COMMISSION OF ENQUIRY INTO

THE COLLAPSE OF FINANCIAL

INSTITUTIONS IN JAMAICA IN **THE 1990s**

SUBMISSION BY FINSAC

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BACKGROUND

1. In the 1990s, Jamaica's financial sector suffered a serious crisis. Several financial institutions failed and others received assistance from the State. The government at the time established four companies to manage the process: FINSAC Limited, Financial Institutions Services Limited ("FIS"), Refin Trust Limited and Recon Trust Limited.

2. FIS is the entity established by the Government in 1995 to take over the operations of the Blaise Financial Entities (BFEs) and a year later, it also took over the operations of the Century Financial Entities (CFEs), as both were experiencing liquidity and solvency problems.

3. FIS took over the operations of the BFEs and CFEs based on Schemes of Arrangement approved by the creditors/depositors and sanctioned by the Courts, whereby the depositors of the former were paid 90% of their deposits in four tranches over 18 months and depositors of the latter received 100% of their deposits in two tranches over six months.

4. Later, a detailed assessment of the financial sector was undertaken and it was determined that the liquidity and solvency problem was more widespread than initially thought. This was due largely to the practice of some entities within the sector using customers' deposits to acquire non-core assets. This had the double

effect of reducing liquidity and since some of the assets were not generating income and profits, eventually solvency was also affected.

5. Therefore, in January 1997, FINSAC (Financial Sector Adjustment Company) Ltd was established to intervene in the wider financial sector and a three-pronged approach was agreed, i.e, intervention, rehabilitation and divestment.

FINSAC's intervention

6. FINSAC's intervention was undertaken in the wider financial sector, i.e. life insurance companies, merchant banks, commercial banks and various connected companies/subsidiaries of these entities, by way of one or a combination of the following methods: acquiring shareholdings of or granting loans to or purchasing non-performing loans or non-core assets from, the various entities into which it intervened, injection of capital in some instances, appointment of boards/management, where necessary and developing and implementing plans for rehabilitation with the assistance of consultants engaged.

7. Due to its serious liquidity and solvency problems, the shares of the Workers' Savings and Loan Bank were in July 1998 vested in the Minister of Finance in exercise of powers conferred on him under the Banking Act and with the approval of Cabinet. FINSAC's managing director was appointed as his agent to manage the Bank on his behalf,

8, In August 1997 and May 1998, FINSAC established Recon Trust Limited (Recon) and Refin Trust Limited (Refin), the two companies which were used as the vehicles to acquire non-performing loans from various institutions, Recon was used for the loan purchase from National Commercial Bank (NCB) and Refin was used to purchase loans from Citizens' Bank and Union Bank. The Recon loans were assigned to Refin in February 1999.

9. In reviewing the lists of loans acquired from the various banks, it was determined that there were common debtors throughout the banks and thus FINSAC decided

to establish a Non-Performing Loan (NPL) Unit to manage the collection of these loans in order that a joint approach could be adopted for debtors with loans in multiple banks. The Unit's goal was to ensure maximum recovery of value for the distressed loans through a fair process which included uniform treatment of debtors with options determined by their particular circumstances.

10. Thus loans acquired from Century National Bank and Workers' Savings and Loan Bank and loans purchased from the Citizens' Bank, Union Bank and over-$5M loans from National Commercial Bank were transferred to the NPL, while it was decided that NCB would initially continue to manage collections of loans with principal balances under-$5M.

11. The American consulting firm, McKinsey & Company, was engaged to assist with establishing the NPL Unit. They recommended a database for the loans and a framework to value the loans based on four Cs, namely, Cashflow, Collateral, Contract and Character. These factors were applied to arrive at the Minimum Expected Recovery (MER) for each loan, which would guide deliberations with debtors.

12. The consultant also recommended that a Committee be established that would approve valuations of the loans to facilitate speedy action in recovery efforts. In this regard, in conjunction with the FINSAC / FIS Board, a Credit Committee was established, with requisite approval rights to receive, consider and approve submissions from the Credit Officers. The Standard Policies for NPL Work-outs were clearly stated in the FINSAC's Annual Report of March 2000,

13. Work-out Teams, consisting of five Credit Officers and a Credit Manager, were employed to undertake collection of the loans and these Officers interfaced directly with debtors. Based on the Officers' research of the files and discussions with debtors, submissions were then made to the Credit Committee for approval of various actions on accounts, including MERs, write-offs, sale of assets, legal action, etc. Where matters were perceived to be sensitive or beyond the approval

rights of the Credit Committee, it was referred to a sub-committee of the Board or the full Board for its deliberation.

14. The Credit Committee met regularly, initially on a weekly basis, and was chaired by the managing director, who was also a member of the Board. In his absence, the general manager for Asset Management & Divestment chaired the meeting.

15. The Board met monthly and as mentioned above some matters were sent to the Board for consideration/approval. While there was mention at one point that politically connected loans were to be submitted to the Minister of Finance/Cabinet for treatment, further research of the files revealed that at subsequent Board meetings it was decided that these debtors should be treated like all others and thus submissions for compromises should be made to the Board for consideration/approval.

16. An Oversight Committee was established based on a National Industrial Policy of the government. It required FINSAC to refer to this Committee, entities/individuals within the productive sector whose debts were acquired by FINSAC for consideration to be given to providing financial assistance in order that their operations could continue. A number of debtors was referred to this Committee but not much assistance, if any, was provided to these debtors based on the level of debt and liquidity problems.

17. It was ultimately determined that the best approach would be to sell the portfolio and in preparation, in October 2000, the NCB under-$5M loans were transferred to FINSAC to be included in the loans being prepared for sale. An American consulting firm, OCWEN Financial Corporation, was engaged for this purpose and it was also required to assist with marketing the portfolio. They prepared a database of the loans including balances, payment history and collateral.

The "Window of Opportunity"

18, Sometime in early 2001, a "Window of Opportunity" was announced by the Minister of Finance & Planning giving debtors up to March 2001 to make arrangements with FINSAC to settle their debts and take advantage of a compromise prior to sale of the portfolio. It was expected that a purchaser would honour these agreements providing the debtors were performing.

