

VERBATIM NOTES
OF
COMMISSION OF ENQUIRY INTO CIRCUMSTANCES
THAT LED TO THE COLLAPSE OF THE FINANCIAL INSTITUTIONS
IN THE 1990s
HELD AT
THE JAMAICA PEGASUS HOTEL
81 KNUTSFORD BOULEVARD, KINGSTON 5
ON
TUESDAY, 24TH NOVEMBER, 2009

PRESENT WERE:

COMMISSIONER

The Hon. Mr. Justice Boyd Carey (Ret'd) MEMBERS

Mr. Charles Ross
Mr. Worrick Bogle

COUNSEL FOR THE COMMISSION

Hon. R.N.A. Henriquez OJ, QC, LLM

SECRETARY TO THE COMMISSION

Mr. Fernando DePeralto

MARSHALLING THE EVIDENCE

Mr. Ransford Braham - Attorney-at-law
Miss Kelly Wong - Attorney-at-law

REPRESENTING HON. OMAR DAVIES

Hon. Mr. Michael Hylton, Queen's Counsel
Mr. Kevin Powell - Attorney-at-law

REPRESENTING JAMAICA REDEVELOPMENT FOUNDATION

Mrs. Sandra Minott-Phillips - Attorney-at-law
Mr. Gavin Goffe - Attorney-at-law

REPRESENTING [REDACTED], BENROS LIMITED AND MICRO FINANCE
CORPORATION

Mr. Gayle Nelson - Attorney-at-law
Mr. Leighton Miller - Attorney-at-law

REPRESENTING [REDACTED] Mr.

Raphael Codlin - Attorney-at-law

1 November 24, 2009

1 CHAIRMAN: Good morning Mr. Chairman, good morning
2 Commissioners. We resume today to take
3 the evidence of Dr. Omar Davies, the
4 former Minister with responsibility for
5 finance and we are ready to proceed
6 whenever you are.

7 DR. OMAR DAVIES CALLED AND SWORN

8 CHAIRMAN: Perhaps you can indicate Mr. Hylton, who
9 are the counsel present and who they
10 represent if you don't mind. It's a
11 changing population.

12 MR. HYLTON: Yes, sir. Kevin Powell is with me
13 representing Dr. Davies. Mr. Kevin
14 Powell is with me representing Dr. Omar
15 Davies. Sandra Minott--Phillips and Gavin
16 Goffe are here on behalf of the Jamaica
17 Redevelopment Foundation. My learned
18 friend Mr. Raphael Codlin represents
19 [REDACTED] my learned friend
20 Mr. Gayle Nelson and Leighton Miller.

21 CHAIRMAN: Who is present?

22 MR. HYLTON: Mr. Nelson is present, sir, he has asked
23 me to indicate that Mr. Miller also
24 appears with him.

25 CHAIRMAN: I am asking if he is present.

1 MR. HYLTON: No, sir. They represent, sir,
2 [REDACTED] and his company, sir.
3 I think those are the counsel present at
4 this stage.
5 CHAIRMAN: Yes, thank you.
6 EXAMINATION BY MR. HYLTON
7 MR. HYLTON: Your name sir, is Omar Davies?
8 DR. DAVIES: Yes, sir.
9 Q And your address?
10 A XXXXXX, Kingston.
11 Q And you are the former Minister of
12 Finance and Planning?
13 A Yes.
14 Q Dr. Davies, the Commission has...
15 CHAIRMAN: Sorry, before you begin to deal with
16 questions which were put for response by
17 Dr. Davies, would you give the
18 Commission an outline so to speak of his
19 responsibility, status as Minister of
20 Finance, all that it entails, his
21 qualification, his whatever, so that we
22 can see him in a setting.
23 MR. HYLTON: To answer, perhaps I should start with
24 the period during which he held that
25 post?

1 CHAIRMAN: Of course, your main concern.

2 MR. HYLTON: Could you tell us when you were

3 Minister?

4 DR. DAVIES: I think there are legal terms; de facto

5 and de jure. I was Minister of Finance

6 de jure since from the first week in

7 December 1993 until the first week in

8 September 2007, but for a four-month

9 period before that I was a Minister

10 without portfolio. Before December 1993,

11 I was Minister without portfolio in the

12 Ministry but because I was not a member

13 of Parliament I could not sit in the

14 Lower House and be Minister of Finance,

15 so subsequently with the by-election, I

16 became Minister of Finance and Planning.

17 Q And could you tell us whether prior to

18 taking that position as a Minister

19 Without Portfolio, did you hold any

20 position in Government?

21 A On yes, well I held technical

22 positions, various technical positions

23 but the last one was between February

24 1989 and February or March 1993, I was

25 Director General of the Planning

1 Institute of Jamaica. Subsequent to that
2 I became a Senator but for a four-year
3 period I was Director General of the
4 Planning Institute.

5 Q Could you say a brief word, Dr. Davies
6 about your academic qualifications?

7 A I have a Bachelors from the University
8 of the West Indies and then I have..

9 CHAIRMAN: Sorry, in what discipline?

10 Q In Maths, Econ. and Geography from the
11 University of the West indies.

12 CHAIRMAN: Maths, Economy and Geography?

13 A Yes, and subsequently I have a Masters
14 and a Phd from North Western University
15 in Regional Economics; which is looking
16 at economic issues over space. This is a
17 follow-up on to the Geography over
18 space. I subsequently taught at Stamford
19 for a two year period, 1973 to 1975.

20 Q Taught what, politics?

21 A I have done a few lectures but not
22 taught. I taught Regional Economics at
23 Stamford University from 1973 to 1975
24 and then I returned to Jamaica in 1975
25 for my first stint at the Planning

1 Institute which was then the National
2 Planning Agency. I worked as -- I worked
3 under Dr. Gladstone Bonnick and
4 Dr. Norman Girvan.

5 Q And after that?

6 A After that I went to the University of
7 the West Indies as a Senior Lecturer in
8 the Department of Economics, this is
9 between 1981 and 1989. The Senior
10 Lecturer in the Department of Economics
11 and Senior Research Fellow in the
12 Institute for Social and Economic
13 Research, ISER, which I think has been
14 renamed as the Sir Author Lewis
15 Institute for Economics and Social
16 Research, it's now SALIESR. That was
17 1981 to 1989 and then 1989 to 1993 I
18 returned to the Planning Institute, this
19 time as Head.

20 Q Now, during the time that you were
21 Minister, perhaps if we could get a
22 brief outline of the areas that fell
23 under your responsibility?

24 A Well, it expanded. Initially I had the
25 traditional responsibilities for the

1 Minister of Finance which would be the
2 Ministry itself, taxation, the Central
3 Bank, the Planning Institute, the
4 Statistical Institute, Gaming, Caymanas,
5 and Betting Gaming and Lotteries
6 Commission and a variety -- Customs --- a
7 variety of other departments and
8 subsequently and I can't recall...

9 CHAIRMAN: As Minister of Finance then, fiscal
10 policy would be your area of concern?

11 A Well, all of the various aspects of
12 macro economic management would be my
13 area of concern but fiscal policy is
14 one.

15 CHAIRMAN: The reason why I asked is because being
16 very selfish our terms of reference are
17 concerned with fiscal and monetary
18 policies I want to ensure where you fit
19 into this?

20 A I would fit into this, I would be the
21 Minister with that responsibility, but
22 note policy for both, and subsequently
23 -- Chairman did I answer your question?

24 CHAIRMAN: Certainly.

25 A Subsequently, the issue, I had pointed

1 out to Prime Minister Patterson that
2 there were several decisions sometimes
3 taken in labour negotiations which had
4 significant implications for the fiscal
5 budget. I wasn't seeking to expand my
6 responsibilities, I just pointed out
7 that I often heard of settlements which
8 had significant fiscal implications
9 without being involved in it and his
10 solution was to give me responsibility
11 for the Public Service. So my
12 responsibility expanded when
13 responsibility for the Public Service
14 was also transferred to the Ministry of
15 Finance and Planning.

16 Q There are references in the Bank of
17 Jamaica Act, the Banking Act and the
18 Financial Institutions Act to the
19 Minister and those references I take it
20 would have been to the Minister with
21 responsibility for finance?

22 A Yes.

23 Q Which would have been you at the time?

24 A Yes.

25 Q Mr. Chairman, is there anything else you

0

1 wish me to explore?

2 CHAIRMAN: At the moment I can't think of one.

3 Q Dr. Davies, the Commission as you know
4 is enquiring into...

5 CHAIRMAN: Sorry, may I just before you get in, as
6 Minister of Finance, your aim would be
7 financial stability of the economy,
8 would it not?

9 A Yes, that would be one of the major
10 aims, but there are other aims.
11 Financial stability would be one but
12 there are several others; social
13 stability also.

14 CHAIRMAN: Both are our concern but since we are
15 concerned with the melt down, I want to
16 start from some base.

17 A Yes.

18 CHAIRMAN: Yes.

19 Q I was saying Dr. Davies, that the
20 Commission's terms of reference involve
21 enquiring into development in the
22 financial sector during the 1990s and
23 the Commission has asked you to respond
24 to a number of questions which I will
25 now take you through.

1

1 A Okay.

2 Q The first question asked, what options
3 were open to the Government to deal with
4 the financial crisis in the mid 1990's?

