CASE STUDY OF ALPHA MERCHANT BANK PLC

1.0 INTRODUCTION

1.1 Institution's Background.

A group of investors from diverse background such as medicine, banking manufacturing, commerce, administration and law promoted the establishment of Alpha Merchant Bank (AMB) at a time the regulatory capital was N6 million. In keeping with the permissible ownership structure, no single shareholder held more than 5% of the paid up capital. The shareholders were also required to maintain a geographical spread covering two thirds of the existing 19 states (i.e 13 states) of the Federation. The bank commenced business on 6th June, 1988.

The bank's issued share capital was increased from N6 million in March 1989 to ₦12 million and from N12 million to N15 million in August 1989 through bonus issue to all shareholders. However, the mode of payment of the initial paid-up capital of N6 million by some shareholders generated controversy. Similarly, the bank's public offer of 50,000,000 shares in May 1992 generateda controversy which warranted regulatory intervention as highlighted elsewhere in this case study. Undoubtedly, ownership and control crisis was one of the major causes of the bank's failure.

The ownership and control crisis polarised the Board to the extent that it could not operate as a team. Board oversight of management was very weak while the management was accused of withholding vital information from the Board, engaging in unprofessional and unethical practices as well as dissipation of the bank's resources. In summary, corporate governance fell below acceptable standards.

Furthermore, the bank engaged in excessive risk taking which manifested in illiquidity, poor asset quality and erosion of capital. As a matter of fact, it was one of the ten banks bailed out during the liquidity crisis which engulfed the banking system in 1989 that is, within its first year of existence.

1.2 Business Environment

Before the promulgation of Banks and other Financial Institutions Act (BOFIA) 25, 1991, the responsibility for licensing and regulation of banks was vested in the President -in- Council and the Federal Minister of Finance respectivelyunder the Banking Decree 1969. Therefore, CBN's capacity to regulate/supervise banks depended on the level of support it received from the Ministry of Finance. Indeed Central Bank of Nigeria (CBN) Examination reports were being forwarded to the Minister of Finance for consideration before Examiners recommendations could be implemented

In the 1980's and 1990s Nigeria operated a dual banking system comprising merchant and commercial banks. The regulatory requirements favoured establishment of merchant banks because they were subjected to lower capital requirement, exempted from compulsory rural branch opening, andcash reserve requirements. However, they were not permitted to mobilize deposits below N50, 000

In recognition of the need to resolve banking distress which had emerged, and enhance supervisory capacity, the Nigeria Deposit Insurance Corporation (NDIC) was established in 1988 even though it commenced operations in March 1989. The establishment of NDIC strengthened the financial safety net and provided a mechanism for bank resolution.

In May 1989, the Federal Government directed that public sector deposits be withdrawn from commercial and merchant banks to the CBN. That directive triggered liquidity crisis in the banking system. The bank regulators (CBN and NDIC) had to bailout 10 banks in order to restore stability. Alpha Merchant Bank was one of the beneficiaries of that bailout.

The adoption of Structural Adjustment Programme (SAP) in 1986 necessitated economic liberalization and deregulation.Consequently, licensing of banks was liberalised such that the number oflicensed banks increased phenomenally from 38 in 1986 to 121 in 1991. AMB was one of the banks that emerged under the liberal licensing regime.

The bank operated in an environment of expansionary fiscal regime which manifested in huge budgetary and extra-budgetary deficits. Financing of *these deficits resulted in rapid growth of banking system credit to the Federal Government which caused monetary instability.*

The adoption of SAP changed the focus of monetary policy from direct control on banks' operations to the indirect system which relies on the use of market-based instruments for the management of money and credit. Under direct monetary control, the main policy instruments comprised imposition of credit ceilings on individual banks, administrative fixing of interest rates and sectoral allocation of credit. However, the indirect system was implemented in phases. Measures taken included deregulation of interest rates, creation of auction market for treasury bills/certificates, introduction of prudential guidelines on asset classification, and income recognition, selective lifting of credit ceilings on banks that met specified criteria, mopping up of banks' excess liquidity and adoption of open market operations (OMO) in June 1993. As a complementary measure to OMO, the CBN sought to curtail the rapid growth of bank liquidity through mandatory allocation of stabilization securities to the banks.

Policy inconsistency hampered banks' operations. For example, interest rate regime was deregulated in 1989 but was reviewed with a cap on lending rate in 1991. Interest rate was again deregulated in 1992 while control was re-imposed in 1994.

Banking system credit to the private sector grew rapidly during 1991-93 mainly attributable to excessive government spending. The deregulation of interest rates engendered stiff competition in the banking industry to attract deposits which was accompanied by high lending rates and exchange rate depreciation. The competition that ensued increased the risk profile of the banking industry while the proliferation of banks over taxed the managerial capacity of the industry as well as regulatory capacity. The banking industry witnessed staff poaching amongst banks and appointment of employees into positions beyond their levels of experience and skill. Furthermore, the licensing requirements such as ceiling of 5% of bank's equity on individual investors and the prescribed geographical spread of shareholders brought about strange bedfellows which triggered crises in some banks.