19. Many submissions were received by FINSAC during this period and from a report submitted to the Commission, 220 of these with total balances of J$4.1 billion were approved for J$2.5 billion write-off, with J$1.6 billion to be paid to FINSAC in full and final settlement of various debts over periods ranging from three to six months with a few getting further extensions to nine months. Sadly, only $306 million of this amount was paid, as some debtors did not honour the commitments and thus their loans reverted to the original balances and were sold as part of the loan portfolio to JRF. The ones who paid benefitted accordingly.

20. FINSAC's records show that some debtors ceased payment under the Window of Opportunity as they were awaiting the much-publicized sale of the portfolio in anticipation of a better deal when negotiating with the new owners.

21. Valuations were obtained for real estate held, i.e. both those securing loans and others acquired by FINSAC from the various entities as being non-core assets. These values were used by OCWEN in conjunction with FINSAC to arrive at an indicative value for the loan and real estate portfolios. Based on offers received for the real estate, it was decided to take these off the market.

22. Thereafter, the loans were marketed by OCWEN, and more than 20 institutions expressed an interest in acquiring the loan portfolio but due to activities in Kingston in July 2001 and in the United States in September 2001, some parties withdrew their interest, An agreement was reached with Beal Bank of Texas for

the sale of the loan portfolio and Jamaican Redevelopment Foundation, Inc. (JRF) was established as the vehicle to which the portfolio would be transferred. Dennis Joslin who was involved in the early negotiations, was engaged by Beal Bank as its agent to collect the loans and was also a party to the Loan Sale Agreement as Servicer.

23. An initial deposit of US$23M was paid by the purchaser, equivalent to 5.87% of the principal balances, with FINSAC sharing on a tiered basis from all future collections. As at September 2011, FINSAC was receiving 45% of collections, net of direct costs and has collected a total of US$72.5M, from the loans (including the US$23M).

24. As part of the agreement reached with Beal Bank when the loans were sold, another "Window of Opportunity" was announced in January 2002, whereby debtors whose primary residence was part of the security for the loan, could make special arrangements with Dennis Joslin Jamaica for a further compromise, with settlement being made over an agreed period. The evidence before the Commission is that a number of debtors benefitted under this arrangement.

Rehabilitation and Divestment

25. As part of the rehabilitation strategy, it was decided that based on the number of entities operating in the financial sector and the existing state of some of them in terms of liquidity and solvency, the only option available was for closure of some, with the transfer of their deposits to other entities controlled by FINSAC.

26. In fact coming out of this exercise, it was decided to merge a number of the small commercial banks and merchant banks to form Union Bank of Jamaica Limited (UBJ). These entities were Citizens' Bank, Workers' Bank, Island Victoria Bank, Eagle Commercial Bank, Eagle Merchant Bank and Horizon Merchant Bank,

thereby creating the `good' bank, while all bad loans were acquired by FINSAC. UBJ was later sold to RBTT Holdings of Trinidad & Tobago.

27. In addition the various life insurance portfolios acquired through FINSAC's intervention in the financial sector (Jamaica Mutual Life Assurance Society, Horizon Life and Dyoll Life) were transferred to Crown Eagle Life Insurance Company Limited and later the portfolio of all four entities was sold in 1999 to Guardian Life Limited.

28. FINSAC also provided financial assistance to Life of Jamaica (LOJ) and Island Life Insurance Company, the latter being a minority interest of only 18%, whereas the former was in the region of 76%. FINSAC's shareholding in LOJ was sold to Barbados Mutual Life Assurance Society, which has now changed its name to Sagicor.

29. The intervention process was completed by 2000 but rehabilitation continued beyond that as FINSAC's role was changed to supervision and monitoring workout plans of institutions that were assisted financially. It was envisaged that the life of FINSAC would have been seven years and indeed, by 2002, the primary mission was completed, as all major assets were divested and thereafter residual activities were being undertaken.

30. After the Credit Committee approves sale of loan-related properties, the necessary legal requirements were followed (demand, statutory notice and up-to-date valuation) and then these are sent by the Credit Officer to the Legal Department (Legal) which in turn sends it to an auctioneer from FINSAC's approved list for sale by auction. If sold, Legal prepares the sale agreement and funds received are sent to the Accounting Department (Accounts) and placed in an escrow account from which related sale costs are paid. When final payment is received, the cheque is sent to Accounts and a memorandum is sent to the Credit Officer with a Statement of Account of the proceeds. This amount is credited to the debt. If not

sold, Legal advises the Credit Officer, who then sends a memorandum with the relevant information to the Asset Disposal Unit (ADU) which had responsibility for disposal of all assets via private treaty, whether loan-related or others acquired as part of the non-core portfolio from the banks. All properties for sale were listed with approved Brokers to ensure transparency and they would submit to the ADU offers received for its consideration.

31. As a result of its intervention into the financial sector, a significant number of companies fell under FINSAC's control and because many of these were no longer trading (and some did not trade at all), they needed to be liquidated.

32. All the hotels acquired through the intervention were sold by 2001, UBJ was sold in March 2001, the loan portfolio was sold in January 2002 (and the staff who managed the loans were employed by the Servicer), NCB was sold in March 2002 and by June 2002, there was a further staff reduction, where all the senior staff left the company,

33. The residual activities included sale of remaining assets (mainly real estate), liquidation of companies, the records management exercise, liaising with attorneys on various litigation matters, accounting work for all active entities and addressing queries from various quarters from time to time. During the last nine years, there has been staff attrition, as the level of work remaining to be done continues to decline. It is expected that in the very near future, closure of the operations will be achieved.

34. In November 2007, the Finance and Administration Manager left FINSAC and in January 2008, the Operations Manager was upgraded to General Manager. In April 2008, the operations of FINSAC/FIS were relocated to the Ministry's property at Shalimar Avenue in Vineyard Town. The business of the various entities continues from this location.

The Commission of Enquiry and its proceedings

35. In October 2008, the new government established a Commission of enquiry ("the Commission") to investigate various matters arising from the financial crisis,

36. The Commissioners' terms of reference were extremely broad, but in relation to the operations of FINSAC, the Commission was mandated to

a. Review the operations of FINSAC in relation to the delinquent borrowers to determine if they were treated fairly and equally, and

b. To review the probity and propriety in FINSAC's management, sale and/or disposal of assets relating to delinquent borrowers.

