The Bavarian state bank's corruption scandal

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The scandal involving Gerhard Gribkowsky, former head of risk management at the Munich-based Bavarian State Bank (BayernLB), has deepened and is engulfing a wider layer of top managers and politicians. The state parliament's committee of inquiry and investigating prosecutor—whose mandate was to examine the murky events leading up to BayernLB's takeover of the Hypo Group Alpe Adria (HGAA)—had previously signalled they were wrapping up their inquiries.

Several weeks ago, Gribkowsky was arrested for concealing the receipt of $50 million, which was deposited in Austrian bank accounts in 2006 and 2007, allegedly en route to a private foundation. The facts revealed so far suggest the money was a payoff for BayernLB's Formula 1 racing car deal, which Gribkowsky had intricate knowledge of as manager of the state-owned bank. He is now under investigation for allegations related not only to tax evasion, but embezzlement and bribery.

In 2001, the BayernLB, along with Lehman Brothers and JP Morgan Chase, loaned media magnate Leo Kirch $1.6 billion (€1.2 billion) to help buy a controlling interest of SLEC, the media business that held the rights for the popular Formula 1 car racing series. Following Kirch's bankruptcy, Gribkowsky was assigned the task of finding a buyer for Formula 1—and he eventually sold the shares to the British investment firm, Corporate Venture Capital (CVC). The public prosecutor's office has charged that no estimate was made of the value of the shares before they were sold off at bargain basement prices. Meanwhile, Gribkowsky was rewarded with a princely commission.

New documents have come to light about a company network overseen by Gribowsky that was responsible for all kinds of shady transactions. As *Stern* magazine reported, Gribkowsky was extended far-reaching powers by Formula 1 boss, Bernie Ecclestone, after the sale of the BayernLB shares went through, enabling Gribkowsky to channel money through a complex network of companies and into his own pocket.

According to the *Stern* report, Gribkowsky's own GG Consulting appeared on the Austrian trade register the same day BayernLB sold its shares to CVC. The first instalment of the alleged commission money landed in the account of GG Consulting nine months later. Exactly $21,196,000, arriving in five separate transfers, was deposited. The money was transferred from a company named First Bridge Holding Ltd, which was headquartered off the southeast African island nation of Mauritius.

On May 3, 2007, Gribkowsky set up a private foundation, named "Sunshine", in Austria. The second tranche of the $50- million commission later appeared on the account of a subsidiary of Sunshine. This time the money was transferred from a firm in the British Virgin Islands.

Criminal investigators have been looking into these events since 2008. It is suspected the bank intentionally and systematically violated its internal guidelines for risk management in relation to securities transactions from 2005 to 2007. With respect to civil law, the BayernLB's executive board has waived any claim against the former overseer of its administrative council.

Gribkowsky's operation was not exposed by the public prosecutor, but through the efforts of journalists from the *Süddeutsche Zeitung*. According to the newspaper, after its journalists had confronted him with evidence of dubious transactions, Gribkowsky approached the Munich prosecutor himself, claiming he was being persecuted by the journalists.

Gribkowsky is facing five to ten years in prison. State investigators say events surrounding Gribkowsky could produce the biggest corruption case in the history of the Federal Republic.

The affair casts light on BayernLB's management, which continued to back Gribkowsky despite his dubious past, including involvement in business failures at the Carinthia (Austria) Hypo Group Alpe Adria (HGAA), which left the bank with billions in losses, and the former BAWAG trade union bank in Vienna.

Gribkowsky's actions were not simply those of an individual. They were an integral part of the state bank's risky transactions, which yielded huge sums for big investors and politicians. Banks and financial companies throughout Europe and the US took similar risks. Since the 2008 crash their gambling losses have all but been covered by state treasuries.

The Bavarian parliamentary committee of inquiry has suspended interrogation of witnesses in relation to the HGAA deal. More than 60 witnesses have testified so far, including former directors of BayernLB and leading Christian Social Union (CSU) party members such as the former Bavarian prime ministers Edmund Stoiber and Günther Beckstein, ex-finance minister Kurt Faltlhauser and former CSU party leader Erwin Huber.

HGAA was involved in dubious and highly risky business operations in the Balkans and in eastern Europe. It has long been known that BayernLB's purchase of HGAA was legally dubious. A private group of investors around the former CEO of HGAA, Tilo Berlin, has made €140 million in profits through the purchase of the ailing bank.

In order to rise to the level of global players in the financial world as quickly as possible—a policy called for by Stoiber—BayernLB also invested heavily in junk securities from the US housing market. This led to BayernLB to the brink of collapse after the bursting of the housing bubble in the US in 2007-08. The losses of the bank were absorbed by the state of Bavaria, which extended €7 billion in equity.

During testimony to the inquiry commission, CSU members on the bank's administrative council sought to conceal their complicity. Beckstein, Huber and others tried arguing that the Austrian executives, who sold HGAA, had misled the bank's executive board and administrative council. They also claimed executive board withheld relevant information from the administrative council.

However, several reports from expert witnesses, including from the accounting firm Flick, Gocke and Schaumburg, showed both the executive board and administrative council were informed of the risks and decided to take them nevertheless. Executive board members, one report said, acted "far beyond the limits of commercial discretion in the context of investment decisions concerning the US portfolios" compiled and maintained by the BayernLB's overseas headquarters in New York.

It continued, "In doing so, they have grossly and culpably violated their obligation to make business decisions only after careful investigation of the grounds for their decisions…There is good reason to believe the proceedings of the members of the administrative council were grossly negligent. ...Further major financial devastation will certainly eventuate."

Gerd Häusler, current head of the BayernLB, has announced the bank will not seek damages from Beckstein and other administrative council members. This is because their conduct was only "negligent" and not "grossly negligent", he said, adding that they were also only "common" members of the administrative board. Following the disclosures about Gribkowsky, it is possible charges will be levied against the chairman of the administrative board and his deputy, the former finance minister Faltlhauser, as well as former bank president, Siegfried Nasser.

The state government will ensure that the losses incurred by the BayernLB will be borne solely by the general population as opposed to the major financial investors, who have earned a fortune from the transactions.

Following years of drastic austerity measures, social spending in the state is again being ruthlessly cut. Finance Minister Fahrenschon has slashed 1,800 teaching posts, even though there is already a severe shortage of teachers in Bavaria. Public servants have had to accept a pay freeze, and the ministries of education, culture and social services have seen a significant reduction in their budgets.

Prime Minister Horst Seehofer called the planned cuts of €1.8 billion a "breakthrough". He leaves no doubt that, should the fiscal situation continue to deteriorate—for example, owing to further funding requirements of BayernLB—his government will introduce even more brutal austerity measures.