The crisis of the Bankgesellschaft Berlin (BGB)

Ulrich Rippert
20 June 2001

In the last week in May, the announcement that the losses of Berlin's largest banking house—the Bankgesellschaft Berlin (BGB)—added up to more than four billion marks unleashed a shock in the general population. At the beginning of the year, the Berlin state government (Berlin has the status of one of the *Länder*, or federal states and controls 56.6 percent of the BGB shares) was relying on deriving a dividend of 135 million marks from the bank's operations in 2000.

The news magazine *Der Spiegel* spoke of the "greatest banking crisis in post-war German history" and stressed, "as opposed to the failure of Herstatt in the mid 1970s, till now the largest bank insolvency, this time it does not involve any elite private bank. The future of the most powerful banking house in the capital is in the balance, a bank with which half of all Berliners have an account, and which finances large-scale projects like the Lausitzring, the restoration of old parts of Berlin or building the planned airport at Schönefeld."

Politicians of all persuasions tried to mollify the situation and referred to the fact that the Berlin state government, which is the principal shareholder of the ailing bank, delivered a " *Patronatserklaerung*" ("public letter of support") and thus provided an unlimited endorsement for the further business activities of the bank. But this transformed the banking crisis into a crisis of Berlin's state government, the Senate.

Berlin's state government is already burdened with 65 billion marks of debt and has to find 12 million marks every day just to service the interest payments. New debts accrued by the city this year will rise from 3.6 to 9.6 billion marks. *Der Spiegel* went on to comment, "This will cause social conflicts on an undreamt-of scale, the consequences of which are regarded as fearfully by the ruling grand coalition [of Christian Democrats and Social Democrats running the Berlin Senate] as the Christian Democrats once feared socialism on the other side of the Berlin Wall."

Recent statements by prominent Berlin Social Democrats imply they were completely surprised by the extent of the financial crisis.

But the hasty withdrawal of the Social Democrats (SPD) from the Senate coalition, and the attempt to dissociate the SPD from the financial machinations of the Christian Democrats (CDU), cannot hide the fact that the SPD was well informed about all financial dealings and transactions and were directly involved in them. Until February last year, SPD politician Annette Fugmann-Heesing, in her function as finance senator, sat on the supervisory board of the BGB.

In the post-war era, eight of Berlin's mayors have been SPD members. The present incumbent Eberhard Diepgen (CDU) has been a mayor for almost 14 years, first in the Berlin Schoeneberg district and then for the city as a whole, but two-thirds of his time in office has been in a coalition with the SPD.

To expect the Social Democrats to clear out the financial sewers of Berlin is tantamount to expecting Beelzebub to drive out the devil.

The cry: "stop thief!" and the vocal accusations being made against CDU nepotism are directed above all to divert attention from the SPD's own dirty dealings and blunt increasing indignation in the population. While Eberhard Diepgen and his CDU party colleague of many years Klaus Ruediger Landowsky have been trying to justify the criminal machinations of the past, the Social Democrats hope that nobody remembers that they also stuffed their faces at the troughs of power during the last years.

Rarely has the close intertwining of business and politics, with the accompanying unrestrained enrichment of party officials and their political favourites, become so clearly visible. As in a kaleidoscope, this banking crisis reveals the corruption and nepotism in all colours of the political spectrum.

The BGB was formed in 1994 by unifying several Berlin credit institutes formerly controlled by the Berlin state government. At that time, the CDU/SPD coalition in the Senate boasted that the BGB, floated on the stock market, was unique in German banking, and not only served to strengthen Berlin as a banking centre, but also was aimed at carrying through a "trend-setting structural policy" in the city and its environs.

The largest single BGB shareholder is the Berlin state government (56.6 percent), 20 percent is held by the north German state bank NordLB, 7.5 percent belongs to the Gothaer insurance company (Parion) and 18.4 percent of the shares are in smaller holdings.

With a balance sheet of almost 405 billion marks in the first quarter of the current year, the BGB is the largest financial company in Germany's capital city. The BGB owns a series of finance houses, including the Landesbank Berlin, the BerlinHyp building society as well as a number of smaller banks like the Weber Bank and the Allbank. The various BGB enterprises employ 16,000 workers, but it is expected up to 3,000 will be dismissed by the end of the year due to the crisis. The BGB operates about 2.5 million private customer accounts and about 800,000 business accounts.