37, In pursuing its mandate, the Commission made copious requests from FINSAC for records and documentation from the commencement of sittings in September 2009 including, but not limited to the following:-

- lists of entities intervened,
- copies of agreements between FINSAC and intervened institutions,
- list of loans acquired by FINSAC,
- lists of persons who reached compromises with FINSAC in terms of their debts,
- lists of assets which were held as collateral by FINSAC when the loans were acquired,
- valuations of assets held as collateral prior to disposal,
- information on rehabilitated entities,
- lists of loans which were settled at FINSAC,
- list of loans which were sold to the Jamaica Redevelopment Foundation ("JRF"),
- documents relating to the sale and/or assignment of the loans to the JRF

- Minutes of all Board and Credit Committee Meetings of FINSAC, and
- records and information relating to the debtors who appeared before the Commission.

38. Despite challenges in gathering all the requested information, the record will reflect that FINSAC complied with all requests made by the Commission for it to provide documents or information.

39. It is important to note for the purposes of these submissions, that evidence in relation to the operations of FINSAC were given by two persons- Mr. Patrick Hylton and Mr. Errol Campbell.

40. Mr. Hylton served as Managing Director of FIS from 1996-2002 and as Managing Director of FINSAC between 1998-2002, and then as consultant up to May 2003, while Mr. Campbell served as Operations Manager from the time of Mr. Hylton's departure until he was appointed General Manager for FINSAC in 2008, a position he still holds.

41. Mr. Hylton gave evidence before the Commission of FINSAC's evolution and operations as well as the principles and policy considerations which guided their operations and decision making up to the sale of the loan portfolio to the JRF.

42. Mr. Campbell was primarily relied on and required by the Commission to provide documents and data in relation to those operations.

43. It has been established in evidence in these proceedings that FINSAC acquired over 23,000 accounts, representing over 17,000 persons/companies properly categorized as delinquent borrowers.

44. Less than 20 persons of this total group appeared before the Commission to give evidence. Their complaints included - not having been communicated with by

FINSAC, not having received compromises similar to what some other persons obtained in terms of write-offs, properties allegedly sold by FINSAC for below par market value, inaccurate balances and even allegations of Fraud on the part of FINSAC.

45. [redacted]

There has been no evidence of fraud or evidence that FINSAC acted with impropriety with respect to any of the debtors who appeared before the Commission or any at all.

46. The evidence put before the Commission demonstrates that in relation to properties disposed of by FINSAC, recent valuations were obtained prior to disposal [redacted] No evidence of impropriety on the part of FINSAC was elicited before the Commission in relation to this entity.

47. Allegations were made by several persons that FINSAC sold their properties for a sum significantly below market value. The evidence presented by FINSAC has clearly demonstrated that those allegations are untrue. The Commission will recall that in respect of the complaint made by [redacted], the evidence showed that the property he alleged he wasn't given value for, was in fact voluntarily transferred by him to FINSAC in part settlement of his debt at a value both parties agreed. The Commission will also recall the complaint of [redacted] who alleged that FINSAC deliberately sold his properties below market value in a conspiracy with countless others to oppress him. Those allegations proved to be unsustainable and grossly inaccurate in the face of valuations and sale agreements put into evidence by FINSAC which proved that the properties were generally sold at market value.

48. Other complainants, such as [redacted], [redacted] and [redacted] failed to put forward any evidence of impropriety on the part of FINSAC and also failed to provide evidence to substantiate the allegations which they made. The evidence demonstrated that [redacted] encashed the very facility he claimed was still owing to him by FINSAC after it intervened in the operations of Corporate Merchant Bank, With respect to the complaint of [redacted], FINSAC's records demonstrated that the bid accepted by FINSAC for the assets of Island Broadcasting Services Ltd was the best offer on the table and received Cabinet approval. [redacted], and like many others, found that his allegations were not made out, In [redacted] case, the Court held that his case revealed no serious question to be tried.

49. There were two complainants, [redacted], who alleged fraud by their banking institutions. The evidence showed that FINSAC enquired into those allegations but found nothing to substantiate the claims. Furthermore, both persons commenced court cases in respect of their matters and in both instances, those cases were not decided in their favor.

50. The most common complaint was that FINSAC failed to correspond with persons- this was alleged by [redacted], [redacted], [redacted] and [redacted]. The evidence presented by FINSAC, including correspondence and Credit Committee Reports containing details of discussions between the debtors and their assigned credit officers from FINSAC, demonstrates that there was little truth in those allegations. The evidence adduced is that credit officers interfaced with these persons at regular intervals, provided updates (written and oral) of account balances and other account information and that FINSAC adopted an open-door policy in dealing with persons who were willing to work towards settling their outstanding debts, The evidence will also show that many of the promises made by persons who agreed compromised settlements with FINSAC were not kept and their accounts remained in default.

51. One issue which the Commission probed is whether politicians or other persons of influence received favorable treatment from FINSAC in dealing with their delinquent loans. [redacted] We submit that there has been no evidence put before this Commission which could lead to a conclusion that politicians or any other group of persons received favorable treatment from FINSAC in the handling of their loans. The evidence is that despite the number of accounts and persons, each case was handled on its own merits,

52. Although we have briefly made reference to [redacted] our position in relation to how the Commission should treat with his evidence is a matter of record,

53. [redacted]

Representation of FINSAC

54. Prior to the engagement of the law firm Samuda & Johnson, FINSAC was not represented at all hearings of the Commission. This was unfortunate because there was no response from FINSAC when persons made allegations against its

operations and its officers. The failure to respond immediately has created a gap in the public perception of FINSACs operations, which has not been easy to fill.

55. By the time Samuda & Johnson took over representation of FINSAC, the Commissioners made it known that they had long grown weary of FINSACs failure to respond to the allegations being made against some of its officers and operations. Counsel for FINSAC made several applications to be permitted to recall those persons who gave evidence against the institution, so that they could be cross examined. The Commission decided not to allow for witnesses to be recalled for cross examination by FINSACs attorneys.

56. The effect of that decision is that FINSAC was never afforded the opportunity of confronting those persons with documentary evidence which would demonstrate the fallacy in most of the allegations. [redacted] Because of its inability to address those complainants directly, FINSAC has suffered from negative publicity from the very beginning of these proceedings.

57. By the time FINSAC was permitted to make a presentation before the Commission responding to the complaints made, public interest in the proceedings and by extension media coverage had waned. Nevertheless, we submit that FINSAC's response exonerates it from any wrongdoing in respect of those who brought complaints to the Commission.