2.0 THE JOURNEY TO FAILURE

A combination of events that took place set the bank on the way to its demise. The board had a crisis early in its life which was followed by a controversy over purchase of shares in Afribank and a struggle for control of the bank. These events are discussed in this section.

2.1 Boardroom Crisis

AMB commenced operations on 6th June 1988 with a seven-member board. The board was engulfed in crisis early in its tenure which resulted in the removal of a Director for alleged interference in the day-to-day management of the bank. The removed Director instituted law suits against some board members. The law suits generated adverse publicity for the bank. A Director was accusedof claiming academic qualifications he allegedly did not possess and that led to the suspension of the Director pending investigation of the allegations against him.

Bank Examination conducted as at 31st July 1989 revealed that the Board met almost every month since June 1988 to deliberate on policies and strategies to guide the bank's operations. It was noted that litigations involving board members had hampered the performance of the bank. Meanwhile, the suspended Director was recalled in August 1989 with the approval of the Minister of Finance upon receipt of a police report of investigation. Also, based on the Terms of Settlement filed in court, a Director earlier removed was re-appointed at the Annual General Meeting (AGM) held on 29th August 1989 subject to withdrawal of cases before the courts and return of bank's assets in his custody.

These reconciliatory moves were designed to stabilize the bank. But the reconciliatory efforts only gave the bank a temporary respite.

Bank regulators require that banks operate on the basis of sound governance principles which at a minimum should comprise setting strategic objectives and corporate values, responsibility and accountability structure, effective oversight of senior management and efficient management information system. However, a review of the bank's management practices revealed non-adherence to sound governance principles in the conduct of its affairs.The Board was ineffective in its oversight of management as would be shown later in this study.

2.2 Purchase of BIAO shares in Afribank.

2.2.1 The acquisition of BanqueInternationale Pour L' AfriqueOccidental (BIAO) shares in Afribank Nig. Plc was one of the contentious issues raised in a petition to the CBN by a Director in May and June 1993 and petition by four shareholders and former directors of the bank to the Inspector General of Police (IGP) and Director General of State Security Services in September/October 1993. It was alleged that some Directors utilized $16 million of bank's fund to acquire Afribank shares for their personal benefit.

2.2.2 The outcome of investigations conducted by CBN/NDIC, Interim Management Board (IMB) of Alpha and the submission of a Director to Mr. Paul Ogwuma (CBN Governor) dated 12th May 1994 can be summarised as follows:

- *BIAO sold its 40% equity interest in Afribank to Meridien International Bank Ltd (MIBL) in March 1991. MIBL was unable to obtain regulatory approval for the transaction from CBN. It therefore entered into an agreement with BIAO to hold the shares on its behalf. MIBL terminated the agreement on 25th September 1991.*
- *Meanwhile, the Federal Minister of Finance had given approval to Nigeria National Petroleum Corporation (NNPC) and Alpha to jointly purchase the 40% BIAO stake in Afribank in August 1991. However, Alpha requires CBN approval for the acquisition under BOFIA which became operative with effect from 20th June 1991. Both CBN and NDIC objected to acquisition of BIAO shares by Alpha.*
- *Notwithstanding CBN disapproval, some Directors incorporated an offshore company under the name-Alpha International Bancorp (later changed to Afri Investment Limited) as the vehicle for the share acquisition.*
- *A Director confirmed that "$5.1 million bank's fund was "remitted to one of the Directors company's account with Union Bank of Nigeria, London Branch........we were able to effect payment of six million dollars to Meridien BIAO in September 1991 upon execution of the purchase contract" He further*

stated “All in all, we spent about ten million dollars (out of which Alpha financed about seven million dollars ....)” and put total cost of acquisition at sixteen million dollars.

- *Thereafter, the 40% stake in Afribank was allotted in the ratio of 17% to a Director , 13% to another Director and 10% to Alpha as averred in one of the Directors letter to the Honourable Minister of Finance dated 13th September 1999. A Company was appointed as Trustees of the acquisition. The basis of allotment of the shares acquired was not disclosed*
- *A Director disclosed that another Director later tried to convert the entire acquisition to his own benefit by seeking to transfer it to another company-Afri InvestmentHoldings Limited incorporated by him. The attempt led to lawsuit instituted by one of the Directors in London.*
- *The acquisition of BIAO shares in Afribank was never approved by the board of directors of Alpha. Indeed, the transaction was shrouded in secrecy and did not reflect good faith on the part of its arrow heads.*
- *The controversies and litigation generated by the acquisition of BIAO shares in Afribank were not resolved until 2003 when the National Council on Privatization facilitated the acquisition of BIAO shares in Afribank by the Bureau of Public Enterprises (BPE) based on agreement reached between the liquidator of BIAO, and two Directors of Alpha Merchant Bank.*

2.3 ***Struggle for Control***

2.3.1 The bank’s issued share capital was increased from N6 million to ₦12 million in March 1989 and to ₦15 million in August 1989 through bonus issue to all shareholders. The authorised share capital was increased from ₦20 million to ₦100 million, ₦50 million of which had been paid up while the balance of ₦50 million was to be raised through public issue. The capital increase was to finance the bank’s head office building project.