The financial problems of the BGB, which are now impacting on the finances of the Berlin state government, were mainly caused by risky real estate deals. This includes a 600 million mark credit from BerlinHyp to the Aubis real estate company. With the money, Aubis, whose dubious enterprises were disputed from the start, bought up concrete apartment blocks in East Berlin and other areas of the former German Democratic Republic to renovate and re-let. The business failed because the renovated apartments were too expensive and remained empty. The Aubis management were never made to account for the failure; the financial risk was carried by BGB and now falls on the shoulders of the general population.

Although the lost Aubis millions were only the final straw, this case reveals the special mixture of Berlin's special brand of nepotism and corruption.

The boss of the BerlinHyp was none other than one Klaus Landowsky, who was also the leader of the CDU parliamentary group in the Senate. The banker Landowsky agreed a 600 million mark line of credit, without the usual collateral and checks, to the two managing directors of the Aubis real estate company, whom the politician Landowsky knew all too well.

They were not just businessmen but old CDU colleagues, who had sat alongside him for many years in parliament.

From 1984 to 1990, Klaus-Hermann Winhold belonged to the CDU's Berlin state leadership and his Aubis business partner Christian Neuling represented the Berlin CDU in the *Bundestag* (federal parliament). Neuling is not completely unknown to the public prosecutor's office. He was investigated in 1985 on suspicion of selling waste oil as fuel oil. But Berlin public prosecutor's office soon dropped all its proceedings against the prominent CDU politician.

In 1991, Neuling sat on the supervisory board of the Treuhand—established to oversee the sale of all East Germany's former state-owned assets—and was chairman of the *Bundestag*'s Treuhand subcommittee when he was suspected of committing fraud. His company received properties and credits from the Treuhand on extremely favourable terms. Once again, Neuling denied everything, but resigned less than two weeks later as chairman of the parliamentary Treuhand subcommittee; and the investigation was shelved.

At the beginning of this year, the Federal Banking Supervisory Office conducted a special audit of the BGB. As a result, it came to light that in 1995 Klaus Landowsky had personally received a CDU party donation of 40,000 marks in his executive office at the BerlinHyp and had not recorded the transaction correctly. The donors were Winhold and Neuling from the Aubis real estate company, who "shortly thereafter" were granted the 600 million mark credit by the BerlinHyp. According to the auditors' comments published so far, "unprofessional and possibly illegal circumstances" prevailed.

When the Aubis bankruptcy loomed in 1999, the bank negotiated a financial disencumbrance in order to prevent the bankruptcy of the real estate company. The bank took over the rights to use the predominantly empty properties, in return forsaking repayment of the credit. In the context of this arrangement, the repayment of private loans to the Aubis managing directors and CDU politicians Wienhold and Neuling—worth more than five million marks—was also expressly dispensed with.

Landowsky stated again and again that he did not have to do anything with such million mark gifts and had not been involved in Aubis's renovation efforts. However, Berlin's *Taz* newspaper quoted a letter to Landowsky dated January 20 2000, which made clear that the CDU leader was well informed about the whole Aubis proceedings: "The private loans to Messrs N. and W. were covered by the purchase of the usufructuary right [the right to use and profit from another's property]".

In February, Landowsky was forced to give up his position on the executive board of BerlinHyp, but continued to draw his lucrative income. He received two full years' salary worth 1.4 million marks and will enjoy a monthly pension of almost 30,000 marks for the rest of his life for his work at BerlinHyp. In the middle of May, he was also forced to resign as a chairman of the CDU parliamentary group, but ensured he was elected deputy regional chairmen at the following CDU state convention. However, in view of the increasing pressure, he has already had to vacate this post.

For more than three decades, Klaus Landowsky has played a key role in Berlin's politics. At the end of the 1960s, he became a law student at the Free University, and in 1971 was already a CDU delegate to the Berlin state legislature. His close political collaboration with Eberhard Diepgen stems from these days. Together they created a political unit based on hysterical anticommunism and materially supported by "Berlin Aid", an almost inexhaustible financial stream from the then federal capital in Bonn.

During the Cold War, West Berlin was regarded as the frontline city of the Federal Republic of Germany, since it was located in the middle of East Germany. The "shop window of the West" was meant to demonstrate the superiority of the free market and capitalism. Billions of marks in subsidies were pumped into West Berlin to avoid having people and businesses leave.