58, It is notable that very few, if any, of the persons who said they felt treated unfairly by FINSAC, expressed any personal responsibility for taking loans at interest rates which their earnings could not sustain, although the evidence presented in the course of these proceedings indicate this was often the route to delinquency.

59. There is also evidence suggesting that some of the loans granted during the period, including to some persons who appeared before the Commission, were not

properly collateralized. The negative impact on the institutions granting the loans and the resultant need for intervention by the government, is now a matter of record

Conclusion

60. Less than 20 persons from the thousands who were categorized as delinquent borrowers appeared before the commission. In most cases, the complaints against FINSAC were proved to be untrue. The Commission has not had evidence from persons whose businesses or homes were saved as a result of the intervention by the government or from persons who were able to pay off their indebtedness and continue to make positive contributions to the development of Jamaica society. The evidence presented before the commission by delinquent borrowers has been one-sided. We believe that the Commission ought to have put more effort into obtaining evidence from persons who benefitted from the intervention.

61. We submit that a careful analysis of the evidence presented before the Commission will show that FINSAC and its officers acted with probity and propriety in the management, sale and/or disposal of assets relating to delinquent borrowers. The evidence will also show that no preference was given to delinquent borrowers based on class, color, political affiliation or social standing. The evidence indicates transparency inherent in the systems put in place at FINSAC and the principles which guided decision making.

62. Having regard to all the evidence elicited, it is submitted that the Commission ought properly to conclude that FINSAC fulfilled its primary mandate to assist with the rehabilitation of the financial sector and that it has done so in an equitable and transparent manner.

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SUBMISSIONS ON BEHALF OF PATRICK HYLTON

(To the Commission of Enquiry Regarding Issues Related to FINSAC)

Introduction

1. The Commissioners were appointed pursuant to the Commissions of Enquiry Act to examine issues (the "terms of reference") identified in a proclamation from the Governor General dated October 24, 2008. In so far as Patrick Hylton is concerned, the terms reference that persons might consider relevant are as follows:

> *(ii) To consider what actions, if any, could have been taken to avoid this occurrence*[1] *and to evaluate the appropriateness of the actions which were taken by the authorities in the context of Jamaica's economic circumstances and in comparison to intervention by the State in other countries which have had similar experiences;*
> *(iii) To review the operations of FINSAC in relation to the delinquent borrowers and to determine whether debtors were treated fairly and equally;*
> *(iv) To review the probity and propriety in FINSAC's management, sale and/or disposal of assets relating to delinquent borrowers;*
> *(v) To review the terms and conditions of the sale of non-performing loans to the Jamaica Redevelopment Foundation. (sic.)*

2. Only those issues stated in the proclamation are relevant for the Commissioners' consideration. I submit that it is important that the Commissioners proceed on that basis, as the proclamation indicated to the Commission, those who appeared in the public hearings and the public at large what the relevant issues are. Consideration of any other issues would be unfair to those persons, as the

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1 That is, the collapse of several financial institutions in the 1990s.

Governor General by his proclamation would not have made persons aware that other issues were to be considered.

3. A responsible consideration of the issues would have to be on the basis of evidence, and not on speculation. Consequently, the comments in these submissions on behalf of Mr Patrick Hylton are presented on the basis of the oral and documentary evidence that has been presented to the Commissioners in relation to the above terms of reference.

4. These submissions are intended only to summarize some of the main points in respect of Mr Hylton, and to make submissions in respect of legal issues and any matters that may have arisen after Mr Hylton gave evidence. Primarily, Mr Hylton relies on the evidence he gave in his written statements of May 5 and July 4, 2011, and when appearing before the Commission in person in May and July, 2011.

(ii) ***To consider what actions, if any, could have been taken to avoid this occurrence[2] and to evaluate the appropriateness of the actions which were taken by the authorities in the context of Jamaica's economic circumstances and in comparison to intervention by the State in other countries which have had similar experiences***

5. In so far as the above term of reference relates to the actions that could have been taken to avoid the collapse of several financial institutions in the 1990s, it is not directly relevant to Mr Hylton, whose involvement (through Finsac Limited and its affiliated entities, referred to in these submissions collectively as "FINSAC") arose after the institutions in question had experienced financial distress. With respect to the appropriateness of the actions taken by the authorities, their actions included establishing FINSAC, and appointing Mr Hylton as Managing Director of Financial Institutions Services Limited (FIS, 1996-2003)

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2 *Ibid.*

and Finsac Limited (1998-2003). Mr Hylton was involved, through a task force, in the decision to establish FINSAC and was clearly heavily involved in the decisions taken by FINSAC at a senior level.

6. In respect of the manner in which the intervention in the financial sector was handled by FINSAC, the following facts, of which Mr Hylton gave evidence, are significant:

    a. The approach taken was consistently informed by available data and expert advice. The data, which indicated the level of financial distress experienced by the institutions, included information provided from the very financial institutions that were intervened. (See, e.g., paras. 22-23, 44 and 48-49 of Mr Hylton's May 2011 Statement.)

    b. Several of the financial institutions that were intervened had approached the authorities for assistance. (See, e.g., para. 24 of the May 2011 Statement.) All the intervened institutions were insolvent, and the debts purchased from them were non-performing and/or sub-standard. (Para. 33.) Many of the institutions' senior managers made repeated approaches for assistance. (Para. 43)

    c. FINSAC was subject to ministerial oversight, through the Ministry of Finance. (See para. 28 of the May 2011 Statement.)

    d. FINSAC had a publicly communicated mandate to protect depositors, policyholders and pensioners. While there was argument about the extent to which this group of persons should be "rescued" in an intervention, rescuing them is not unusual - as the experience in the US and Europe have shown. (See para. 32 of the May 2011 Statement.) Such a widescale rescue, in which bank depositors were able to receive 90-100% of their deposits, would obviously have significant implications for the country

which had to find the resources to fund the intervention. However, the potential consequences in terms (at least) of possible further erosion in confidence in the financial sector post-intervention threatened to be dire.

e. Several of the intervened institutions were rehabilitated and are now important players in the financial sector strong enough to weather the global financial crisis in 2008 and the Jamaica Debt Exchange programme in 2010. (See paras. 34 and 71 of the May 2011 Statement.)