2.3.2 A special investigation by CBN and NDIC as at 16th July 1993 revealed that the bank offered 50 million units of N1.0 shares for sale at ₦2 per share payable in full on application. The offer opened on 6th May 1992 and closed on 19th June, 1992. A concessionary extension of two weeks was granted for the return of applications which ended on 3rd July 1992. The offer was undersubscribed with applications for 17,362,592 shares received as at 3rd July 1992. However, applications for 53,392,920 shares were submitted to the Securities and Exchange Commission (SEC) which SEC approved on 14th August 1992 based on information provided by the bank.

2.3.3 The allotment proposal approved by SEC was later manipulated to give ownership advantage to two directors. Whereas SEC had approved 5,162,715 shares each in favour of the two directors, their allotment was increased to 13,075 430 shares each without the approval of the board.

2.3.4 Sequel to a petition by an aggrieved director, investigation conducted by CBN & NDIC revealed numerous irregularities in the payment by subscribers as summarised below:

i) One of the Directors paid only ₦3,718,200 as at the close of public offer on 19th June 1992.

ii) On 31st December 1992, ₦14,753,011 was transferred from the account of UNIJOY Products Ltd by a Director which was applied to pay for shares as listed below:

A Director	***₦9, 357,230***
,, ,,	***₦2,395,781(Part Payment)***
Subscriber	***₦1, 000.000***
,, ,,	***₦1,000.000***
,, ,,	***₦1,000.000***

iii) a Director paid ₦7,279,648 (made up of ₦5 million draft dated 1st July 1992 and $94985.34 transfer by Sovereign Risk Group, New York on 16th December 1992). He paid ₦9, 675,430 out of ₦13, 075,430 due from him.

iv) Monument Finance & Securities paid N10 million for shares allotted to it in various tranches between August and October 1992 after the close of offer.

v) ₦5 million shares allotted to NICON Insurance not taken up was re-allotted to VEE PEE Industries Ltd and paid for on 31st March, 1993.

vi) 3,718,200 shares allotted to a Subscriber was paid for on 29th July 1992 via an unauthorised overdraft credited to the account of a company.

2.3.5 The CBN/NDIC Investigation report showed that the allotment of shares was not transparent and was manipulated to put control in the hands of a few shareholders.

2.3.6 Sequel to the controversial public offer and manipulated share allotment, an Annual General Meeting (AGM) was held on 22nd April 1993. The AGM was fraught with irregularities. Two persons who were not duly nominated in accordance with the bank's Articles of Association stood for elections. Some shareholders acted as proxies for other shareholders using proxy cards not duly filed before the meeting nor was there evidence that they were duly authorised to act as proxies. A Director voted as a proxy for an aggregate of 21,500,000 shares while another Director voted as a proxy for an aggregate of 25,000,000 shares

2.3.7 Examiners therefore, recommended that the elections were fraught with malpractices and should be cancelled.

2.3.8 However, consequent upon the AGM, a special resolution was passed to adopt a new Memorandum and Articles of Association (MEMART). The MEMART provides for the creation of "Founders Shares" which shall be those shares held at any time by some Directors of the bank.

2.3.9 Article 5(b) (ii) further provides that "No resolution on any of the following matters shall be deemed to be decided by the members of the company in the general meeting unless the votes of at least 60% of the total amount of shares constituting the Founders Shares at any time, were cast in favour of such resolutions:

(a) The change of the company's name

(b) The appointment of the Chairman of the board

(c) Alteration of the authorised or issued share capital of the company

(d) The establishment and changes in the borrowing powers of the company, guarantees, loans, mortgages, and a charge on the assets of the company

(e) The appointment or removal of the Managing Director"

2.3.10 Examiners observed that the existing shareholding structure concentrates 60% of the Founders Shares in the hands of some Directors and empowers them to exercise the rights conferred on the Founders Shares.

2.3.11 Examiners also noted that the special rights not only undermine the interest of other shareholders but a flagrant violation of section 10 of BOFIA 1991 which states that "Notwithstanding the provisions of the Companies and Allied Matters Decree 1990, or any agreement or contract, the voting rights of every shareholder in a bank shall be proportional to his contribution to the paid-up share capital of the bank"

2.3.12 The adoption of the new MEMART was a clear manifestation of the scheming to control the affairs of the bank by a few shareholders. The development aggravated the existing acrimony amongst some shareholders/directors.

2.3.13 The aforementioned developments resulted in petitions to both the CBN and SEC which warranted regulatory intervention. The main issues in contention include irregularities in the public offer of shares, unwholesome practices at the AGM held and purchase of Afribank shares allegedly shrouded in secrecy.

