Clandestine loans fortified Athens bank

Piraeus chairman Sallas and his children borrowed 100 million euros to buy secret stakes in the lender, a Reuters investigation finds

IN THE SPOTLIGHT: Chairman of Piraeus Bank Michael Sallas addresses reporters during a news conference in Athens. REUTERS/YIORGOS KARAHALIS

BY STEPHEN GREY AND NIKOLAS LEONTOPOULOS

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The chairman of one of Greece's largest banks and his family took out loans totalling more than 100 million euros to finance an undisclosed stake in the bank, according to audit documents seen by Reuters.

Offshore companies owned by Michael Sallas and his two children paid for shares in the Piraeus Bank, the country's fourth-biggest, by borrowing money from a rival bank.

Together the shares make the Sallas family the largest shareholder in Piraeus, with a combined stake of over 6 percent. The purchase of these shares has not been declared to the Athens stock exchange by Piraeus.

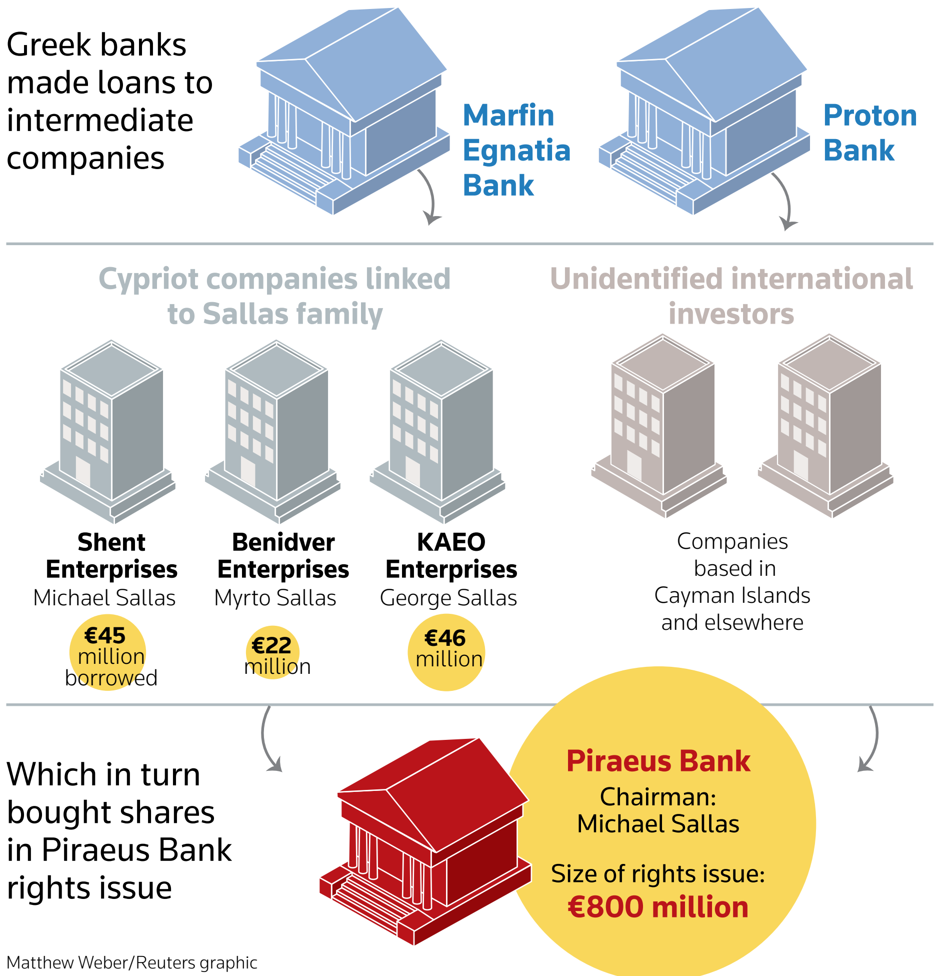
The loans to Sallas, who was executive chairman of Piraeus Bank until last month and remains its non-executive chairman, raise new questions about the stability and supervision of the Greek financial system at a time when European taxpayers and the International Monetary Fund are bailing out its banks with more than 30 billion euros.

The IMF had no comment on the issue, and a spokesman for the Bank of Greece declined to comment on Sallas's holdings in Piraeus, citing banking confidentiality guidelines. "Our supervision department cannot comment on specific prudential data available or actions taken with regard to any specific bank as such information is confidential," he said.

According to audit reports seen by Reuters, most of the money borrowed by companies linked to Sallas was used to buy shares in a Piraeus Bank rights issue in January 2011. The issue was designed to strengthen Piraeus's capital base.