f Several of the intervened institutions had strayed far from their core financial services activities, into a wide array of commercial activities in which they competed with their customers and for which their management had limited knowledge. [redacted] a former executive of National Commercial Bank, candidly admitted in his evidence *to the* Commission *that this may have* been *unwise.*[3] *A* consequence *of* these activities was that Finsac was left with a significant interest in over 200 companies that were operating in the real, rather than in the financial, sector. These interests required attention as part of the intervention, because (regardless of the wisdom of financial sector companies acquiring them) they formed part of the assets of the intervened institutions. An appropriate and key element of the strategy was to have an orderly and speedy disposal of the real sector holdings so that the focus of FINSAC could remain on the rehabilitation of the financial sector. (See paras. 36 and 57-59 of the May 2011 Statement, and paras. 3 and 911 of the July 2011 Statement.)

g. After a diagnostic exercise in 1998 involving FINSAC and its external consultants, which exercise gave detailed consideration to the scale of the problem and the approach that would be needed to address it, FINSAC's

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operations were reorganized to facilitate an orderly approach to the intervention. (See paras. 50-55 of the May 2011 Statement.)

h. **A key constraint for FINSAC was the absence of sufficient liquid funds to finance the intervention.** This made it difficult for FINSAC to meet the liquidity needs of the intervened institutions. FINSAC issued notes to intervened institutions in exchange for the purchase of nonperforming loans. However, with FINSAC not having the immediate funding to repay the notes, and having to pay interest on the notes with further notes, the notes were not liquid. (See paras. 60-61 of the May 2011 Statement.)

i. **The liquidity constraint represented a major hurdle for the senior management of FINSAC in its drive to rehabilitate the financial sector.** This constraint had the consequence that assets, such as real sector holdings and non-performing loans needed to be disposed of quickly. One option to this approach would have been to simply allow all the insolvent intervened institutions to undergo insolvency proceedings. Under that approach, depositors, policy holders and pensioners would have received a portion (for some institutions, a small portion) of the sums they had placed with the intervened institutions. This would have had significant negative implications for those depositors, pensioners and policy holders, and probably the future of the financial sector which was to be dependent on confidence being re-established. Another option would have been to fund the intervention to a greater extent from the public purse, which could ill afford it. Weighed against these options, the approach taken was a reasonable and responsible one. So far as Mr Hylton was concerned, based on the authorities' decisions as to the repayment of depositors, policy holders and pensioners, and the limited funding that would be provided to FINSAC, the options for FINSAC's senior

management were few. The approach they, therefore, took was appropriate in those circumstances.

j. Importantly, less than a decade after the crisis, stability had returned to the financial sector in Jamaica.

7. In the circumstances and given the constraints faced, it is submitted that Mr Hylton acted appropriately and sensibly in his stewardship of FINSAC.

(iii) *To review the* ***operations of FINSAC in relation to the delinquent borrowers and to determine whether debtors were treated fairly and equally;***
(iv) To review the probity and propriety in FINSAC's management, sale *and/or* ***disposal*** *of* ***assets relating to delinquent borrowers.***

8. Mr Hylton outlined in his evidence the fact that the approach FINSAC took in the handling of non-performing loans was based on a clear framework, a summary of which was publicized in Finsac Limited's 2000 Annual Report. (See para. 82 of Mr Hylton's May 2011 Statement and exhibit PH5.) FINSAC's preference was to negotiate a compromise rather than to resort to the uncertainties, delays and cost of litigation. (See, e.g., paras. 83-84 of the Statement.) Compromise was, understandably, preferred for those matters in respect of which FINSAC's management recognized that their position could be sustained in litigation. Thus, FINSAC was largely successful in those matters in which there was need to resort to litigation. (Para. 88 of the Statement.)

9. Similarly, compromise was preferred to the realization of security, (Paras. 83 and 113 of Mr Hylton's May 2011 Statement.) The approach of preferring compromise (on one hand) to litigation and realization of security (on the other hand) is consistent with that taken by most financial institutions seeking to recover outstanding loans from their customers.

10. In compromising claims, it is impractical to expect that all debtors will receive compromises with which they are happy and which are in all respects no more or less favourable to them than those reached with others. For one thing, borrowers come to the process with different circumstances, (See para. 114 of Mr Hylton's May 2011 Statement.) However, the use and publication of the framework makes it possible for persons to have some assurance that, at least at the senior management level, there was a consistent expectation (to the extent that there can feasibly be consistency among individual compromises) as to how nonperforming loans and debtors would be approached.

11. The writing off of debts was constrained by the fact that this would have increased the need for funding from the public purse -- that is, at taxpayers' expense. (See paras. 85 and 119 of Mr Hylton's May 2011 Statement.) Also, it had to be borne in mind that the debts had been purchased at par from the intervened institutions. However, this had to be balanced with FINSAC's need to obtain repayment quickly and, in those circumstances, to sometimes accept significant discounts on the amounts outstanding. Discounts also had to be considered where the quality of the documentation from the intervened institutions was found wanting. (Paras. 94-96 and 118 of the Statement.)

12. It is to be noted that the operations of FINSAC's Non-Performing Loans Unit were subjected to independent review by CIBC Canada, which generally commended the Unit on its activities. (Para. 82 of Mr Hylton's May 2011 Statement.)

13. An issue frequently raised in relation to the treatment of debtors has been why FINSAC continued to charge interest on loans that were not performing. From a legal perspective, FINSAC was clearly entitled to do so. The rights in respect of the non-performing loans were acquired by FINSAC through assignments of those rights from the intervened institutions (or vesting in the case of the

institutions intervened through FIS). Such assignments give the assignee (FINSAC) the rights that the assignors (the intervened institutions) originally had, including the right to continue to charge interest. (The position is similar with respect to the assets vested in FIS pursuant to vesting orders.)