3.0. APPRAISAL OF BANK'S PERFORMANCE

In his letter to the CBN Governor, a Director admitted the bank's precarious condition as quoted below:

> *"For the avoidance of any doubt, let me state clearly that mistakes were made during my tenure of office, such as:*
>
> *1 As I alluded to previously, the bank's credit exposure was too high*
>
> *2 In an attempt to disguise the excessive credit exposure we resorted to making several adjustments some of which were legal and some of which border on the verge of legality"*

He also stated in the same letter that "up until the advent of the crisis, not only was the bank operating profitably <u>(admittedly without full provision for doubtful debts)</u>" How can a bank make profit without full provision for doubtful debts? He further stated that "by August 1993 ...and in spite of CBN having refunded the stabilisation securities, Alpha was not only insolvent but also illiquid and patently unable to repay it (sic) depositors"

Given this admission, the bank's financial statements did not reflect its true financial condition. Such manipulated financial statements cannot be used to assess the bank's performance. The appraisal in this section relies on information available from bank examination reports using the CAMEL parameters. The components of this acronym are Capital Adequacy, Asset Quality, Management, Earnings and Liquidity

3.1 Capital Adequacy

Examiners' computation of adjusted capital as at 31st December 1992 revealed a negative capital position of N174.7 million while capital to risk asset ratio (CAR) was negative to the tune of 10.57% as against the minimum prescribed ratio of 8%. The CAR plummeted to -77.39% as at September 1993.

Given its total erosion of capital, Examiners recommended a minimum capital injection of N306.88 million, as at 16th July 1993 by its shareholders to support its level of operations

3.2 Asset Quality

Examiners noted various acts of insider abuse with regard to credits extended to the bank's directors or their related companies. Credit facilities in excess of single obligor limit were granted to companies associated with some directors. Draw-down was allowed on facility sought by a director in anticipation of approval which was declined. Credits to some director-related companies were delinquent and also unsecured. The liquidity problem experienced by the bank was partly attributable to the quantum of delinquent credit facilities. Bank Examination of the bank as at 31st Jan. 1992, put classified insider-credits at 30% of total classified credits.

Most credit facilities were either unsecured or were granted based on inadequate collaterals. Also the bank relied on valuation provided by customers' valuers in respect of pledged collaterals

The bank was in the habit of crediting delinquent accounts (mostly ADB/ESL and NERFUND facilities) at month ends with huge amounts described as "Sundry Cheques lodged" only to reverse the entries in subsequent months. Examiners opined that the practice was adopted to understate the bank's credit exposure and provision for bad and doubtful credits. As a result of these manipulations, provision was understated by N271.9 million as at 31stJanuary 1992.Under-provision was put at ₦341.8 million in the Special Investigation report as at 16th July 1993.

3.3 Management

3.3.1 The board was ineffective in performing its functions. Examiners noted various weaknesses as reflected by the under listed observations:

- *Board directive that report on non-performing credits be presented at each board meeting was not complied with*
- *Board Audit Committee established in August 1989 reported to the Board only once in 1990 on credit and operational matters*
- *Board Credit Committee met only four times between 1988 and January 1992 to ratify credit approvals by the CEO which were in excess of his authorised limit. No queries were raised about CEO's violation of his approval limit with impunity*

- *No inspection or internal control unit was established for almost two years after the bank commenced operations. A Chief Inspector was only employed in 1990.*
- *A new organogram approved by the Board put key operations such as treasury, foreign exchange and credit administration under direct control of CEO while the two Executive Directors in charge of Investment Banking and Finance & Admin respectively have few departments reporting to them.*
- *The bank had no procedures manual until 1990/91 when it engaged a Consultant who developed manuals for:*

    - *Credit and marketing*
    - *Treasury and financial services*
    - *Investment banking services*

- *These manuals were approved by the Board in December 1991 but were yet to be put into use as of March 1992. There were no manuals for other functions as at March 1992*
- *The MD/CEO had no contract of employment as at July 1993. He did not execute the service agreement prepared by the company secretary at the instance of the Board.*
- *The Board did not seek update on proposal to acquire equity interest in Afribank Nigeria Plc which the MD/CEO brought to its attention at its meeting held on 27th August 1991. The investment later generated controversy as highlighted above:*

3.3.2The board and Management failed to appreciate the critical role of internal control in a banking institution. Hence, an Inspection Department was not established until August 1990 when a Chief Inspector (CI) assumed duty. The department was under staffed. The CI was the only staff until April 1991 when an Assistant Manager was employed to assist him. The third staff (a senior supervisor) assumed duty in February 1992. It was no surprise that no inspection was carried out in 1990.