5 A Sir, there are a whole range but I had
6 summarized and suggested two, and then
7 you could have combinations or parts
8 from each of those. One would be to
9 treat each challenge, each crisis on a
10 case by case basis and appoint receivers
11 for the failed institutions and these
12 receivers would then dispose of the
13 assets of the institutions and pay
14 depositors in line with the ratio of the
15 amounts realized from the sale of the
16 assets to the liabilities which by and
17 large would be the deposits from the
18 citizens. That is one, and i say that
19 you can have a whole range of
20 variations.

21 The other one was to have a generic
22 intervention as was done with the
23 establishment of FINSAC and therein
24 rather than on a case by case you would
25 have an umbrella organization through

1 which the depositors, the holders of
2 insurance policies and also pensioners whose
3 funds had been compromised in this period,
4 where they would be protected. This latter
5 intervention as opposed to the first, came
6 with the clear understanding that the state,
7 the Government, would absorb the difference
8 or take responsibility for the
9 difference between the value of the assets
10 realized as opposed to the liabilities, so
11 in the first, you would simply intervene and
12 this has been done, whereby a receiver is
13 appointed, he or she goes in, takes total
14 command, sells the assets and then settles
15 with the creditors who would be by and large
16 the depositors as a percentage of the ratio
17 of the value of the assets as opposed to the
18 liabilities.

19 The second choice, and it was the one which
20 whereby you had a generic intervention
21 along the line of FINSAC, but that generic
22 intervention came with the clear
23 understanding that given that
24
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1 a problem existed, there is a difference
2 between the value of the assets and the
3 liabilities and that difference would be
4 met by the state.

5 Q I take it that the first option...

6 CHAIRMAN: Sorry, I don't think I heard clearly the
7 last part of your answer.

8 A Okay, the first option, whereby the
9 receiver would dispose of assets and
10 then settle with the creditors, the
11 depositors is the ratio of the value of
12 the assets realized and the liabilities
13 and the second, where is a generic
14 intervention with the clear
15 understanding that there is that
16 difference between value of assets and
17 liabilities but that difference would be
18 assumed, would be met by the state.

19 Q I take it that the first option would
20 involve the closure of institutions?

21 A Well yes, that's the whole nature, it
22 was an explicit recognition.

23 CHAIRMAN: That is the appointment of the receiver?

24 Q Yes, but he had said the first option
25 involved sale of assets?

1 A Yes, and as I said that has been done,
2 and that one would require the closure
3 of institutions.

4 CHAIRMAN: Excuse me.

5 COMM. ROSS: Sorry, I am not really very clear. At
6 the beginning you said that there were a
7 number of options but only two were
8 considered, am I understanding you
9 clearly?

10 A No, that's not what I said, Commissioner
11 Ross. I said there is a range. For
12 example, one could have taken a decision
13 to treat with some institutions with the
14 appointment of a receiver whilst in
15 other instances you would take the
16 decision to save the institution or you
17 could take the decision to do a
18 comprehensive resolution.

19 COMM. ROSS: It would seem to me that there were many
20 other options other than the two you
21 mentioned and even of the two that you
22 have mentioned there still are many
23 other options that could have been
24 pursued within those two options and the
25 second option that you say was followed,

1 within that option there were different
2 treatments for different institutions. I
3 am not really too clear about the
4 choices as you have told us.

5 A Well Commissioner Ross, I could
6 elaborate on a full range of
7 possibilities. What we are doing now is
8 looking retrospectively at events, but
9 what you are dealing with within that
10 context were events unfolding, not just
11 in terms of the challenges each
12 institution faced but in terms of public
13 reaction or even panic. Even to this
14 day I don't speak publicly even in
15 Opposition about certain issues because
16 one of the difficulties you face is how
17 to predict what will be a public
18 reaction or so. If, for example, and
19 God forbid, there is a mention of a
20 Securities Trading Institution with
21 which you may or may not be associated
22 being in problem, there is a difficulty
23 in stopping, in predicting what the
24 public reaction is and I have on various
25 occasions had to deal with intervening,

1 and I don't mean in a technical sense
2 but behind the scenes, just to allay
3 fears or to ensure that there is no
4 immediate erosion of public confidence.
5 So the answer I say to you is that I
6 could list and we could have an
7 extensive discussion on probably thirty
8 different options, but I have summarized
9 it in this regard because clinically,
10 you can have that discussion clinically
11 in a theoretical way, but faced with
12 actual events unfolding, and many of
13 which you can't predict or have any
14 control over, I have summarized these as
15 the two options.

16 COMM. ROSS: Well essentially these are the two
17 options that you considered given all
18 the circumstances?

19 A Yes.

20 COMM. ROSS: So that you would concede that there may
21 have been many other options that could
22 have pursued and could have been
23 considered?

24 A Concede would suggest that I would be

25 hesitant to accept that. I would

1 stipulate that there are many other
2 options but I am -- whilst I have made a
3 living from time to time as a lecturer,
4 this is not a theoretical discourse,
5 this was actually things happening.
6 CHAIRMAN: These are historical facts?
7 A Yes.
8 CHAIRMAN: So that looking back one can categorize
9 them, I would suppose.
10 A Yes.
11 CHAIRMAN: May I just say this? We are as the
12 Commission of Enquiry required, and I
13 quote from our writ, "...to make a full,
14 faithful and impartial enquiry into
15 matters specified in the Terms of
16 Reference, so we need to hear.
17 everything.
18 A Mr. Chairman, I could state for example,
19 that there are, in retrospect, there are
20 issues which we have reflected on should
21 we have paid people back principal plus
22 interest, or should we have prorated
23 depending on the size of your deposit?
24 These are issues, these are all options
25 which could have been explored, but,

1 even in the terms of ..

2 CHAIRMAN: I am sorry, that would relate to how you

3 are treating people.

4 A Sorry sir..

5 CHAIRMAN: I mean the question which we posed is,

6 "What were the options open to the

7 Government...? And as I understand what

8 you have said, from your perspective, it

9 is either appointing a receiver or what

10 you say is an intervention in the form

11 of FINSAC.

12 A Yes.

13 CHAIRMAN: These are your two broad....

14 A Yes my two broad, and I said that there

15 is a whole range on that spectrum. But

16 to follow the point, let's say we also

17 determine -- or one option is to say we

18 will give you fifty cents in the dollar.

19 That immediately changes the size of the

20 liabilities, that is another

21 possibility. The hindsight helps but it

22 doesn't capture the immediacy of the

23 situation in terms of the range of

24 issues which are before you. And I

25 would just like to indicate, for

1 example, if you decide to intervene in a
2 an institution, that exercise almost
3 became a military operation in the sense
4 that if an institution has a head office
5 and 15 branches, intervention meant that
6 first of all, you have to find personnel
7 unconnected to the institution; you have
8 to check whether auditors...
9 CHAIRMAN: It's a logistics problem?
10 A Much more than logistics, you know, sir,
11 you had to get things like locksmiths...
12 CHAIRMAN: I follow the logistics.
13 A Okay.
14 CHAIRMAN: Finding people.
15 A Finding people but...
16 CHAIRMAN: Acting like a commando raid.
17 A I wouldn't want to describe it in that
18 way, so the issue is that whilst we
19 could -- we can clinically speak of a
20 wide range of options, there are certain
21 objective realities which constrained
22 the options which could be followed.
23 COMM. ROSS: Dr. Davies, what we are trying to
24 understand is, what were the
25 considerations which led to the

1 decisions that you took.

2 MR. HYLTON: I have not reached to that question yet.

3 COMM. ROSS: We are just trying to understand what
4 your assessment of the situation was.

5 A Well, Commissioner Ross .

6 COMM. ROSS: If I could just finish, and the choices
7 as you saw them, so I think this is the
8 point.

9 A Commissioner Ross, our assessment and
10 analysis was aided by our consultation
11 with the multi-laterals. We consulted
12 with the IDB, the World Bank, the IMF,
13 both here and in Washington and to
14 summarise again, as I stated, their
15 recommendation would be the first
16 option. In a sense, they said the
17 market must work in a sense that banks
18 prosper and banks fail; the market
19 should work.
20 But part of what perhaps the Chairman
21 was speaking about, the logistics, they
22 even had a proposal of closing the
23 system for a two-week period to clean up
24 the mess.

25 CHAIRMAN: Sorry, all right I will not -- what we

1 are trying to you are going to come
2 to the question specifically about what
3 informed?
4 CHAIRMAN: So we are anticipating.
5 Q Yes, sir.
6 CHAIRMAN: The only question that he was answering
7 now, is what were the options as he saw
8 them, not...
9 COMM. ROSS: Actually the question was a little
10 broader than that, but, what we
11 understand him to be presenting to us is
12 the options as he saw them.
13 A The question is broader than what is
14 here.
15 COMM. ROSS: It says: What options were open to the
Government, and it could be argued that there were other options than
16 the two that were mentioned here and we have
17 already agreed that there are many
18 permutations and combinations within these
19 two options, but I think it was, first of all,
20 to understand what were the options, and we
21 do have a responsibility as the Chairman
22 mentioned to look at the broader picture. You
23 have
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25

1 other options however, and to inform
2 ourselves so that you know if, Dr. Davies,
3 it does happen again, he could perhaps be
4 broader in some of the approaches.

5 Would you wish the witness to then explore
6 what other options there might have been?

7 Q

9 COMM. ROSS: No.

10

10 Q

So might I go on

11

then?