The disclosure highlights concerns that Greek banks have been borrowing money from each other and using it to meet recapitalisation requirements, but not making that clear.

"This (the Greek financial system) is a closed circuit, operating as a system of power with no transparency and effective supervision," said Louka Katseli, professor of economics at the University of Athens and former Greek minister of economy. "Through triangle deals between banks, businessmen and other banks, capitalisation requirements were fulfilled without new money injected."



Matthew Weber/Reuters graphic

Piraeus Bank and Sallas declined to answer specific questions for this story, but offered an interview later this month. On Sunday Sallas issued a statement to the Greek media attacking Reuters and accusing the news agency of "slandering" and "undermining" the bank.

"It is not the first time that I or Piraeus Bank have been the target of attacks," the statement said. "What should be of concern to all of us in the present situation is the safety and the further strengthening of our banking system."

Reuters Global Editor for Ethics and Standards Alix M. Freedman said: "Our coverage of Piraeus and of the Greek banking system has been accurate and fair to every person and institution involved."

In April, a Reuters investigation found that Piraeus had failed to tell shareholders it had rented expensive properties from a network of private companies run by the Sallas family. The bank has sued Reuters for defamation over the story, claiming 50 million euros in damages.

Reuters has also reported allegations of mismanagement at the Proton Bank and at a Cyprus-based bank formerly known as the Marfin Popular Bank that operates in Greece. Proton's former president and major shareholder, Lavrentis Lavrentiadis, has vigorously denied allegations that he used the bank to loan himself and associates hundreds of millions of euros.

Andreas Vgenopoulos, former chairman of Marfin Popular Bank, now renamed Cyprus Popular Bank, has denied conflicts of interest alleged by a Greek parliamentary inquiry and Cypriot lawmakers.

It was Marfin's largest then Greek subsidiary, the Marfin-Egnatia Bank (MEB), that issued the loans to the Sallas family. According to two audit reports on Marfin, the loans were ranked among its riskiest exposures, judged both by their shortfall in collateral, which is mainly Piraeus shares, and risk of future losses to the bank.

The two audit reports, from January and May this year, were shown to Reuters by separate and unconnected sources. They were authenticated in interviews with banking sources and officials in Greece and Cyprus.

Internal Marfin auditors said executives at MEB had "failed to act in the best interests of the bank" by granting successive loans to Sallas to buy his own bank shares. By 2011 his investment in those shares, the auditors found, had "dire prospects" and had been made through special purpose vehicles and with no personal guarantees.

The auditors wrote: "Worth noting is that loan approval took place at a time when it was all but clear that the outlook for the Greek banking sector and by extension for Piraeus stock was deeply negative." The loans were issued "when our Bank [Marfin] was already in a precarious liquidity situation".

SHARE PURCHASES

According to the records, Sallas first obtained a loan agreement from MEB in May 2009. A facility for up to 150 million euros was signed off by the Marfin group's Vgenopoulos, then executive vice-chairman. A spokesman for Vgenopoulos and Efthymios Bouloutas, the bank's chief executive at the time, declined to comment on the loans due to "banking secrecy legal obligations."

By January last year, according to the first audit report, MEB loans to Sallas companies amounted to 48 million euros. But that month, "another 65 million was used" to purchase shares in Piraeus's 800-million-euro rights issue.

The Sallas family bought their shares via three separate Cyprus-based companies, according to both audit reports. The purchase brought the family's total loans to 113 million euros, secured on collateral estimated to be worth less than 30 million euros, based on Piraeus's recent share price.

The three Cyprus-based companies are Shent Enterprises, which is owned by Sallas and which has 45 million euros in outstanding loans to MEB; Benidver Enterprises, which has 22 million in loans; and KAEO Enterprises, which has 46 million in loans.

Records at Cyprus' corporate registry show that both Benidver and KAEO were owned by Michael Sallas personally until a month before Piraeus's rights issue.

Ownership was switched to two Greek companies linked to the family and in turn owned by a single Cyprus company called Avecmac, whose shareholders are anonymous. But MEB audit documents from 2012 seen by Reuters record Benidver as owned by Sallas' daughter Myrto and KAEO as owned by Sallas' son George.

SAVINGS AND LOANS: Piraeus is Greece's fourth biggest bank. **REUTERS/JOHN KOLESIDIS**

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>
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> University of Athens

Avecmac, contacted through its representative in Cyprus, did not respond to requests for comment. Myrto Sallas declined to comment; George Sallas could not be reached.

Exactly how many shares Sallas and his family bought in Piraeus last January, and in whose name they were registered, is not clear.