For most of 1990 and 1991, the CI was saddled with functions other than audit and inspection. He was attached to the Consultant engaged to develop procedure manuals for credit and marketing, investment banking and financial services departments of the bank. It was the CI that had to develop the procedure manual for audit and inspection. For effective *management, procedure manuals should have been developed before commencement of operations by the bank. As at February 1992, major departments listed below had not been subjected to inspection:*

- *Treasury*
- *Credit and Marketing*
- *Investment banking*
- *Financial control*
- *Company Secretary/legal*
- *Computer System*

The CI reported to Executive Director (Finance, Planning and Admin) and copied inspection reports to the MD/CEO and Head of departments inspected. Disagreements with inspection findings are referred to an Arbitration Committee chaired by the MD/CEO Meetings of the Arbitration Committee are convened at the instance of MD/CEO. There is no doubt that this arrangement cannot ensure effectiveness and independence of inspection function.

3.3.4Against the backdrop of an ineffective inspection function, the bank's operations exhibited numerous control lapses some of which are highlighted below:

- *Both Board Credit Committee and Board Audit Committee were ineffective*
- *The computerised accounting system exhibited system and posting errors. There were cases of debit entries appearing as credit and vice versa. Subsidiary records (ledgers) which ought to provide details of general ledger (GL) balances did not agree with G/L*
- *The Information Technology system was procured without feasibility study and analysis. The programme and software problems were partly attributable to this lapse. The system's memory capacity was also considered inadequate.*
- *Fixed asset register did not reflect date of purchase, monthly depreciation, accumulated depreciation, net book value etc. Also, purchase of fixed assets worth ₦1.5 million was treated as "I.O.U" on the pretext that the transaction has not been concluded*

- *The only branch of the bank carried forward profit for the year 1991 instead of transferring it to the Head Office*
- *Reconciliation of foreign correspondent bank nostro accounts revealed:*

- Credit and debit items not in local bank's books

- Credit items not taken up by correspondent bank

- *The bank resorted to creating numerous foreign cash accounts with physical cash on hand because foreign cash register could not be reconciled*
- *Numerous domiciliary accounts were overdrawn. For example, a customer's travellers cheques purchased by the bank were rejected when sent for collection on the ground that they were stolen. In response, the bank debited the customer's unfunded domiciliary account.*

- *About US$5.1 million of bank's fund was utilised for acquisition of equity interest in Afribank without Board approval and undetected by the internal control system.*
- *There were several instances of wrong interest calculation due to software malfunction. Hence, customers protested interest over-charge or errors in interest computation. The bank had to resort to manual reconciliation and reconstruction of customers accounts*
- *Examiners noted instances where only one staff undertook call-over of transactions at the Head Office while there was no call-over at Kano Branch*
- *Comuttal of annual leave to cash was virtually the norm. Examiners noted that between 1989 and February 1992, 74 out of 134 staff (or 55%) commuted their annual leave to cash while 52 (or 39%) still had leave arrears ranging from 1-85 days.*
- *Routine Examination conducted as at Jan 31, 1992, established misreporting in prudential returns submitted to the CBN. Examples cited include:*

  - *Deposit lumped with other liabilities*
  - *Staff loan lumped with other assets*

- *Advances from NERFUND treated as other assets*
- *Money at call was inflated*

3.4 Earnings

Given the wilful manipulation of financial records, the published financial statements were not used for the analysis in this study. The bank reported a profit before taxation of N31.1 million as at Dec 31st 1991. Against the backdrop of under-provision of N31.9 million as at Jan 31st 1992, the bank should have reported a loss before taxation. Examiners also noted that between 1989 and 1991 expenses were increasing at a faster rate than income which is symptomatic of a loss-making scenario. As at 31st Jan. 1992, the bank was required to increase provisions for doubtful debts from ₦30.4 million to ₦62.3 million.

3.5 Liquidity

Examiners noted that 44% of the bank's deposits was on call, while another 50% was mobilized from other banks. Hence, the bank was vulnerable to shocks in the interbank market. Also, its current account with CBN was being overdrawn from time to time. As admitted by a Director, it was patently unable to pay depositors before regulatory intervention

The loans to deposit ratio was as high as 124% as at Jan 31st 1992 and 126% as at 30th Sept. 1993 which is indicative of liquidity problem. Liquidity ratio was negative to the tune of 5:25% in September 1993. It is noteworthy that the Lagos State Administrator detained two staff of the bank for its inability to repay a placement of ₦10 million to Lagos State Government. It took the intervention of NDIC before they were released

4.0 CAUSES OF BANK'S FAILURE

4.1 Weak Corporate Governance

As noted in section 2.1, the board was engulfed in crisis right from inception in 1988. It experienced a cycle of crises until regulatory intervention became inevitable in 1993. Consequently the board was unable to perform its major role of setting a strategic direction for the bank. The board was ineffective and failed to ensure implementation of its decisions by management.

4.2 Management Ineptitude

The various lapses highlighted in section 3.3 indicate that the executive management lacked the technical competence to run the bank prudently and profitably. Hence, it resorted to manipulation of financial records to portray the bank as sound and operationally efficient. The management exhibited a high risk disposition but had no regard for transparency and accountability. The board members that petitioned against the management accused the latter of withholding vital information from the board with particular reference to the purchase of 40% BIAO shares in Afribank.