12 A

Can I say something, sir? I am very much
13 aware of a full range of options and we
14 could, as I said I could have easily
15 have listed twenty but that is why I
16 deliberately in my response said two
17 main options, because after you seive
18 through I would argue and argue strongly
19 that these represented the two main
options available.

20 Q

I suspect that in the course of the
21 hearing, there will be discussions of
22 other options.

23 You have indicated Dr. Davies that the
24 Government chose the second option?

25 A

Yes.

Q Could you indicate to us why that was, what were the factors that motivated that decision? Well, let me start with a response to a previous question from the Chairman in that not only is a Government concerned about the financial stability, but the social stability and the second option was chosen because if you recall at that stage there was no deposit insurance scheme and hence whatever range of options you selected, if you decided that you put receivers in etcetera, a significant percentage of the population, those banking institutions or with their pension funds being managed by the insurance companies, would have lost, if not all, but a significant percentage of their life savings or their pension benefits or the insurance policies which they had. So at that level, there is both the impact on the financial system as well as social stability. And again, one could argue for ever as to are you certain that there would have been

1 chaos, but we had enough signs even for
2 small institutions, which would suggest
3 that that wholesale closure or allowing
4 to fail without protection would have
5 resulted in social instability.

6 CHAIRMAN: May I just interpose? I don't want to
7 forget the question. I was trying to say
8 that we have heard before about the
9 suggestion from one of the multi...
10 international people, about closing the
11 banks, we have heard of it but we have
12 so far not seen any paper where that was
13 actually suggested and we have been
14 supplied with a great many documents
15 from IMF and all the various people
16 around and somebody from the Bank of
17 Jamaica told us that, but we have never
18 been referred to the document from which
19 it said that specific proposal, it was
20 put forward in a specific proposal. Are
21 you aware of it?

22 A Yes, I am very much aware of it. 23

24 Continued

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1 DR. DAVIES: Mr. Chairman, the discussions with the
2 multilaterals were not -- well, to begin
3 with, we sought for private and secret
4 discussions with multilaterals and many
5 took place in Washington and we became
6 increasingly frustrated for several
7 reasons:
8 One is that we were keeping this, or we
9 were seeking to keep this confidential
10 and our first meeting was with the GOJ
11 team and one or two representatives from
12 the various institutions. By the time we
13 had got around to the fourth meeting we
14 had a room with people, a larger gathering
than is here now, and we realised that this couldn't happen but think
15 that we could keep the confidentiality within
16 that context. But furthermore, the advice we
17 received was one: Those institutions which
18 had to pay let them pay and in the process
19 of, in order to clean out the situation or
20 close the system for couple weeks and then
21 when you remerge you remerge with a clean;
22 a whole new structure with the
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1 new rules. I don't have my files; my
2 files aren't with me, but I do not
3 recall it being formally written but it
4 was in response to a question, "What do
5 you do in that period?"

6 CHAIRMAN: Yes.

7 MR. HYLTON: You were indicating Dr. Davies, the
8 considerations that led you and the
9 Government to choose a second option.
10 Yes. I didn't know the first in terms of
11 total erosion or almost total erosion of
12 the savings of -- and I define savings
13 broadly, not just actual deposits but
14 also your insurance policies; your
15 pension; whatever you had put away for
16 your pension. So I am defining it in the
17 case that Commissioner Ross seeks to get
18 me it to be totally technically correct
19 but I am defining savings in that
20 broader sense.

21 It was a gamble which the administration
22 had felt it couldn't take in terms of
23 social stability. We had evidence from
24 other countries --countries from South
25 America of what would happen when it

1 that there was no need to panic. Let me say
2 this -- obviously I won't indicate by name,
3 but even during that period of stability
4 from time to time there are
5 rumors about the institutions and as
6 Minister, I have had to have late night
7 meetings; weekend meetings to preclude
8 that; just to ensure that come Monday
9 morning there is normality. It's not
10 unique to Jamaica, the same thing
11 happened in the US recently where..

12 CHAIRMAN: I said hold that, but I just wanted
13 to whether insofar as Jamaica is
14 concerned, whether there was You mean
15 in America they had runs on banks,
16 people gathered and demanded their
17 money?

18 A You had situations sir, where
19 institutions; even within the interbank
20 settlement institutions would cease
21 lending to an institution and the
22 Central Bank would step in in such a
23 situation.

24 CHAIRMAN: I am going to go back. I didn't know it
25 was a run but if you tell me so.

1 A Mr. Chairman, could I say again, that I
2 saw part of my job and the job of the
3 Ministry of Finance sir, as to allow
4 normality to prevail even when there
5 were troubles behind the scenes. It's is
6 a major factor and it's something which
7 even in hindsight I am convinced is the
8 correct approach.

9 COMM ROSS: Just one question. Regarding option
10 one, was the proposition of guaranteeing
11 investors and others mutually exclusive
12 with that option one?

13 A No it isn't because even in instances --
14 well in a sense instances where we
15 assumed responsibility or said you may
16 go to institution 'x' with your papers;
17 your passport papers, you could at the
18 same time, put someone in to clean up
19 the mess in the existing institution.

20 COMM ROSS: So to some extent option one was used in
21 your judgement with a guarantee of
22 depositor's savings?

23 A Yes. The only challenge we faced
24 Commissioner, was that there were many
25 persons who thought that they were

depositors who actually -- and they may even have started as depositors but they found that there was a clause in their deposit agreement which said: "After three months I will offer you a Certificate of Participation and with the same interest rate, et cetera, and in several instances, and I could name institutions, persons had been transferred from being depositors to being investors not covered by us.

MR. HYLTON: And just to clarify. Would there be cases where there was a group of entities that invested with another entity in the group or the same group?

A It would often move them -- persons would have gone in to say Merchant Banks...

Q Which would be a deposit-taking institution?

A ...which would be a deposit-taking institution. And then there would be one of these complicated financial bonds sent out to people; I don't know how much people read them and in instances

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1 Pensioners don't have that opportunity. So
2 we also took the decision to deal with
3 pension funds and insurance policies. When
4 I use the word, I
5 presume you too, when you use the word
6 "depositors".

7 COMM ROSS: It's a broad term.

8 MR. HYLTON: Sir, that early answer made reference
9 to international credibility; the
10 credibility of the system that was why
11 the Minister I think, used depositors.

12 COMM BOGLE: Dr. Davies, we might come to it later on
13 but in order to have reduced the level
14 of eventual debt that the country had to
15 bear, couldn't we take deposit insurance
16 posture when we were paying our
17 depositors to say, to stratify it
18 whereby all deposits let's say up to
19 fifty thousand dollars would have been
20 paid? Because what we I am sure,
21 obtained were that there was some very
22 large depositors who were taking full
23 advantage of some very high interest
24 rates that eventually the public purse
25 had to bear.

1 A Yes. Obviously we would agree certainly
2 in terms of the cost but there was no
3 deposit insurance scheme, and that's one
4 of the reasons -- that was one of the
5 priority pieces of legislation and the
6 JDIC is now in existence and God forbids
7 a recurrence, but the formula which you
8 have now outlined is now there by law.

9 Q But what I am saying is, couldn't we
10 have done it although we did not have
11 the deposit insurance?

12 A Commissioner, the problem would be; you
13 would have to have had the panoramic
14 view; you had to have just sat with all
15 of those figures but all these figures
16 never came. The only time when we became
17 aware of them was when like put forensic
18 auditors in, et cetera, so we had a full
19 understanding of the size of the
20 problem. So I agree with you in a
21 conceptual way that we could have -- one
22 approach could have been to act as if
23 there had been a deposit insurance
24 scheme. But we also had the challenge
25 that having intervened in the Blaize

1 institutions and set a precedent there was
2 an issue of others being treated less fairly
3 and the lawyers also raised questions as to
4 given that you didn't have a deposit
5 insurance scheme bolstered by legislation,
6 what would be the basis on which you would
7 differentiate and how do you select a
8 cut--off point, at cetera. When you have a
9 deposit insurance law which then allows you
10 through Parliament to state the cut-off
11 points then it's a different situation. But
12 conceptually I don't disagree with you.
13 May I just find out. Of course we are being
14 perhaps wise after the event, I don't know.
15 CHAIRMAN: But if you are doing what is a now called a
16 'bail out' of the
17
18
19 institutions why can't you make your own
20 rules? Because you are doing something
21 that you are not obliged to do so you
22 can set out what you think are the
23 parameters of your assistance.
24 A The...
25 CHAIRMAN: Excuse me, may I just complete the

1 question? Because you state that you are
2 concerned and I have accepted, that you are
3 concerned about social stability, you didn't
4 want to cause social dislocation, a very
5 important factor would be a realisation that
6 there are some -- let me call them 'investors'
7 who were making money, a great deal of money.
8 These are persons who could bear the loss and
9 therefore it obliged you, the person
10 responsible for finance to
11 12 protect the more
vulnerable and not to
13 protect -- well, protect everybody
14 because takers couldn't bear it.

15 A Chairman, I you appreciate the point you
16 make but again, we benefit from not being
17 in the situation, one. But the second
18 point I would like to ask you to
19 consider is regardless of our assessment
20 as to whether them that got the wealth
21 can bear the loss you should also
22 accept and it's a cold and hard fact
23 that if them that got become displeased
24 or feel that you have treated them
25 unfairly they can do serious damage to

1 that very stability that you are seeking to
2 establish. It's an unwritten rule which
3 governs even how you treat with the foreign
4 exchange market et cetera, in the sense that
5 persons with wealth they are critical to any
6 notion of stability.