14. As to the question of whether the charging of interest and pursuing full recovery were the right things to do, it is submitted that they were appropriate for the reasons described in paragraphs 99-114 and 128 of Mr Hylton's May 2011 Statement and paragraphs 17-23 of his July 2011 Statement. Paragraph 99 of the May Statement sets out the following considerations:

    a. *Firstly, it was important that persons who were holders of the debt acquired by Finsac be incented to come in and negotiate a settlement quickly. Continued interest accrual would represent a powerful incentive in this regard. It is important to note that the fact that Finsac accrued interest was no constraint on our ability to write back that interest as well as in some cases part of the principal in reaching settlement within our policy framework.*

    b. *The notes which Finsac issued accrued interest at market rates. These notes were used to fund the acquisition of the loans at their full book value. It was therefore also important that Finsac apply and collect interest on those loans when it was fair and equitable to do so. The rates charged by Finsac were also consistent with existing market rates and primarily at the lower end of those rates.*

    c. *To have stopped accruing interest would have the potential to create perverse incentives in the banking industry. It would be seen as unfair on the face of it to the customers who continued to pay on performing loans in both the intervened and non intervened banking sector. We need to*

always remember that even as Finsac managed non-performing loans, it also had a significant interest in existing performing loans in the 60-plus percent of the banking sector it controlled.

d. *Worse than that it could create a powerful incentive for borrowers to default particularly in banks that were controlled by Finsac, so that their loans could be sold to Finsac thereby giving them a break on interest accrual but creating worsening problems in the financial sector.*

e. *There may have been instances where persons were delinquent in one institution, but have significant resources in another institution, or invested in GOJ LRS, earning high rates of interest, whether in their own name or that of an entity they controlled.*

f. *Our experience also supported that continued application of interest could be beneficial as we on several occasions were able to collect some of this interest.*

g. *!f Finsac did not charge a rate commensurate with the market rate on the loans it bought, a delinquent borrower would be incented to sell assets and instead of paying Finsac, invest in GOJ paper and earn those levels of interest from the same government that bought his debt with an instrument on which the government was accruing interest obligations.*

15. In addition to its framework being publicly available, the opportunity for debtors to enter into compromises with FINSAC was well known and generally available to all debtors. Evidence was led, including by Mr Hylton (see para. 90 of his May 2011 Statement), in relation to the "window of opportunity" for persons to compromise their debts, that was publicized in 2001.

16. Mr Hylton's evidence is that there were in excess of 20,000 debtors whose loans were "acquired" by FINSAC. (Para. 130 of Mr Hylton's May 2011 Statement.) Jamaican Redevelopment Foundation Inc. ("JRF") put the number of loan *accounts it* acquired *from* FINSAC *at 23,530,* representing 17,459 borrowers.[4] Bearing in mind that some of the accounts acquired by FINSAC had been settled before the sale to JRF, the number of loan accounts originally acquired by FINSAC from intervened institutions would have been *well over* 20,000. The Commissioners, of course, should have available to them schedules of the debtors and can confirm the number acquired by FINSAC and the number of accounts sold to JRF.

17. Of the thousands of debts acquired and handled by FINSAC, the Commission has heard evidence from fewer than 20 debtors and, understandably, the evidence comes from those who believe they have a basis for complaint. This small number hardly constitutes a representative sample on the basis of which any general finding can be supported that FINSAC's senior management failed to properly manage the non-performing loan portfolio and treat with debtors fairly. The Enquiry concerns the wider, public issues in relation to the FINSAC experience, not how individual cases (which the evidence cannot establish to represent either practice or exception) were treated.

18. Further, of the debtors who gave evidence, an even smaller number provided evidence that can properly be taken into account. Evidence from several of them ought to be excluded from this analysis on the basis that their claims are or have been the subject of claims in the Supreme Court. It would not be appropriate for the Commissioners to reach a finding that is, or (in the case of claims not yet decided) might be, inconsistent with the findings of the Honourable Court, worse without the benefit of the full material provided to the Court.

Page 16 of the transcript of May 17, 2011 (Evidence-in-chief of Jason Rudd).

19. In asserting its claims for the debts outstanding, FINSAC used the balances that had been extracted from the intervened institutions' core systems as being outstanding. Mr Hylton's evidence given in July 2011 was that the institutions used reputable core systems, and the institutions were subject to annual audits by independent audit firms. There was generally no reason to question the accuracy of the information in the core systems, but where the balances were challenged by a debtor, such challenges were entertained. (See paras. 20 and 26-28 of Mr Hylton's July 2011 Statement.)

20. There were complaints that persons should have been more favourably treated for various reasons. [redacted],[5] for instance, sought to approach his matter through the auspices of his member of parliament, the [redacted]. It appeared that [redacted] and/or his attorney were of the view that on that basis, the matter should be handled by Mr Hylton personally and not by the persons in the Non-Performing Loan Unit who would have had responsibility for handling the matters of other debtors. [redacted]'s matter was, appropriately, referred to the Unit and so that it could be handled consistent with the process established to facilitate taking a consistent and unbiased approach (as described in para. 87 of Mr Hylton's May 2011 Statement).

21. [redacted] also complained that consideration should have been given to the fact that he was awaiting payment from the Ministry of Education. However, when one considers the principles, including the "moral hazard" problem described by Mr Hylton, primarily in his May 2011 Statement and oral evidence, this would not have been fair. It would have put [redacted] in an advantageous position as compared to borrowers who were being required to meet their obligations to private sector financial institutions notwithstanding

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5 See transcripts of March 16 and 31 and April 13, 2011.

obligations outstanding from the Government to those borrowers who had continued to perform on their obligations to those institutions. FINSAC, despite being formed by the Government, was a separate legal entity with its own mandate from the Government and obligations to satisfy (particularly payment under Finsac notes) from the recovery of debts in order to fulfill that mandate. In this context also, were a different approach to have been considered appropriate for persons who were owed by Government, that would clearly have required a decision by the Government, with appropriate funding to be provided to address the consequence of such a decision, and not by Mr Hylton and the senior management of FINSAC.

22. Finally on this issue, it is to be noted that despite FINSAC being Government-established, to the credit of the senior management, the evidence before the Commission establishes no pattern or even instance of more favourable treatment of politicians (regardless of their party affiliations) as compared to the treatment of other debtors. Following specific consideration of whether any additional process should be applied to debts owed by politicians, it was decided that there should be no different process and politicians' debts should be treated in the same manner as those of other debtors.[6] interestingly, the one politician who gave evidence as a debtor [redacted] was a member of the then ruling party, who complained of his treatment and confirmed that he had received no favourable treatment from FINSAC as a member of that party.'

23. In the circumstances, it is submitted that FINSAC's senior management established a framework that was appropriate and consistent in its approach. The evidence fails to establish that debtors were not fairly treated.

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6 *See* evidence *of* Errol Campbell *on* November 2, 2011 (Transcript *not* provided *at* time *of* writing).

7 *See* transcripts *of* July *14 and 21 and August* 4, 2011, *in* particular *pages* 91-92 *of* the transcript *of* July 21, 2011 (cross-examination of Dr Blythe).