A Director in collusion with another board member undermined the bank's interest by diverting the bank's funds to acquire equity interest in Afribank using a company jointly-owned by them (Afri investment Limited) without regard for the liquidity impact on the bank. A bank whose interest has been subjugated to those of its directors cannot survive. The struggle to control the bank by some Directors through the controversial public offer of shares and the manipulated AGM was indeed the last straw that hastened the bank's collapse

4.3 Financial Engineering

A Director of the bank in his various submissions after regulatory intervention and revocation of the bank's license revealed the various gimmicks employed to siphon the bank's funds for the benefit of a few board members, or to side-track regulatory requirements or to contrive profitable operations.

A bank is as good as its financial records. But Alpha's management opted to mislead the various stakeholders. Spurious prudential returns were rendered to CBN/NDIC. The documentation for the 1992 public offer of shares was deceitful to innocent investors. Board members were oblivious of secretly incorporated offshore company to acquire BIAO shares in Afribank. The combined effect of all these malfeasance was a loss of public confidence. Consequently, the shareholders found it impossible to raise fresh capital to recapitalize the bank. The revocation of the bank's license and liquidation was inevitable.

5.0 REGULATORY INTERVENTION

5.1 Dissolution of Bank's Board

Given its intractable board-room crisis, insolvency and illiquidity, CBN dissolved the bank's board of directors in August 1993 and appointed an Interim Management Board (IMB) to superintend over the affairs of the bank. The IMB's mandate include:

- *Determining the true financial condition of the bank*
- *Investigating allegations of improprieties against some directors of the bank including the CEO, and*
- *Submission of a turn-around plan for the bank*

In the process of determining the true condition of the bank, it came to light that its audited accounts did not reflect a true and fair view of its state of affairs. The auditors of the bank accused of not being professional in discharging their duties. It was noted that some staff of the audit firm involved in the bank's audit were indebted to the bank. Hence, issues impacting on the bank's viability prospects such as non-performing credits were not critically appraised.

CBN/NDIC directed that the bank's 1992 accounts should be re-audited. Consequently, the IMB appointed an Audit Firm to conduct a special audit to cover January to September 1993 in order to determine the bank's true financial condition.

The IMB liaised with SEC on alleged irregularities in the public offer of the bank's shares between May and June 1992. The Administrative Hearing

Committee of SEC directed that the shares paid for after the allotment date which were not approved by SEC be cancelled and that money deposited be returned to the subscribers. The Management took advantage of the bank serving as the Registrar to its own share issue to enter in the register of shareholders names of persons who had not paid for their shares as at the date of the allotment contrary to the terms of offer which required subscribers to pay in full on application for shares. The IMB also investigated the purported acquisition by Alpha of 40% BIAO shares in Afribank

Based on the information at its disposal, the IMB averred that the fundamental problems of the bank revolved around falsification of accounts and records, weaknesses in internal controls, improper record-keeping and accounting, poor management of risk assets, fraud and numerous malpractices which led to misallocation of the bank's financial resources

The IMB further noted that the management of the bank engaged in under-provision for non-performing loans and advances contrary to the provisions of prudential guidelines for banks; understatement of the volume of risk assets; inflation of reported profits, thereby misleading the public about the bank's true condition.

After the receipt of the report of special audit conducted by an Audit Firm, an Extraordinary General Meeting (EGM) of shareholders was held on April 19, 1994 at which the true financial condition of the bank was made available. The shareholders considered two options comprising raising capital through public offer of shares and seeking a loan from NDIC. Noting that securing a loan from NDIC was not feasible, the shareholders were left with the option of injecting additional capital to salvage the bank

The inability of the shareholders to heed the call on them to recapitalize the bank, left the regulatory authorities with the last option of revocation of the bank's licence in September 1994 as a prelude to its liquidation.

5.2 Liquidation

Pursuant to revocation of licence, NDIC was appointed liquidator of Alpha Merchant Bank. As liquidator, NDIC commenced payment of insured deposits from its Deposit Insurance Fund (DIF). Thereafter, it embarked on debt recovery, disposal of fixed assets and recovery of the bank's fund *irregularly applied to acquire BIAO shares in Afribank. It received N1.2 billion (i.e $10 million) as proceeds of BIAO Shares in Afribank in July 2003.*

As at 31st Dec. 2011 recoveries by NDIC are as follows (NDIC 2011 Annual Report)

		₦
Debt recovery	-	*903.5 million*
Asset disposal	-	*123.02 million*
Investment in Afribank	-	*1.2 billion (i.e $10m)*

Those funds were applied as follows:

		₦
Payment of insured deposit	-	*18.52 million*
Payment of uninsured deposit	-	*1.20billion*
Payment to creditors	-	*86.78 million*
Payment to shareholders	-	*600 million*

It is noteworthy, that depositors recovered their money in full. Not only were creditors claim settled, shareholders received six times the nominal value of their shares. Admittedly, the liquidation period has dragged on for too long which is partly attributable to slow judicial process which hampered debt recovery and the antics of the directors that misapplied the bank's funds for equity investment in Afribank without requisite approvals.