7 8 CHAIRMAN: I see. " To him
 that hath more shall be
9 given".

10 A That's precisely the point. "To him that
11 hath not" we ensure that he didn't loose
12 everything. (laughter)

13 COMM BOGLE: So I still though feel that there were
14 a lot of persons who stayed with certain
15 institutions getting very small interest
16 rates compared to some of the interest
17 rates that were being offered but in the
18 long run they are the ones that lose
19 out because they were getting very small
20 interest rates but had to now bear part
21 of the taxation to clear the debt which
22 was used to pay out a lot of investors
23 that were collecting quite handsome
24 interest rates. So isn't that a bit of
25 unfairness on the taxpayers?

1 FINSAC came in to the situation. Once the
2 policy decision was taken and the word FINSAC
3 -- the name FINSAC was Gladstone Bonnicks'
4 invention because we had been thinking of
5 something which strange enough had the
6 initials IRS and Gladstone, he felt that --
7 also, FINSAC was his creation but the
8 important thing was the orderly intervention
9 because you had this overriding body which
10 would then be in charge of the intervention
11 business. So people had a point of reference
12 whether local or foreign, to preserve the
13 stability of the system.

14 The second thing was that FINSAC was charged
15 with healing the system; the intervention,
16 repackaging of institutions; for example, a
17 set of institutions were combined as Union
18 Bank and then sold, which is now RBTT. And
19 third, it was through technical assistance
20 from the IDB in particular, it spearheaded
21 the revamping of the financial legislation;
22 the legislation

23
24
25

1 governing the financial system and part
2 of the problems arose from the laxity of
3 the legislation in parts.

4 Q There are some questions relating to the
5 establishment of FINSAC and the
6 financing and so on.

7 CHAIRMAN: One moment, please.

8 COMM ROSS: Dr. Davies, was any consideration given
9 to cost in choosing the options to
10 resolve the problems in the financial
11 sector?

12 A To what?

13 Q Cost. You have given us the major policy
14 objectives, the basis of which is
15 understable, but having set that as the
16 objective, was any consideration given
17 to cost and minimising cost and the cost
18 of rehabilitation?

19 A Yes, Commissioner Ross, yes. The
20 consideration was given but I do not
21 know of one instance where the initial
22 estimates of the size of the problem was
23 not significantly below what the
24 eventual results were. Dr Bonnick, who
25 was the first Executive Chairman of

1 2 FINSAC just expressed his amazement at what
3 4 has happened in terms of covering up the real
5 6 story. And people have asked about where was
7 8 the BOJ? The BOJ isn't in these institutions
9 daily, they do samples at cetera, in terms of
10 their audits. And so in every instance the
11 initial estimates provided by auditors or the
12 BOJ examination was far below what the
eventual cost turned out to be. And this was
before you had the issue of; as in one instance
where an auditor
13 was himself a bad
debtor in an
14 institution. You had situations of wrong
15 things being done in institutions which
16 were only fully revealed when we put
17 forensic auditors in.
18 COMM ROSS: Minister, I am sorry.
19 A I am responsible for what's going on,
20 Commissioner.
21 COMM ROSS: I mean there are a number of -- it
22 seems almost clearly the omnibus reasons
23 for that.
24 A For what?
25 Q For the escalated cost. The first one

1 being, that when you are compounding at very
2 high rates of interest whether you are rich
3 or poor the problems double in short order;
4 grow almost exponentially. So that the time
5 between the
6 identification of the problem and the
7 resolution just that passage of time alone
8 which might have been two to three years would
9 have doubled and more the size of the problem.
10 So that's one factor that is working and I
11 guess

12 later on we will
discuss the reasons

13 for the very high interest rates and the
14 long time that you introduced them. But
15 the other question I think relates to
16 the way in which institutions..

17 A No, what is the first question?

18 COMM ROSS: In other words, there is the impact of
19 environment on cost you know given the
20 fact that problems might have been
21 concealed, but even problems that were
22 identified, were growing very rapidly
23 because of the very high interest
24 rates.

25 A Are you finished?

1 COMM ROSS: Well, if you wish to comment.

2 A Commissioner Ross, I notice that you

3 almost handled the problems that were

4 concealed in passing but one of the

5 critical elements of a financial system

6 -- I mean the financial system is almost

7 unique. There is no other thing whereby

8 John Brown takes his life savings and

9 hands it across the counter to someone

10 and there is a notion that this person

11 is fit and proper and trustworthy, and

12 it would be very difficult to start

13 with the assumption that this person is lying

or has taken steps to conceal, et cetera. And you say it in passing

14 but it is one of the most critical issues

15 because even the delay to which you made

16 reference was occasioned by persons giving

17 firm undertakings that I am doing the

18 following or I am in discussions which are

19 about to be completed to introduce more

20 capital and it turns out that these were

21 concoctions and lies. So

22 I don't want

23 you to see the thing simply as the time has

24 elapsed but the

25

1 fact is that we were seeking in almost every
2 instance to try to heal institutions and
3 relied on the formal commitments -- the Band
4 of Jamaica can provide you with them; provide
5 by institutions as to concrete steps they
6 asserted they were taking only for us to
7 discover by and large that these were
8 figments of their imagination. So I don't
9 want you to labor under the impression that
10 we knew the full story and then delayed.
11 May I say this? We understood,
12 certainly from the Bank of Jamaica, that they
13 CHAIRMAN: were operating in a culture of
14 non-compliance. I suppose one could use
15 other terms to describe it. The Bank of
16 Jamaica was aware that they were dealing with
17 people who were doing exactly what you were
18 saying. So this is not something that came
19 as any surprise; they were well aware of the
20 environment, the culture -- they referred to
21 it as a culture. If this is a culture, this
22 is something that they are well aware of, 1

23

24

25

1 take it therefore, you would be aware
2 of.

3 MR. HYLTON: Mr. Chairman, let's me at least make a
4 point of clarity. Because the questions
5 are being asked "Were related the point
6 of time of which decisions were made to
7 choose an option and so on.

8 CHAIRMAN: I am not talking about that. What I am
9 talking about is FINSAC.

10 MR. HYLTON: You talking about how FINSAC was set up
11 and Commissioner Ross asked the question
12 whether consideration was given at that
13 point. I don't know Mr. Chairman,
14 whether the Bank of Jamaica's awareness
15 of the culture was at that point in
16 time. It needs to be cleared up.

17 COMM BOGLE: The Ministry got a number of forensic
18 audits done, were these post the
19 formation of FINSAC or previous FINSAC?
20 A Post, by and large. We brought in two
21 highly respected international
22 institutions, one out of Canada,
23 Lindquist Avey and one out of the UK.
24 Ernst and Young to carry out different
25 tasks.

[illegible]

4 DR. DAVIES: Well, I would say detailed in terms of -
5 these forensic auditors actually went
6 into day by day operations and revealed
7 to us some of the activities which were
8 carried out. If I should indicate, the
9 principal -- we had Lindquist Avey, once
10 they completed their major work, we had
11 them on a retainer and they voluntarily
12 gave it up because they felt that
13 criminal charges should be laid and
14 prosecuted almost immediately based on
15 the work which they had done but there
16 was, and I hazard to guess, there is
17 still a deficiency in terms of our
18 investigative capabilities in that area.

19 COMM. ROSS: I just have one initial question, which
20 is that the eventual whole approach to
21 the problem. One of the approaches that
22 has been used internationally is a more
23 gradual approach. It achieves the same
24 objectives of protecting depositors and
25 it deals with institutions that are

1 beyond hope, but essentially Its an
2 approach that deals more with the
3 workout of the problems, it's an approach
4 which is really not similar to option one
5 that carries with it a guarantee. It
6 certainly seems to us that the approach that
7 FINSAC took to resolving the problem, which
8 was to take on all the bad debts and resolve
9 them elsewhere, that that very approach
10 contributed and is still contributing to
11 the very high cost of the
12 resolution. What comments you could make on
13 that?

14 Well, in terms of the other possible
15 A: approaches, Commissioner Ross, I can't, I
16 don't want to sound repetitive but in terms
17 of the personnel to intervene for example,
18 in Workers Bank, took us, stretched us to
19 the absolute limit in terms of all the
20 branches, et cetera, and in a sense you have
21 to compare the problem you are facing with
22 your ability to effect a solution is related
23 to the resources you have. And I am not
24 talking

25

1 about money, not only about money, I'm
2 talking about the human resources to do this.
3 Again, this is almost like family funerals,
4 you are never that good at it unless you are
5 an undertaker that you know exactly what to
6 do, how best to approach it. We even in
7 retrospect, I think we sought, if there is
8 *one error*, which it's very clear in my head,
9 it is that we were struck with attempting to
10 work with the institutions -- there is one
11 institution, Century Financial, Mr. Crawford
12 never kept a single commitment given to the
13 Bank of Jamaica and when we took the decision,
14 this is the end, the group of local owners,
15 called themselves The Owners Club - Mr.
16 Fullerton from Caldon, Mr. Elon Beckford from
17 Horizon, Mr. Lindsay from Workers - they came
18 to us with a
19 proposal to create a 'good bank, 'bad bank'
20 and we thought they were going to introduce
21 capital et cetera, we thought that they were
22 close to a solution and then at the last
23 minute Mr. Crawford

24

25

1 said they were trying to steal his bank
2 and the whole thing collapsed. Now, if
3 you said to me, you should never have
4 trusted them in the first instance,
5 right, you are probably right and
6 perhaps my successors elsewhere should
7 take that lesson. Govenor Boussaires
8 told us, he said that he would be the
9 best person to advise us because he had
10 no emotional ties and he was able to see
11 the problem for what it was, but if you
12 ask me for an error it is that we
13 trusted them.