Enterprises of all kinds received favourable credits; cultural facilities were generously supported. In addition, young families could receive favourable loans unavailable anywhere else in the country. Berlin's special status under the four powers (Britain, France, the US and the USSR) meant its citizens did not have to undertake compulsory military service, which attracted many pacifists.

An inflated administrative apparatus developed, a highly subsidised cultural sector and a pronounced subculture with its "alternative enterprises" and social initiatives of all kinds. In 1990, of the total expenditure of the city, worth some 35.6 billion marks, almost 60 percent was financed through federal subsidies (19.6 billion marks). Above all, however, a close intertwining of business and politics developed with mafia-like structures: the notorious Berlin "subsidy biotope".

German reunification over 10 years ago fundamentally changed the situation. The subsidies were reduced from almost 20 billion to 7.5 billion marks last year. In the same period, the city's debts increased dramatically. In 1991 per capita debt stood at 4,600 marks, almost 1,500 marks below the German average, rising last year to 20,700 marks, more than the double the average.

Initial hopes that the effects of Berlin becoming the capital city and the transfer of businesses there would cover the costs of German unification were soon dashed. Instead of the hoped for economic upswing, social problems grew. The drift away from the capital increased more rapidly than the numbers moving there. Between 1991 and 2000, the number of manufacturing sector jobs in Berlin sank by around 185,000, or 40 percent. This was only met by a rise in service sector employment of 60,000 jobs.

Compared with other large German cities, such as Munich or Hamburg, Berlin has only half the tax revenues from manufacturing. However, the capital has more than twice as many people receiving social security benefits compared with Munich, six times as many retired government officials and twice as many public service employees.

When the BGB was founded in 1994, it rapidly became the centre of Berlin's corrupt web of patronage and bribes. The centre of its dubious business practices was the assignment of shares in various real estate funds, with which the entire risk was removed for each investor. They kept the rental incomes for 25 years and afterwards were ensured a right to buy back the property at the original price.

Out of these "VIP funds", valued at more than 20 billion marks, not only Landowsky and his cronies benefited, but according to press reports also Social Democrats, like the present Minister for Development Aid Heidemarie Wieczorek Zeul.

Under these conditions, the debts of BGB assumed ever-greater proportions. In the last year, management tried to conceal the looming bankruptcy by the fictitious sale of the bank's real estate subsidiary. A sham transaction was contrived with the help of the American investment bank J.P. Morgan. But behind the purchaser, ostensibly based in the Cayman Islands, stood the BGB itself, which wanted to finance the purchase price from a new line of credit.

The deal was stopped by the Federal Banking Supervisory Office, which initiated an investigation resulting in the end of the BGB in its previous form. Criminal proceedings have been launched against 23 managing directors and leading bank officials. The key figure of Klaus Landowsky is not yet among those facing such proceedings. His old political friend Eberhard Diepgen still holds a protecting hand over him. In his dual role as Berlin mayor and justice senator, Diepgen has managerial authority over the public prosecutor's office. But Landowsky's days are numbered.

Although anger is growing among the general population over the unrestrained scams being run by the business and political elite, with calls for those responsible to be punished, the SPD, the Greens and the Party of Democratic Socialism are pursuing completely different aims. Much points to the fact that Landowsky and some of the other main culprits could be publicly pilloried and face criminal proceedings. But prising the lid of Berlin's sewer serves will, above all, be used to implement a drastic austerity programme with severe cuts in all areas of public spending.

The corrupt system of clientele politics, originally financed from "Berlin Aid" and since reunification by increasing indebtedness, also cloaked a developed social system with far more kindergartens, publicly funded after-school clubs, sports and youth facilities than in other cities. Berlin also enjoys an expansive cultural sector, with three opera houses, five orchestras, 123 museums and 196 libraries. It is against all of these gains that the present policies of the SPD are directed.

Berlin's mayor-designate, Klaus Wowereit (SPD), is also a trusted friend of Chancellor Gerhard Schroeder, and has already announced "a new dimension to public spending cuts" in the capital. At the same time, many areas of the public sector are to be privatised and rationalised, which means mass redundancies and welfare cuts. Because this will lead to social conflicts, the SPD is striving for cooperation with the Party of Democratic Socialism—the strongest party in five of the six east Berlin districts where it holds the district mayor posts.

Every indication points to intensified social and political conflicts in Berlin over the coming period.