***(v) To review the terms and conditions of the sale of non-performing* loans to the Jamaica Redevelopment Foundation. (sic.)**

24. In his evidence, Mr Hylton presented some key reasons why a decision was made to sell the non-performing loan portfolio that had been acquired by FINSAC. An examination of those reasons shows that they were good and legitimate bases for FINSAC to have proceeded as it did at the time. The reasons included concern that the holding of the portfolio by a public institution was (a) threatening efforts to maximize the value of the portfolio as an asset that needed to be used to fund the intervention and (b) prolonging the existence (and public expense) of FINSAC. (See paras. 130-139 of Mr Hylton's May 2011 Statement.) Ultimately, the sale of the portfolio became a condition of the World Bank and IADB providing funding the conversion of the FINSAC notes to Government of Jamaica Local Registered Stock. (Para. 140 of the Statement.) These reasons merely set the context, as the issue raised in the Governor General's Proclamation relates not to whether a sale of the portfolio was advisable at the time, but to the "terms and conditions of the sale" to JRF.

25. Clearly, a key issue relates to the price at which the portfolio was sold. Mr Hylton gave evidence that an assessment of the value of the portfolio had been conducted by independent consulting firm, McKinsey and Company, who had concluded that the net present value of the portfolio was only ten cents in the dollar if FINSAC took "urgent and aggressive action". (Para. 135 of Mr Hylton's May 2011 Statement.) This valuation was understandably kept extremely confidential as, had it been publicized, it would have affected borrowers' expectations as to what they should pay on their debts and negotiations for the sale of the portfolio. Regarding the question of why borrowers would not simply have been allowed to each pay 10% of the value of their outstanding loans, it should be noted that 10% represented an average, so if persons at the highest paid 10%, the average value realized would have actually been lower. (See para.

146 of Mr Hylton's May 2011 Statement.) Moreover, the net present value assessment was not an assessment of what all persons were legally obliged to pay, but of what FINSAC was likely to recover. By reason of its public funding and liquidity needs (as further developed in Mr Hylton's evidence, and in the submissions above on issues (iii) and (iv) of the terms of reference), it was *necessary for* FINSAC *to maximize recovery from the* portfolio, *whether through seeking payments from debtors or through the sale of the portfolio to another party.*

26. In the context of assessing the price negotiated for the sale of the portfolio, it is important that the public understand that the process of selecting a buyer was fair, competitive, public and transparent. It was no secret, in Jamaica or elsewhere, that a buyer for the portfolio was sought. The process involved advertisement in major international fora and the compilation of data in relation to the portfolio unto compact discs which were sold to interested parties. Mr Hylton insisted that the competitive process be the manner in which a buyer was selected. Approximately 20 expressions of interest were received from global institutions and local interests. (Paras. 141-142 of Mr Hylton's May 2011 Statement.) Beal Bank (which subsequently established JRF) was selected through the competitive process, after four other attempts to sell to other parties fell through. (Para. 143 of the Statement.)

27. Under the terms of sale, JRF was required to make an initial payment of US$23 million. This represented approximately 6% of the aggregate principal of the debts (estimated at US$380-US$390 million). While this represented less than the 10% net present value assessment by McKinsey and Company, it must be recalled that this was an initial payment agreed with JRF following a competitive process for selecting a buyer - in which, Mr Hylton said, there were bidders who felt that they should actually be paid to take the portfolio. It must also be recalled that the US$23 million *did not represent the price at which the portfolio was sold,* but simply the first payment on the purchase price.

28. The terms of sale included waterfall payments to FINSAC, under which FINSAC could continue to benefit from any "upside" in collections, to the extent that the collection efforts of JRF proved to be better than FINSAC had anticipated at the time of sale. The payments also provided an ongoing source of funding for an FINSAC, which had to be concerned with satisfying its obligations under the FINSAC notes and meeting its operational expenses, without significantly increasing the ultimate cost to taxpayers. (See para. 138 of Mr Hylton's May 2011 Statement.) Because of these waterfall payments, FINSAC continues to recover the purchase price, and the purchase price accordingly continues to increase under the formula prescribed in the January 2002 agreement between FINSAC and JRF. [redacted], testified that US$70 million has been paid for the non-performing loan portfolio by JRF pursuant to the agreement between JRF and FINSAC.[8] This represents approximately 18% of the aggregate principal of the debts sold, and with all debts not fully recovered, that percentage will increase. Indications from the recovery, therefore, are that the waterfall payments represented a wise position for FINSAC to have taken in the negotiations.

29. Given FINSAC's ongoing interest in JRF's recovery efforts, FINSAC negotiated the right to maintain a presence in JRF's offices, which was maintained subsequent to the sale. (See para. 145 of Mr Hylton's May 2011 Statement.)

Other* issues that *have Arisen

[redacted]

[redacted]

[redacted]

[redacted]

Treatment of intervened Institutions

32. During the course of the sittings of the Commission, questions were raised as to how various intervened institutions were treated, and in particular the reasons the intervention was not carried out in the same way for all institutions. It is not clear to what issue in the terms of reference such questions would relate. However, in paragraphs 62-66 of his May 2011 Statement, Mr Hylton explained how FINSAC

generally proceeded, and commented in particular on the question most often raised -- that of why some institutions were rehabilitated when others were not. This, he explained, was largely determined by whether rehabilitation was feasible (and even possible), based on "the state of the institutions, particularly the significant insolvency, their size and the composition of their balance sheet". (Para. 62.)

33. Two groups of institutions that were the subject of intervention and that were found to be seriously insolvent were the Eagle Group of Companies, that had been controlled by Dr Paul Chen-Young, and the Century Financial Entitles, that had been controlled by Mr Donovan Crawford. Notably, litigation in the Supreme Court ensued in respect of both of them, with FINSAC being successful in claiming that Dr Chen-Young and Mr Crawford (respectively) had acted negligently and improperly in their management of the entities. So powerful was the evidence against Mr Crawford that he was also found by the Court to have acted fraudulently, even though this had not been a part of FIS' claim! The activities of these gentlemen contributed significantly to the insolvency of the entities and the need for intervention.

34.In its public sittings, the Commission received evidence from Dr Paul ChenYoung, who complained of his treatment by FINSAC. However, his attempt to bring himself within the class of persons whose treatment is to be considered by the Commission was strained and cannot be supported by reasonable analysis. Dr Chen-Young's position, as found by the Supreme Court, was that of a controlling shareholder of companies in the Eagle Group. His complaints relate to his treatment in that capacity, not to the handling of his debts to the Group. In any event, any issues he might raise would be completely overshadowed by the significant liability, found by the Court, to the Eagle Group.