14 CHAIRMAN: Of course Workers Bank was a bank?

15 A: Yes, sir.

16 Q: Oh, the documents that we have suggest
17 otherwise but we will see.

18 CHAIRMAN: The documents so far reproduced and the
19 records show that it was insolvent from
20 almost its birth and money was pumped
21 into that bank, a great deal of money,
22 four point something billion dollars.

23 Q: You say the documents you have sir,
24 include the results of the forensic
25 investigations.

1 CHAIRMAN: Yes.

2 MR BOGLE: Dr. Davies, could we have approached, if

3 we had moved more quickly, could we have

4 ended up with a situation where we could

5 have avoided the need for all of the

6 human resources almost at once? Because

7 in talking to the Bank of Jamaica and in

8 the documents that we saw, we saw that

9 the Bank of Jamaica made reports and

10 recommendations from very early on one

11 or two institutions but nothing seems to

12 have been done on the face of it until

13 the situation really got into a very

14 very bad way and by then a number of

15 other institutions started or were

16 advanced on the road as well as. Had we

17 moved more quickly originally, would

18 that have eased the need for the

19 resource problem?

20 A: Commissioner, I disagree with the notion

21 nothing was done and you have access,

22 the Commission of Enquiry will have

23 access to the records of both the

24 Ministry of Finance and the Bank of

25 Jamaica, I don't know, but I am

1 indicating to you that you will see in
2 every instance a lot was being done but
3 we were seeking to avoid that ultimate
4 action to the extent which is possible.
5 And this is not unique to Jamaica,
6 sometimes you have to call it as we
7 did, but the first line of the approach
8 is to seek to work with the principals
9 assuming they are trustworthy, to find a
10 resolution.

11 You know, one of the interesting
12 developments in this whole matter is that these
13 owners, majority share holders who call
14 themselves The Owners Club, have somehow
15 managed to sell the notion to the nation or to
16 the country that they have been wronged and it
17 is, if I can contribute in anyway to this
18 Commission of Enquiry, I will invite you to
19 examine the full details of the inter--reaction
20 between the Central Bank and Ministry of
21 Finance and these owners so we can once and for
22 all put to rest that matter.

23 CHAIRMAN: Maybe you can help us to get them here. Well,

24 A: I thought you have those powers, sir.

25

1 Q: Oh, we have the powers all right, we
2 want the persons to come but we want
3 them to come voluntarily since they
4 were wronged. That would their sense of
5 grief if they indeed have been wronged.
6 A: Yes.
7 Q:: We have no powers at all ourselves, sir.
8 Mr. Chairman, there are some questions
9 which will follow, some of which use the
10 word 'capitalize' and some of which
11 refer to debt and funding. I take it you
12 are more interested in the latter, so I
13 need not go into the former,
14 capitalization.
15 A: Indeed, I thought that that was a little
16 off.
17 MR. HYLTON: I think that later answers addressed
18 the Commission.
19 Q: Was the public debts increased as a
20 result of the establishment of FINSAC
21 and to what extent?
22 A: Well, again sir, even the phrases, not
23 the establishment of FINSAC but the fact
24 that as part of the resolution the State
25 explicitly would assume the

1 2 responsibility for servicing the
3 4 difference between that which was garnered
5 6 from the sale of assets and the liabilities
7 8 so the public debts that's the only --
9 another solution clearly, which I should
10 indicate was reflected on a dismissed -
11 Commissioner Ross would be interested in
12 that -- you could have inflated away the,
13 you could have used the Central Bank to clear
14 some of these obligations and give them
15 useless paper over time but clearly that is
16 CHAIRMAN: only a superficial resolution which would
17 A: seem to diminish but down the road you would
18 pay the penalty.
19 That involved printing money?
20 Exactly. Essentially what the Central Bank
21 would do is make the advances unlike the
22 situation whereby the Ministry of Finance
23 CHAIRMAN: assumed responsibility for the debt that
24 would be dealt with differently.
25 I am sorry, Dr. Davies, I am going to take
you back it has occurred to me what we were
discussing, you were asked what

1 was the prime purpose of FINSAC, I just want
2 to return, if I may.
3 A: You are in charge sir.
4 Q: Now is my time. I understood having read in,
5 I think one of Dr. Bonnick's papers....
6 Yes, sir.
7 A: That FINSAC was intended to be
8 Q: temporary, let me use that word, five to
9 seven years, I think it was estimated. We
10 have gone now quite a period, have we not?
11 Well, yes, but I have a response, over ten
12 years.
13 A: Yes, sir.
14 And we certainly haven't achieved
15 A: healing, have we?
16 Q: Yes, sir. But can I answer you more
17 fully, sir?
18 A: Indeed.
19 In fact what has been achieved, what is left
20 Q: of FINSAC is like a rub, they have some real
21 A: estate or some minor things but the five to
22 seven years by and large, the five to seven
23 years timetable
24
25

1 was achieved, has been achieved. The
2 institutions, NCB was healed and sold;
3 Union Bank which was healed and sold,
4 the Financial Legislation has taken
5 place, has been put in place, the Fit
6 and Proper criteria have been
7 strengthened, the Deposit Insurance
8 Scheme has been established, the FSC has
9 been established; by and large the
10 objectives have been achieved.
11 Q:: But the debts haven't been collected,
12 have they?
13 A: Well, the bad debt portfolio was sold
14 sir.
15 CHAIRMAN: It's very bad healing.
16 A: With all due respect, Chairman, the
17 debts -- you have a crisis because you
18 have assessed that the debts cannot be
19 collected in totum.
20 CHAIRMAN: Have not and cannot.
21 A: Well, what you are seeking to collect is
22 as many cents in the dollar as possible.
23 MR. HYLTON: Which is of course why they are bad.
24 A: If they were all collectable debts owed,
25 one of the interesting things which we

1 discovered again is that the debts which
2 were not collateralized, like credit
3 card debts, they have been far more
4 successful in collecting those than
5 those which were ostensibly
6 collateralized.

7 MR. ROSS: You have been asked whether they were
8 secured?

9 A: Yes, ostensibly so.

10 MR. ROSS: So it must be possible to collect some
11 of those debts.

12 A: But they are collecting, they have
13 collected and they continue to collect.

14 HIS LORDSHIP: One of the complaints. sir is that their
15 debts are escalating, not just because
16 of the normal increase or arrears of
17 interest but because of the continuing
18 increase of the interest rate. So, if
19 the intent is to collect money I don't
20 know how it is thought that would you
21 achieve it that way.

22 CHAIRMAN: You mean, Commissioner, I think we need
23 to make a separation and distinction
24 between FINSAC and the activities of
25 the...

1 HER LADYSHIP: Other people.

2 A: Yes, and obviously they could speak for
3 themselves, but your specific question
4 was whether FINSAC hasn't gone way
5 beyond what Dr. Bonnick's first -- and
6 I am saying within the context of, if
7 you read Dr. Bonnick's first
8 Chairman/CEO statement in the first
9 report, he laid out clearly what the
10 objectives are and I think that his
11 successor achieved most of those
12 objectives.

13 CHAIRMAN: He wrote papers subsequent to departure,
14 many papers that is.

15 A: You mean Dr. Bonnick, and he has also...

16 HIS LORDSHIP: Storm in a Tea Cup is one I remember.

17 A: Well, and he also, and I hope that you
18 are going to have him before you sir,
19 because it would bring a sort of
20 perspective which is not subject to our
21 normal issues but he was also, he could
22 not believe some of these discoveries.
23 He just never thought that such things
24 were possible.

25 MR BOGLE: Dr. Davies, you mentioned that as one of

1 the achievements of FINSAC and the
2 closure or reduction in activities of
3 FINSAC, that the debts have now been
4 sold.

5 A: Yes, sir.

6 Q: Can you give us any information
7 regarding whether or not we have
8 collected on the sale, what is the
9 projection for us to collect on the
10 sale, can you give us information on
11 that?

12 A: There are details which FINSAC can
13 provide you. There is a formal
14 agreement in terms of initial payment, I
15 mean I could give you guesses, FINSAC
16 can just give you precise numbers and
17 everything has operated as per the
18 agreement. There is a payment at the
19 beginning and then there were payments
20 for the next 'X' million collected and a
21 percentage. That agreement to the best
22 of my knowledge has been adhered to and
23 even as we speak about that collection,
24 I think it should be noted that there
25 were local firms who initially indicated

1 an interest but felt that the percentage
2 being asked for by the government was
3 not realistic and dropped out of the
4 race. But, Commissioner, FINSAC can
5 provide you with full details. There
6 was a newspaper article which just
7 listed the conditions, et cetera, and to
8 the best of my knowledge they have been
9 adhered to.

10 MR. ROSS: Thank you.

11 MR. HYLTON: Back to the financing of FINSAC, Dr.
12 Davies. How was FINSAC financed in
13 terms of meeting those obligations?

