBVA-Bancomer, Manuel Medina Mora of Banamex, and Alexander Flockhart of Bital denounced the ASF report and reiterated their intentions to oppose a new audit, saying they have nothing to hide. "We oppose the reopening of the FOBAPROA contract," said Guajardo Touche. The bank executives, however, expressed willingness to work on a compromise. "We're completely open to looking for formulas to agree to a final and definitive audit," said Medina. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on Sept. 24, reported at 10.79 pesos per US$1.00] (Sources: Epoca, 06/02/03, 06/23/03; Agencia de noticias Proceso, 08/04/03; El Financiero, 06/05/03, 07/29/03, 08/01/03, 08/05/03, 08/06/03, 08/08/03; The New York Times, 08/08/03; Financial Times-London, 06/04/03, 08/17/03; Milenio Diario, 06/09/03, 07/31/03, 08/01/03, 08/05-07/03, 08/13/03, 08/20/03; El Sol de Mexico, 08/01/03, 08/20/03; Unomasuno, 08/04/03, 08/20/03; Reuters, 08/21/03; La Cronica de Hoy, 06/05/03, 06/17/03, 06/24/03, 07/30/01, 07/31/03, 08/01/03, 08/04-06/03, 08/20/03, 08/25/03, 08/26/03, 09/08/03, 09/15/03; Notimex, 07/29-31/03, 08/04/03, 08/05/03, 09/18/03; La Jornada, 06/11/03, 06/17/03, 06/18/03, 06/20/03, 07/29-31/03, 08/01/03, 08/05-08/03, 08/13/03, 08/20/03, 08/25/03, 08/26/03, 09/19/03; Reforma, 06/16/03, 06/17/03, 07/31/03, 08/04-08/03, 09/17/03, 09/20/03; El Universal, 06/25/03, 08/01/03, 08/05-07/03, 08/13/03, 08/18/03, 08/20/03, 09/05/03, 09/10/03, 09/18/03, 09/22/03)