6.0 PROSECUTION OF DIRECTORS & OFFICERS FOR WRONG-DOING

6.1 In keeping with internationally accepted principles of effective bank resolution (IADI Core Principles 14 and 16) directors and officers found to have contributed to a bank's failure should be subjected to due process of the law. In this regard, NDIC advocated and contributed to the efforts that crystallised in the promulgation of the Failed Banks (Recovery of Debts) and Financial Malpractices in Banks Decree 18, 1994

6.2 Sequel to the failure of Alpha Merchant Bank, some Directors of the bank and two others were arraigned before the Failed Banks Tribunal in 1995. The charges against them were:

<u>COUNT 1</u>: That you, Lord Chief UdensiIfegwu (now at large) Jimi AdebisiLawal (now at large). Tony Nnachetta, and Jeff Fayomi while being Directors and or Managers of Alpha Merchant Bank Plc. (now in liquidation) at Lagos, between 30th June 1988 and 1st October 1993 conspired to commit a felony, to wit fraudulently granting credit facilities to Dubic Industries Limited without lawful authority in contravention of rules and regulations of the said Alpha Merchant Bank Plcand the regulatory authorities (CBN/NDIC) and thereby committed an offence punishable under Section 516 of the Criminal Code Act, Cap 77 Laws of the Federation 1990 to be read with Section 3 (1) (b) (c and d) of the Failed Banks (Recovery of Debts) and Financial Malpractices Decree (Act) 1994 as amended

<u>COUNT 8:</u> That you, Jimi AdebisiLawal (now at large). Tony Nnachetta, and Jeff Fayomi while being Managers of Alpha Merchant Bank Plc. (now in liquidation) at Lagos, between 30th June 1988 and 1st October 1993, granted credit facilities to Dubic Industries Limited in the sum of US$2,962,062.89 (Two Million, Nine Hundred and Sixty Two Thousand, dollars Eighty Nine Cents) (sic) now equivalent to N242,889,156.98 (Two Hundred and Forty Two Million Eight Hundred and Eighty Nine Thousand, One Hundred and Fifty Six Naira, Ninety Eight Kobo) without lawful authority in contravention of the rules and regulations of Alpha Merchant Bank Plc (now in liquidation) and the regulatory authorities (CBN/NDIC) and thereby committed an offence punishable under Section 18(2) of the Banks and other Financial Institutions Decree 1991.

<u>COUNT 9:</u> That you, Jimi AdebisiLawal (now at large). Tony Nnachetta, and Jeff Fayomi while being Directors and or Managers of Alpha Merchant Bank Plc. (now in liquidation) at Lagos, between 30th June 1988 and 1st October 1993, granted credit facilities to Dubic Industries Limited in the sum of US$2,962,062.89 (Two Million, Nine Hundred and Sixty Two Thousand, dollars Eighty Nine Cents) (sic) now equivalent to N242,889,156.98 (Two Hundred and Forty Two Million Eight Hundred and Eighty Nine Thousand, One Hundred and Fifty Six Naira, Ninety Eight Kobo) without lawful authority in contravention of the rules and regulations of Alpha Merchant Bank Plc (now in liquidation) and the regulatory authorities (CBN/NDIC) and thereby committed an offence punishable under Section 18(2) of the Banks and other Financial Institutions Decree 1991.

COUNT 10: That you, Lord Chief Udensi Ifegwu (now at large), between 30th June 1988 and 1st October, 1993 at Lagos while being a Director of Alpha Merchant Bank Plc (now in liquidation) and also a Director of Dubic Industries Limited was connected with the granting of credit facilities totalling US$2,964,062.89 (Two Million, Nine Hundred and Sixty FourThousand Dollars, Eighty Nine Cents) (sic) now equivalent of N242,889,156.98 (Two Hundred and Forty Two Million Eight Hundred and Eighty Nine Thousand, One Hundred and Fifty Six Naira, Ninety-eight Kobo Only)to Dubic Industries Limited without declaring your personal interest in the said facility to the then Board of Directors as required by Section 18 (3) of the Banks and Other Financial Institutions Decree 1991 thereby committed an offence punishable under Section 18(9) of the same Decree"

6.3 The Tribunal convicted the Plaintiffs of the charge and sentenced them on the first count to 5 years term of imprisonment and on Counts 8, 9, and 10 to 3 years term of imprisonment each. The sentences are to run concurrently.

6.4 Dissatisfied with the Tribunal judgement, D.U. Ifegwu appealed up to the Supreme Court. On 23rd May 2003, the Supreme Court ruled that the convictions and sentences were illegal because the Tribunal did not have the jurisdiction to try the Respondents in view of Section 33(8) of the Constitution of the Federal Republic of Nigeria 1979 (also reproduced as Section 36 (8) of 1999 Constitution.