14 HIS LORDSHIP: What question is that?

15 MR. HYLTON: It's question six.

16 A: In two ways. One, the first way, the
17 Ministry of Finance drawing on surpluses
18 which it had in the Bank of Jamaica
19 provided some funding in the first
20 instance and I presume you are speaking
21 about the period after FINSAC took firm
22 control. And the second way it was
23 financed is that it issued paper, FINSAC
24 bonds which were pieces of paper
25 guaranteed by the Ministry of Finance

1 and then when it got into operation in
2 dealing with some of debtors there were
3 inflows from payments made consequent on
4 settlement.

5 Q: The question I asked about the increase
6 in the public debts, how does that tie
7 in to the FINSAC bonds?

8 A: In the first instance we issued FINSAC
9 bonds which were essentially pieces of
10 paper, stamped, guaranteed by the
11 Ministry of Finance, such that John
12 Brown knew that this was as good as a
13 Treasury Bill or a long term
14 certificate. This meant that for a
15 period the value of those bonds or the
16 debts implied by those bonds were not
17 part the official debt stock. However,
18 once we reached the point of selling
19 the institutions, the repackaged
20 institutions, the purchasers demanded,
21 and rightly so, that we move from FINSAC
22 bonds to actual LRS, the government
23 paper, and at that stage you get these
24 spikes in terms of the increase in the
25 debts. So the debt was there being

1 accumulated via FINSAC bonds but you would
2 only have it officially recorded by the Debt
3 Management Unit and the Accountant
4 General's Department when we substituted
5 LRS's for FINSAC bonds.

6 Q: Do you recall the extent of the increase in
7 the public debt?

8 A: No, I have seen the question, I have not
9 checked the validity but it sounds more or
10 less within the range.

11 Q: Not the question suggesting of you. Do you
12 know what the extent of the increase was,
13 what percentage of GDP the intervention
14 accounts for?

15 A: I have seen estimates of 40% of GDP but these
16 are naturally estimates because you have
17 situation overtime, both the numerator and
18 the denominator changing but I would accept
19 the 40%.

20 Q:: Let us move Dr. Davies, subject to any
21 guidance of the Commission, to the question
22 of interest rates which were mentioned in
23 the course of earlier questions and
24 exchanges with the Commission. There were
25 between 1995 and

1 2000 for the various periods relatively
2 high interest rates...

3 CHAIRMAN: Excuse me. Since we
4 are moving to a new
5 area would this be a convenient time to take
6 a short break?

6 MR. HYLTON: As you please sir.

7 CHAIRMAN: We will take a 15 minute break Dr.
8 Davies.

9 A: Okay.
10 Break taken at 10:55 a.m.

11 On resumption at 11:15 a.m.

12 CHAIRMAN: May we resume. Mr. Hylton. Dr. Davies
13 you are still under oath.

14 DR. DAVIES: Yes, sir.

15 MR. HYLTON: Thank you Mr. Chairman. Dr. Davies..

16 CHAIRMAN: Before you begin, may I just make an
17 announcement. I understand that there are persons in the audience
18 who may have questions of the Minister. The Commission is willing
19 to allow you to ask him these questions but that will take place
20 after the completion of the questioning of his counsel, Mr. Hylton,
21 so at the appropriate time I will invite you. Thank you.

22

23

24

25

1 MR. HYLTON: We will now turn Dr. Davies, to the
2 question of interest rates and just
3 before the break I was observing that
4 during the period 1995 to 2000, and your
5 response was that there was a high
6 interest rate regime, let me use that
7 phrase. Could you indicate to the
8 Commission the reason, in your view, for the
9 interest rates as they were.

10 A: Let me begin by indicating that although the
11 Bank of Jamaica is not independent in the
12 legal sense, the previous administration
13 had taken the decision to allow the Central
14 Bank almost total latitude in terms of the
15 in determination of interest rate, so
16 interest rate policy was determined by and
17 large by the Central Bank, and I say by and
18 large because interest rate policy fitted
19 within the overall macro economic
20 programme. Well, currently we are
21 discussing this Letter of Intent to the IMF.
22 That Letter of Intent will essentially
23 contain a macro economic programme which
24 will speak to fiscal
25

1 deficit, revenues, the intertest rate
2 policy, et cetera, and the Central
3 Bank's determination of interest rates
4 was within such a context but that was
5 the responsibility of the Central Bank.
6 Q: There is a question here that indicates
7 some percentages of GDP which by which
8 the...
9 MR. ROSS: Have we finished with interest rates?
10 MR. HYLTON: Unless you have any questions.
11 Q: The question really was speaking to
12 reasons for high interest rates.
13 MR. HYLTON: I think it was said that it was a Bank
14 of Jamaica...
15 HIS LORDSHIP: Well, if that is his answer, the fact is
16 since the Bank of Jamaica was not
17 independent one would suppose that there
18 was some input by the Minister, when I
19 say Minister I include this, which is
20 your ministry. You understand me in
21 that sense?
22 A: Oh, yes, I understand you in that sense.
23 MR. HYLTON: I will proceed Chairman.
24 HER LADYSHIP: Yes.
25 Q: What your understanding Dr Davies,

1 2 especially given any input from your
3 ministry, of the reason for the high
4 A: interest rates?
5 Well, I go beyond. The Chairman's
6 7 introduction or his observation is correct,
8 it is not that this was outside of the remit.
9 If I may anecdotally indicate that apart from
10 official consultations, when I was Minister,
11 each Tuesday morning -- that's the day after
12 Cabinet, each Tuesday morning I met with the
13 Govenor the Central Bank, the Director
14 General of the Planning Institute and the
15 head of the FSC when it was establish and
16 Financial Secretary, et cetera, and within
17 that context we discussed overall macro
18 economic policy. So the interest rate policy
19 was consistent with what are the needs of
20 central government to finance the budget;
21 what are the objectives in terms of
22 inflation; what are the objectives in terms
23 of stabilizing the foreign exchange markets;
24 what are the objectives in terms of the
25 domestic

1 capital market? But in terms of the
2 actual calculations in terms of what
3 targets, et cetera, would be, that would
4 be the responsibility of the Central
5 Bank.

6 HIS LORDSHIP: You could answer the question, what was
7 the reason?

8 A: Okay.

9 MR. HYLTON: What were the reasons for this
10 particular period?

11 A: Well, at that particular period, one, with
the intervention ensuring stability within
12 the domestic financial system was critical
13 and stability in the domestic financial
14 system is twinned to stability in the foreign
15 exchange market. With a liberalized foreign
16 exchange market, if there are questions about
17 the domestic financial system or about the
18 overall macro economic programme, the
19 inevitable result with a liberalized foreign
20 exchange system is capital flight and one of
21 the critical positive results of the
22 intervention was that there was no capital
23 flight. You

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1 had movements from either weak or
2 perceived to be weak institutions to
3 strong institution. The Bank of Nova
4 Scotia was the major beneficiary of
5 that, but during that period it was the
6 determination that there was a need to
7 establish an interest rate regime which
8 would ensure stability in the foreign
9 exchange market and in the domestic
10 capital market. These were some of the
11 reasons.

12 MR. HYLTON: Yes, Mr. Commissioner.

13 MR. ROSS: During that period, interest rates,
14 lending rates averaged over 50%, deposit
15 rates or Bank of Jamaica rates were
16 probably over 40%.

17 A: Over what?

18 Q: Forty percent. How would a regime of very
19 high interest rates contribute to to
20 stability in a financial sector where a large
21 number of loans or a large percentage of
22 loans are going bad and companies are
23 becoming insolvent? How does a high interest
24 rate regime foster stability in that
25 environment?

1 A: As you would be aware, although I know you
2 from your various public utterances, you and
3 I differ in terms of the importance of
4 stability in the foreign exchange market,
5 but that is a critical element to us in
6 maintaining stability in the overall macro
7 economy, stability in the foreign exchange
8 market. But Commissioner, I invite you to
9 examine the record of some of our
10 institutions. Unfortunately, most of them
11 foreign own and managed during the same
12 period, in that they did not have the same
13 level in terms of bad loans during that period
14 and I think it is too simplistic a notion to
15 have this cause and effect between the
16 interest rate regime, because it is not a
17 unique situation within the Jamaican context
18 in terms of the interest rate regime and
19 failure of businesses, et cetera. Clearly
20 there must be an impact, but at the same time
21 there are financial institutions which not
22 only survived but remained stable and were
23 not beneficiaries of the FINSAC
24
25

1 intervention.

2 MR. ROSS: From some of the reports that we have
3 read, bad loans, delinquent loans were a
4 major part of the problems in
5 institutions.

6 A: Yes.

7 Q: And the institutions that failed, and
8 looking back there were really only two
9 commercial banks that were are not
10 affected one which really didn't do an
11 awful lot of lending and the other which
12 was I think the bank of the government.
13 Again, you know, I understand the policy
14 objectives of protecting depositors, but
15 I am trying to understand how a high
16 interest rate regime which is
17 contributing to the problem, it may not
18 be the only factor but certainly was a
19 significant factor, how maintaining that
20 regime could have fostered, helped to
21 foster stability? (11:25 a.m.) 22

23 Continued. .

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1 DR. DAVIES: Mr. Commissioner, let me respond. First
2 of all just a point of correction. You said
3 two institutions, there are
4 actually three and I could name them if
5 you wish.

6 CHAIRMAN: By all means.

7 A Well, ENS, CIBC and Citibank. I
8 think
9 you forgot one, I don't know which you
10 forgot, but just a point of correction.
The second point though.