Some indication comes from the number of Piraeus shares pledged by the Sallas companies as collateral for the loans. Those rose by 62 million after the rights issue, bringing the total number of Piraeus shares pledged as collateral to more than 66 million, or around 6 percent of ordinary stock in the bank.

In filings to the stock exchange and in other declarations, Sallas has said he owns around 16 million shares in his name, as well as a total of around 16 million purchased through Shent Enterprises. He has declared no share purchases by his children.

Under Greek and European law, any holding in a public company of more than 5 per cent should be announced publicly. Greek law also requires all company executives "and persons closely associated with them" to make all share transactions public.

Marfin's auditors, according to their report, regard loans to Sallas and his family as "connected."

But Kostas Botopoulos, chairman of Greece's Capital Market Commission, which regulates the country's public companies, said the decision of who to define as a "person closely associated" was "considered on an ad hoc basis." There is no specific ruling on whether a spouse or children would fall in that category, he said.

Piraeus Bank released a statement saying the bank would not answer the detailed questions sent to Sallas and the bank due to "civil and criminal cases" between Piraeus and Reuters, and between the bank and a former Piraeus employee "charged with serious crimes." Piraeus has previously said the former employee had defamed the bank.

"The Bank will refute the allegations in court," the statement said. "To do otherwise would clearly be in contempt of the proceedings. In the interest of transparency, to defend its reputation and reassure its shareholders, the Bank has provided the Bank of Greece with all the relevant information."

CAPITAL BASE

The loans to investors in the Piraeus rights issue highlight a bigger concern in the Greek banking sector. Piraeus issued more shares last year to strengthen its capital base, enabling it to score higher in European bank stress tests.

The successful issue, Sallas said at the time, showed "a sign of confidence in Piraeus Bank, the Greek banking system and of course the prospects of the Greek economy."

But Sallas did not make public the loans he and other shareholders had taken out to help make the rights issue a success.

In all, according to loans disclosed so far, nearly one-fifth of the new capital in Piraeus was raised with financing from other Greek banks - including another 20 million euros or so loaned by MEB to investors, and 70 million euros loaned by the Proton Bank. The Proton loans went through offshore companies in tax havens such as the Cayman Islands.

Proton has since been nationalised after Greece's money-laundering authority alleged fraud and embezzlement in cases unrelated to Piraeus or MEB.

According to several European banking and accounting experts, if banks loan money to finance major stakes in other banks, then the industry's regulator, in this case the Bank of Greece, should deduct the same amount from the capital the lending bank claims to hold.

Dr Peter Hahn, a fellow at London's Cass Business School and an adviser to the UK Financial Services Authority, said that a loan scheme whose only means of repayment was shares in another bank should, under international rules, be treated as if the lending bank was directly purchasing shares in the other bank. "The equity in the lending bank would otherwise be supporting risk of loss in both banks," he said.

> "It's our money and it has been given without controls. It's a disaster
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> **Hans-Peter Burghof**
> University of Hohenheim


SPEAKER: Then Executive Vice Chairman of Marfin Popular Bank Andreas Vgenopoulos. Marfin loaned money to Sallas and his family which was used to buy shares in Piraeus.
REUTERS/ANDREAS MANOLIS

Hans-Peter Burghof, a professor of banking and finance at the University of Hohenheim, Germany, said that billions of euros had been given to the Greek banking system without adequate supervision of the sector. "It's our money and it has been given without controls. It's a disaster," he said.

If banks lent to finance each other's shares, he said, then "this way you can produce as much equity as you like and make banks as big as you like. It is not real equity." He likened it to "a kind of Ponzi scheme."

Burghof said that, whether deemed to be covered by regulations or not, if bank equity was raised in this way, the banks and companies involved should be treated as a consolidated whole. "If the regulator finds out (about loans from one bank to finance share purchases in another), he should discount this equity," he said.

The European Banking Authority, which is meant to safeguard the stability of the financial system and transparency of markets, generally agreed with that analysis, though a spokeswoman said there may be exceptions in the case, say, of a "financial assistance operation".

There is no indication in their financial statements that either Proton or Marfin made deductions in their capital levels after their loans for Piraeus shares.

In a statement the Bank of Greece said it does not ordinarily require capital deductions from banks that lend money for the purchase of shares in other unconnected banks.

"European Union law does not prohibit granting loans to an entity (person or organisation) in order to participate in a share capital increase of another credit institution," the bank said. Such a deduction from regulatory capital would only take place if a bank granted loans to buy its own shares, it said.

It added that the disclosure of major stakes (over 5%) in a public company was "indeed a requirement on the stakeholder". But this was policed by the Capital Market Commission, not the Bank of Greece.

The CMC said that shareholders, in calculating whether they hold 5% or more, should aggregate holdings if they have an agreement to act together.

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