35. Dr Chen-Young's evidence confirms the insolvency that existed within his Eagle Group of Companies. However, the Commission need not (and perhaps should

not) rely on that evidence, but should instead accept the findings of the Supreme Court that the Group was insolvent. Again, the Commission ought not to trespass on the issues that have been ventilated in the Court proceedings. Suffice it to say that based on the evidence that was led before and accepted by the Court, intervention in that group was warranted.

36. In similar vein, evidence was received by Mr Donovan Crawford of the Century Financial Entities. His evidence is also to be disregarded by reason of the fact that he does not fall within the class of persons whose treatment is to be examined. He made no complaint of his treatment as a debtor. Moreover, whereas Dr Chen-Young has a pending appeal before the Court of Appeal, Mr Crawford has exhausted his appeals, having twice had appeals considered by the Judicial Committee of the Privy Council. These concerned the steps taken to intervene and his liability to FIS based on his fraudulent and negligent conduct of the Century Financial Entities. He directly challenged the decisions of the Courts in a manner that was contemptuous and any invitation to the Commissioners to accept his complaints may be considered an invitation to be complicit in the contempt.

37. Finally, as counsel representing Mr Hylton, I was denied the opportunity to cross-examine Mr Crawford following Mr Crawford's refusal to comply with the directions of the Commissioners regarding the conduct of his evidence. In those circumstances, even if the Commission does not agree that Mr Crawford's evidence should be entirely disregarded (which is my primary submission), at the very least, no finding that is in any way adverse to Mr Hylton can properly and fairly be made based in part or in whole on Mr Crawford's evidence.

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[9] See transcript of July 27, 2011.

Divestment of Assets

38. Yet another issue that had arisen, without apparently coming specifically within the terms of reference, related to FINSAC's divestment of the real sector assets it had acquired when intervening in the financial institutions that had originally acquired those assets. In paragraphs 64-73 of his May 2011 Statement, Mr Hylton described the process of divestment, which was a competitive process open to local and international bidders. He also noted that several of the real sector assets (in particular hotels) were sold to local persons, while observing that in a credible competitive process, one could not simply sell assets to persons simply because they were local. This clearly represented a reasonable and responsible approach to the divestment.

F/NSAC Representation

39. Finally, the extent of FINSAC's representation in these proceedings must be taken into account as any findings in relation to the senior management of FINSAC, and in particular Mr Hylton, are considered. Whereas counsel appeared for Mr Hylton at many of the public sittings - almost from the start and through to the end, FINSAC unfortunately did not benefit from similar representation. Instead, Mr Lackston Robinson and of the office of the Director of State Proceedings appeared as counsel for FINSAC on December 8, 2009, when Mr Campbell was scheduled to give evidence. Prior to that, there was no indication that FINSAC was represented, and afterwards, Mr Robinson attended a limited number of sittings.[10] Apart from when he later gave evidence with FINSAC having secured representation by a law firm, Mr Campbell, understandably, was not present for much (or perhaps all - the transcripts do not show) of the time after Mr Robinson ceased attending the sittings.

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10 The transcripts show that in late 2009 and early 2010, he (accompanied sometimes by Mrs Michelle ShandForbes) attended sittings at which evidence of Mr Campbell, Hon. Shirley Tyndall, Q.J (former chairperson of Finsac Limited), and Mr Robert Martin (current chairman of Finsac Limited) was taken. However, they were not present when the testimony of debtors (and many other persons) was given.

40. Thus, the persons who gave evidence of complaints against FINSAC were able to do so without being cross-examined by counsel for FINSAC equipped with such documentation as FINSAC may have had or been able to access in relation to their complaints. Eventually, toward the final stages of the proceedings,[11] the law firm of Samuda & Johnson was engaged to represent FINSAC, and Mr Brian Moodie and Ms Danielle Chai (primarily) began attending the hearings regularly. By then it was too late to effectively address or clarify many of the complaints made. The witnesses were not recalled, and their evidence accordingly not challenged in the way it otherwise might have been had effective representation been in place for FINSAC throughout the proceedings.

41. The concern that arises from the representation of FINSAC in the proceedings is its effect on Mr Hylton. He was involved in the day-to-day management of FINSAC as Managing Director in full-time, permanent employment up to June, 2002, and then as a consultant up to May, 2003. (Paras. 8-9 of Mr Hylton's May 2011 Statement.) In so far as Mr Hylton is concerned, a distinction must clearly be drawn between the activities up to May 2003 and those which occurred after that date. However, even in assessing the activities of FINSAC up to May 2003, account must be taken of the undesirable manner in which FINSAC's involvement in the Commission of Enquiry was handled. Mr Hylton could answer questions regarding individual complaints that were referred to him while at FINSAC based solely on his recollection of events that occurred 9 or more years ago (bearing in mind the period between the sale to JRF in early 2002 and when he gave evidence in mid-2011). At the time of giving evidence he did not, and reasonably could not, have had custody of the documents regarding individual debtor files. However, he could reasonably provide information and respond to issues regarding decisions taken at a senior level, but bearing in mind that this

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11 See page 2 of the transcript of May 3, 2011, when Mr Christopher Samuda attended and announced his firm's recent engagement to represent FINSAC at the Enquiry,

information and these responses were based primarily (again) on his recollection of events that occurred at least 9 years ago.

42, While it may be fair to hold Mr Hylton accountable for the policy and higher level decisions to which he would have been a party as Managing Director of FINSAC at the relevant time, it would be unfair and unreasonable in the circumstances to reach any adverse finding against him in relation to the specific complaints of debtors. He did not have the facts and documents to respond to most of their complaints, and those who ought to have put forward the facts and documents to challenge the complainants did not do so. This aside, as earlier submitted, with the small number of complaints relative to the number of debtors, there is not adequate evidence on which to make any general findings regarding the treatment of debtors based on the complaints received by the Commission.

Conclusion

43. In the circumstances, and having regard to the evidence, it is submitted that on the evidence it is appropriate for the Commissioners to find that Mr Hylton acted with integrity and in a manner that was responsible in his management of FINSAC's affairs.

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on behalf of Patrick Hylton

November 8, 2011