11 CHAIRMAN: One moment, please.

12 A Yes.

13 COMM. ROSS: The information that we have from the
14 Bank of Jamaica is a little different
15 from that.

16 A That what?

17 Q The institutions that you mentioned one
18 of them was in fact assisted by FINSAC
19 through that whole intervention. I don't
20 know whether it was FINSAC but one of
21 them was in fact assisted by the Bank of
22 Jamaica.

23 A Well, I would wish to be, I have to be
24 appraised of that.

25 MR. HYLTON: Indicated by Bank of Jamaica during the

1 course of this enquiry?

2 COMM. ROSS: Yes, a report that we have from them.

3 Q I don't recall that.

4 COMM. ROSS: We have it in the table. It was one of

5 the first documents that we received.

6 Trafalgar Commercial Bank I think was

7 the other institutions that was not

8 affected, it was the other Commercial

9 Bank.

10 A With all due respect I would have to be

11 shown that document.

12 demonstrate the somewhat simplistic notion

13 between high interest rates and

14 banking problems. Ir

15 important than the issue of interest rates are

16 management practices which have people

17 making loans which should

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1 never have been made and people
2 concealing bad loans and taking actions
3 which bad management practices. So
4 Commissioner, I would never ever suggest
5 that high interest rates are good for
6 business, but I am suggesting that the
7 notion that high interest rate, that is
8 the problem, is somewhat simplistic.

9 COMM. ROSS: Dr. Davies, since you mentioned current
10 events the responses in almost all
11 jurisdictions to problems in their
12 financial sector recently has been to
13 lower interest rates to historical lows.
14 So I think that there obviously is the
15 recognition that high interest rates...

16 A That wasn't my point Commissioner. My
17 point Commissioner, is that seeking to
18 establish high interest rates as the
19 causal factor is faulty, because I am
20 speaking that these countries were
21 experiencing -- prior to their recent
22 crisis they were experiencing interest
23 rates which we can only dream about,
24 low interest rates. Your introduction
25 of the fact that their various

1 approaches including their stimulus
2 packages would have included lowering
3 interest rates is a separate issue.

4 COMM. BOGLB: Dr. Davies, I agree with you the fact
5 that generally interest rates is one of
6 those tools which are available to
7 protect the exchange rate. However,
8 what I think is our major problem in
9 Jamaica was the sustained high interest
rates that we had.

Not

10 spike, but then when the interest rate is
11 moving from, let us say, in the teens to the
12 sixties, I would venture to say that I don't
13 know any business that would be able to manage
14 that type of interest rate without
15 faltering. So the interest rate as a tool to
16 protect the foreign exchange, I understand,
17 but where I think that we have the biggest
18 problem was the length of time that we had;
19 as a matter of fact it still
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1 obtains even today where we have this
2 high interest rate policy.

3 DR. DAVIES: Commissioner, I don't how many ways I
4 could say it, is that I am not an
5 advocate of high interest rates and I am
6 not suggesting that high interest rates
7 are good things. What I am saying, you
8 will have to view the interest rate
9 policy within a context. And
10 Commissioner this is not a hypothetical
11 question, this is a real question and it
12 may be more real than you even think
13 even now. One of the worst things which
14 can happen is when a Government puts out
15 an offer with an interest rate which it
16 believes is appropriate and supportive
17 of industry or whatever --the
18 Trinidadians have an expression, "you
19 call a fete and no one comes." When you
20 put out an instrument and nobody buys
21 it, that sort of crisis -- so it's not
22 that anybody wishes to have high
23 interest rate just to be punitive, but
24 in the mix of things there is also the
25 issue of ensuring stability but also

1 that the needs of Central Government to meet
2 its obligation are met and these are some
3 of the factors which go into the
4 determination as to the interest rate
5 policy. So I don't want us to get into a
6 pointless discussion that I am for high
7 interest rates.

8 administration is
for low interest rates

9 but interest rates are almost twice what
10 obtained when I left office. So simply
11 saying I am for or against is not an
12 issue. What is the issue is the context
13 within which this interest rate is
14 determined.

15 CHAIRMAN: I don't think anyone has suggested that
16 you are for it. I don't think anybody
17 here in this room is saying that you are
18 for it.

19 A My apologies, sir.

20 CHAIRMAN: But high interest rate is definately a
21 factor?

22 A Yes.

23 CHAIRMAN: You are not suggesting that and I
24 haven't gotten the statistics at the
25 moment. I don't want to be inaccurate

1 but you aren't suggesting that because
2 some banks were within this culture of
3 noncompliance to use a very **parochial**
4 term that that is what caused the
5 collapse?

6 A I am not suggesting that, sir, at all
7 Mr. Chairman, but what I am not
8 suggesting but stating as a fact is that
9 the forensic audits which were carried
10 out and which should be available to you
11 would reveal practices which would,
12 well, probably help to turn my hair
13 gray.

14 CHAIRMAN: The question for us would be the extent
15 of the practice. I don't recall at the
16 moment the precise figure of failed
17 banks. A large number of banks failed,
18 but I don't know if the majority of
19 those banks were guilty of this
20 noncompliance culture.

21 A I would think so.

22 CHAIRMAN: You would think they were?

23 A Yes.

24 COMM. ROSS: I just have to ask. Sir, we were
25 presented with information from Bank of

1 Jamaica suggesting that a large number
2 of institutions that failed were really
3 very small when compared to the overall
4 systems and in fact there was a very
5 large local institution that was
6 intervened which probably accounted for
7 50% of the cause of the intervention.
8 That institution was allowed to continue
9 operating and I presume that that would
10 not have been done if that institution
11 was guilty of major transgressions. So
12 I think that while we can accept that
13 management practices were a factor, I
14 think the evidence before us certainly
15 suggests that the economic environment,
16 and in fact later on I think we will
17 deal with that, the economic environment
18 was a major factor and for the
19 institutions that failed the high
20 interest rate policy was perhaps the
21 greatest challenges they had to face.

22 DR. DAVIES: Well, Commissioner I wouldn't wish to
23 suggest that your analysis is guided by
24 your initial beliefs, but I will invite
25 you to access the forensic audits which

1 are available which would speak to those
2 issues. As regards to one institution to
3 which you made reference in that instance the
4 issue was not that of corrupt practices but
5 that insitution became involved in planting
6 oranges, planted papaya, a whole range of
7 things and you really get into a culture
8 where your farm manager is being paid by the
9 bank manager and these diversions were
10 critical factors and these I also term as bad
11 banking practices and it is one of reasons
12 in addressing the subsequent legislation we
13 have spoken to the range of activities in
14 which a deposit taking institution can
15 become involved. So I am not for any one
16 moment and I don't want us -- clearly I am
17 here and guided by the Chairman and the
18 Commissioners but I don't want us to -- I am
19 not suggesting high interest rates is not a
20 factor but I am saying that the issue of
21 illegal practices as well as bad management
22 and banking practices these are to me the
23 critical issues.
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1 CHAIRMAN: Let me understand this, you have used
2 the word illegal. Are you aware of any
3 criminal prosecutions that were initiated?
4 I don't know if it would be by the Bank of
5 Jamaica or whoever, are you aware of any?
6 I am aware of instances where the forensic
7 DR. DAVIES: auditors have presented the case and for one
8 reason or another there has not been a follow
9 through. Let me deal with the other reason.
10 In certain instances we have been advised
11 by the lawyers we have case which we believe
12 we will win, but in that process given the
13 length of the time in the justice system all
14 the issues; disposal of assets, et cetera,
15 would be put on hold during that period and
16 bearing in mind our objective of trying to
17 clear our way through we have to sometimes
18 make judgment calls in that regard and there
19 were negotiated settlements in that regard
20 I am aware.
21 Mr. Chairman in relation to your last
22 question, would you wish him to attempt

23

24 Q

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1 to elicit specific answers and names
2 because -- I don't if you want to?

3 CHAIRMAN: You see I merely ask if he is aware of
4 any criminal prosecutions and the answer
5 is not really. They were not taken for
6 any reason.

7 MR. HYLTON: I may be able to assist. I don't know if
8 you wish me to go there.

9 CHAIRMAN: Very well.

10 MR. HYLTON: Do you recall, Dr. Davies, whether any
11 of the principals of the Blaise
12 Financial Institution were prosecuted?

13 A Yes.

14 Q You recall if any of the principals of
15 Caldon were prosecuted?

16 A Which one?

17 Q Caldon?

18 A I believe so, I am not certain but I
19 believe they were.

20 CHAIRMAN: Sorry, you paused, I mean two out of?
21 MR. HYLTON: Two, that I am aware of, sir.

22 CHAIRMAN: Yes.

23 MR. HYLTON: May I continue, sir?

24 CHAIRMAN: Please.

25 Q I am about to move on so something else

1 I don't if there is anything else on
2 interest rates you wish to address or I
3 should go on.

4 CHAIRMAN: For the moment I suggest you go on.
5 MR. HYLTON: Question 9 asked, "What was the reason
6 for the public debt rising from 124% of
7 GDP in 1997 to 144% of GDP at the end of
8 1999? "

9 DR. DAVIES: I'll have to accept the valuator's
10 figure. I have not personally checked
11 them, but the major reason would be --
12 I have described before the financing of
13 the operations of FINSAC through the
14 issuance of FINSAC bonds. Whenever an
15 institution was sold or divested then
16 the FINSAC bonds were converted to GOJ
17 debt or LRS so you would get these
18 spikes, so for example when RBTT
19 purchased Union Bank then we had to
20 substitute government bonds --
21 government debt formally for FINSAC
22 bonds. Similarly when NCB was formerly
23 sold to AIC the same occurrence.
24 A All this was necessary in order to
25 effect the sales?