6.5 In respect of Count 1, the Supreme Court held that the commencement of the Failed Banks Decree is 9th November 1994 while that of BOFIA is 20th June 1991 and that by Section 33 (8) of the 1979 Constitution a person cannot be convicted for an act which did not constitute an offence under the law which the person is charged. Attention was drawn to the fact that the acts constituting the offence are six loans granted between 2nd April 1991 and 31st October 1991. Three of the loans were granted (on 2nd 16th and 26th April 1991) before the commencement of BOFIA and Failed Banks Decree while the three other loans were granted on 4th and 12thSeptember 1991 and 31st October 1991. The Supreme Court held that it is illegal, improper and unconstitutional to combine what by Section 33(8) of 1979 Constitution is prohibited with what is not prohibited in a single charge which resulted in a single conviction. Hence, the sentence and conviction are considered unconstitutional

6.6 Counts 8, 9, and 10 relate to $2,962,062.89 (equivalent to ₦242,889,156.98) which consists of three loans granted before 20th June 1991 and three loans granted after that date. The Supreme Court equally held that the conviction and sentence cannot stand because what is prohibited by Section 33(8) of the 1979 Constitution cannot be combined with what is not prohibited.

6.7 Against the backdrop of the defective charges filed by the prosecution, the conviction and sentences of the accused persons were set aside

7.0 LESSONS LEARNT

This case study provides lessons for various stakeholders in the financial services industry ranging from policymakers, through regulators to bank directors and management. Some key lessons learnt from the case are:

7.1 Unduly restrictive ownership regulations in terms of ceiling and spread of investors could be counter-productive. It contributed to the unwholesome struggle for control which manifested in the creation of Founders Shares and acrimony amongst the directors/shareholders

7.2 Policy-induced shocks such as the sudden withdrawal of public sector deposits from banks in 1989 are bound to have unintended consequences. More so, that banks asset and liability structure require reasonable time to adjust.

7.3 licensing of banks should take into account availability of both regulatory and managerial capacity. The phenomenal growth in the number of banks over-stretched regulatory and managerial capacity.

7.4 Implementation of monetary policy through direct control instruments such as sectoral allocation of credits and mandatory investment in stabilization securities impeded bank's performance. Banks should not be made to bear the brunt of monetary and fiscal policy misalignment

7.5 Policy inconsistency as illustrated by the cycle of interest rate deregulation and control between 1989 and 1994 hampered bank's operations.

7.6 Effective board oversight requires shared vision and mutual trust amongst directors. Lack of a common visioncontributed to board-room crisis which engulfed Alpha Merchant Bank from cradle to grave

7.7 Inability to appreciate the vital role of internal control mechanism is a recipe for failure. There was lack of controls over the bank's processes and decision making. The CEO seems to be above controls

7.8 Self-dealing and excessive risk-taking are detrimental to a bank's viability. The penchant for both contributed to the failure of the bank

7.9 Financial misreporting, creative accounting and lack of transparency can only be sustained in the short-term as the bubble must eventually burst. The bubble did burst in the bank.

7.10 Inadequate or lack of coordination amongst policy-makers can provide arbitrage opportunities for market participants. Ministry of Finance approval of acquisition of BIAO shares should have taken into account CBN's position because the bank's financial condition did not justify the approval. Indeed substantial depositors' fund was diverted for the acquisition which is not prudent.

7.11 External auditor's negligence is capable of facilitating erosion of investors' confidence. The bank's 1991 accounts which did not reflect a true and fair view of the bank's financial condition was not qualified by an Audit Firm thus misleading those who invested in the bank's public offer of May/June 1992.

7.12 Capital injection is critical to the resuscitation of an insolvent bank. The inability of the shareholders to recapitalize Alpha led to its liquidation

7.13 A company should not serve as registrar to its own public issue of shares in view of possible conflict of interest or insider dealing it can be subjected to. Alpha management took undue advantage of the bank serving as its own Registrar to enter into the shareholders register names of persons who had not paid for shares after SEC approval. Alpha's case led to SEC's directive barring companies from serving as registrar to their own share issue.

7.14 Prosecution of directors and officers accused of contributing to a bank's failure should be handled by highly experienced and diligent lawyers. The defective charges filed by lawyers engaged to prosecute the four persons accused of contributing to Alpha's failure paved the way for their acquittal thus defeating the objective of sanitising the banking system.

8.0 CONCLUSION

8.1 "Given that the bank was engulfed in crisis early in its life which became intractable, its failure was therefore a matter of time. The directors appeared to be strange bed-fellows. The situation was compounded by inept management which was characterised by acts of insider abuse, falsification of accounts and records, weak internal control, excessive risk-tasking, wilful violation of laws and regulations, absence of risk management, contrived profits, largevolume of non-performing loans and misapplication of the bank's financial resources.

8.2 Alpha Merchant Bank graphically illustrates that any bank subjected to reckless mismanagement is bound to fail. It also provides useful lessons for various stakeholders including policy-makers, regulators and board of directors and bank management

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