1 Q Oh, yes. The truth is a FINSAC bond was
2 a piece of paper with a stamp of a
3 government that the government can't --
4 but the institutions wanted something,
5 something which was formally from the
6 central government, from Ministry of
7 Finance to be particular.

8 Q Ultimately it was a cause for
9 intervention?

10 A Yes.

11 Q Insofar as?

12 CHAIRMAN: Sorry, I am being ignoramus here. But
13 It had value?

14 A Which one, FINSAC bonds?

15 CHAIRMAN: Or the government paper?

16 A Yes and people traded it. But in terms
17 of the -- I will say international
18 recognition clearly Government of
19 Jamaica, former Government of Jamaica
20 paper was a preferred instrument.

21 COMM. ROSS: Did these bonds pay interest?

22 A Yes.

23 Q In cash?

24 A No. Well, it depended on what the cash
25 flow of FINSAC was in terms of its

1 divestment proceeds and so FINSAC from
2 time to time had cash which they would set
3 off and so they would do partial payment
4 with cash and partial with FINSAC bonds.
5 Insofar as financial institutions were
6 MR. HYLTON: 7 concerned, Dr. Davies, was a distinction
8 made between those that had liquidity
9 problems and those that were insolvent? Yes,
10 A always. But you should accept or you should
11 understand that that distinction relied on
12 the data available to the inspectorate of the
13 Central Bank and virtually in every case it
14 was discovered that either the level of the
15 size of the bad debt portfolio or whatever
16 or the size of the performing loans
17 portfolio one was understated or one was
18 exaggerated. So there are clear
19 instances when the revelation of the size
20 of the problem came only after
21 the intervention. This was even more so
22 in the instances where you had the group of
23 companies because what was done is what they
24 call evergreening of loans.
25

1 So Company X, the deposit taking
2 institutions would make a loan. It's
3 not performing and in anticipation of a
4 BOJ inspection that loan would be sold
5 to another entity which was not subject
6 to the same inspection, so you have a
7 clear up of loan in the books of the
8 deposit taking institution, but within
9 the overall group of companies that bad
10 loan was there and continued not to
11 perform and that knowledge both because
12 of the restricted legislation as well as
13 the fact, that is the fact that the
14 interventions hadn't taken place that
15 knowledge in many instances was not
16 something available to us.

17 Q I thought Commissioner Ross had a
18 question.

19 COMM. ROSS: I understand the size or the issue of
20 size but to the best of my knowledge I
21 think the question is trying to address
22 the difference or the quality, in other
23 words the insolvency versus liquidity?

24 A Yes.

25 Q Was there an early determination that

1 some of these institutions were
2 insolvent?

3 A Or approaching insolvency unless steps
4 were taken and in those instances --
5 Commissioner, let me just indicate that
6 from our position the first order of
7 business was to seek to heal
8 institutions and if you were working
9 with persons whom you assumed, logically
10 you would assume...

11 CHAIRMAN: Who want to be healed?

12 A Yes, but there are persons who gave firm
13 undertakings, persons who - Mr. Crawford
14 on various occasions spoke of new
15 investors who have been identified and
16 who were that close to bringing new
17 capital in and it turned out to be
18 fictitious, but judge us for perhaps
19 not being overly suspicious, but the
20 reality is what do you do if the
21 principals in a financial institution
22 give you firm undertakings et cetera, do
23 you a priori assume that they are lying.

24 CHAIRMAN: It shouldn't be naive though?

25 A In retrospect you are correct, sir, we

1 have no quarrel.

2 COMM. ROSS: I just wanted to make sure that the Bank

3 of Jamaica Inspectorate had been

4 examining institutions all along and I

5 presume that they would have made

6 reports as to the solvency or insolvency

7 of institutions. I can understand the

8 difficulty of resolving the problem once

9 you make that identification. I am just

10 trying to get an understanding as to how

11 early in the game BOJ would have made

12 those reports and the response that

13 would have followed?

14 A Well, certainly I am most acquainted with

 that, in regard to that with the central financial entities. In fact,

15 I gave a full report to Parliament on the total

16 history of our interaction. So in that regard

17 I was fully informed, in that regard. But we

18 also in seeking to heal that to move out Mr.

19 Crawford, we also responded positively to the

20 overture from the group of persons -Mr.

21 Crawford, Mr. Lindsay, Mr. Beckford, Mr.

22 Fullerton. For some reason I don't

23

24

25

1 think Dr. Chen-Young was in it but they
2 called themselves the Owner's Club and they
3 came up with a proposal as I indicated which
4 blew up and perhaps it was a good thing they
5 6 blew up because I don't think there was much
7 8 substance, in retrospect, and in reality
9 there was not much substance in it, but the
10 point I am making Mr. Ross is that nothing
11 was being done and that paper I can make it
12 available to you through the Honorable
13 Michael Hylton. I gave a full report to
14 Parliament so it is not that I am saying
15 anything that was concealed but it is
16 extremely difficult to deal with persons who
17 later on we found out not only they operated
18 like a group of companies and they moved
19 around problem loans within that group too
20 and much of that we discovered after the
21 fact.
22 As regards the Bank of Jamaica
23 Inspectorate, These are spot checks, they
24 are not living in the institutions as you
25 would know and one of the problems when they
wished to prolong

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Q

MR. HYLTON:

COMM. ROSS:

1 MR. HYLTON: In BOJ taking action, I am just saying
2 that high interest rate was not one of
3 them.

4 COMM. ROSS: Yes, I am just trying to understand the
5 circumstances that would have led to the
6 delays which have obviously compounded
7 the problem?

8 A Can I help, Commissioner? I gave an
9 address to Parliament on July 16, 1996
10 concerning the Century financial
11 entities and it detailed the rationale
12 for what you call the delays. We were
13 operating in good faith, we were seeking
14 to avoid the situation of a collapse of
15 institution.

16

17 If you say in retrospect you should have just
18 hit them and move them out you are perhaps
19 correct but I am not saying anything I
20 haven't said thirteen years ago. I detailed
21 all the interventions, all the meetings --
22 one of the problems we were running people
23 ragged because we never summoned anybody to
24 the Ministry of Finance in daylight for
25 obvious reasons. We were meeting late at

night et cetera, just seeking to

1 intevene, but I have provided in that
2 address to Parliament full details of the
3 Century financial entities and we could
4 do the same for several of the
5 other entities.

6 CHAIRMAN: May I just ask a question. We have a document
7 from one of these agencies written to, I
8 believe, Governor of the Bank of Jamaica,
9 who were suggesting that what the Government
10 should get the administration to do is to
11 take prompt and urgent action against what
12 they call financial laxity and they use a lot
13 of nice words not complimentary to our
14 system and they were told, we understand,
15 that the government could not take any action
16 because of political and logistics reasons.
17 I am not sure that he said the
18

19 Q Government any at all. His question 44
20 says?
21

22 A Commissioner I have no difficulty in
23 dealing with the question now.

24 CHAIRMAN: Very well, let me see if I can find the
25 -fiscal laxity.

1 Q It's in the November 1996 report.

2 A 44, question 44.

3 CHAIRMAN: Am I running ahead of things?.

4 MR. HYLTON: He said he is quite prepared to deal

5 with it now, sir

6 CHAIRMAN: I don't want to take you out of your

7 order of things. This is what

8 anticipated from the question. Question

9 45. The IMF in its letter of November

10 27, 1996 stated. "It has been our

11 experience that no resolution strategy can

12 be successful in restoring a financial

13 system to soundness in the absence of a sound

14 macroeconomic framework that is consistent

15 with achieving a sustainable and low rate of

16 inflation as well as external viability.

17 Jamaica's policy mix of fiscal laxity,

18 monetary restraint, and exchange rate

19 stability is, in our view, not consistent

20 with achieving such macroeconomic

21 objectives". That was the question which I

22 have anticipated?

23 I must confess -- Chairman, I'll answer that

24 A one too but I must confess that I

25

1 thought you were asking question 44.

2 CHAIRMAN: In light of what he was answering I just
3 thought I would ask. Well I don't mind
4 which one you want to answer it's all
5 the same. If you find it convenient to
6 answer now you may do so and at the
7 appropriate time you deal with what you
8 want to deal with.

9 MR. HYLTON: In relation to the statement the
10 Chairman just read do you agree with the
11 assessment?

12 A I just want to be clear which question
13 you are asking.

14 Q The statement 45 "No resolution
15 strategy."

16 A I am in agreement with the first sentence of
17 that assessment. It would be impossible to
18 disagree with you that what it has outlined
19 are a set of contradictory policy
20 initiatives. I don't agree with the second
21 part of the assessment. In fact, if you note
22 the Government agreed, the then
23 administration agreed with the first part.

24 If you note several of the steps
25

1 which were taken by the administration
2 following the intervention of FINSAC,
3 Jamaica for several years, I don't know what
4 its present situation is now ranked, had
5 one of the highest primary surpluses
6 anywhere in the world; we were over 10%.

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8 Continued. .

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