

# **STATUTORY PROTECTION OF BANK DEPOSITS GRADUALLY EXTENDED TO INCLUDE ALSO LEGAL ENTITIES**

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Since the beginning of December 2001 there has been in force an absolute majority of the provisions of what is to date the most extensive and primarily for depositors the most important amendment to the Deposit Protection Act (National Council SR Act no. 118/1996 Z.z. as amended). This amendment is published in the Collection of laws of the SR under no. 492/2001 and its aim is primarily the gradual harmonisation of the Deposit Protection Act with the requirements of the European Union for protection of bank deposits.

For this reason statutory bank deposit protection is to be gradually extended from the hitherto protection of bank deposits of only natural persons (citizens) also to the bank deposits of the majority of legal entities. As part of this the first extension of bank deposit protection to include also deposits of certain selected non-business legal entities occurred on 1 December 2001. Gradually the total maximum amount of compensation payments that the Deposit Protection Fund may pay out for unavailable bank deposits protected by law will be increased.

Also for these reasons it was among other things necessary to increase the amount of contributions which banks and branches of foreign banks (hereinafter simply "banks") are obliged to pay to the Deposit Protection Fund (hereinafter simply "DPF") so that there is guaranteed the payment of unavailable bank deposits in cases where a bank becomes insolvent, i.e. when the bank is declared to be unable to pay out deposits, as well as in the case where a court through a decision issued in bankruptcy proceedings on a bank's assets suspends deposit handling in the bank even prior to the bank's being declared as unable to pay out deposits.

## **Decrease in percentage protection of deposits**

For natural persons, i.e. for citizens having bank deposits protected by statute prior to December 2001, there is the extremely important change that compensation for unavailable deposits will no longer be provided in the amount of 100% of the nominal value of the deposit, but exclusively in the amount of 90% of the nominal value of the protected unavailable bank deposit. The percentage decrease in the protection of bank deposits from 100% to a maximum 90% is permitted by the EU, although such a decrease is not stipulated in its regulations. The Associ-

ation of Banks' request for a lowering of the percentage protection of bank deposits was accepted as economically justified, because a significant share of depositors deposited their money in the amount protected by statute in banks paying the highest interest rates. In doing so depositors did not take account of published expert information on the risk and the weak economic and financial situation of these high-risk banks, but rather for the case of a high-risk bank becoming insolvent and deposits in the high-risk bank being unavailable they relied on the fact that compensation for deposits in these banks would in the end one way or another be paid out to depositors in the full amount by the DPF.

The aim of the approved percentage reduction in bank deposit protection is to move to a situation where depositors looking for banks in which to deposit their money do so not simply on the basis of the highest promised interest rates, but also monitor information on the economic and financial situation of individual banks. Incidentally rational behaviour of depositors could substantially affect the Association of Banks itself, which as a professional organisation has an overview of all banking subjects in Slovakia and of the individual types of bank services provided. The Association of Banks' could thus provide up to date and qualified information to the public from what rate are the promised interest payments on deposits economically unrealistic or speculative, and could possibly inform the public also about individual economically risky banking subjects.

## **Changes to the maximum limit of compensation for deposits**

The maximum possible amount of compensation which the DPF pays out for unavailable bank deposits has since the beginning of December been unified for all banking subjects including building societies. Up until this date the applicable amount of the maximum limit for deposits in building societies had been twice that for other banks. From 1 December 2001 for all banks including building societies there applies the rule that the maximum possible amount of compensation to be provided to one depositor for unavailable deposits in one bank is equal to thirty times the average monthly salary in Slovakia for the past four statistically concluded calendar quarters prior to the occurrence of the bank's insolvency.



From 1 July 2002 however the maximum possible amount of compensation to be provided to one depositor for unavailable deposits in one bank will be raised to forty times the average monthly salary in Slovakia for the past four statistically concluded calendar quarters prior to the occurrence of the bank's insolvency.

This valorisation mechanism of gradually raising the maximum possible amount of compensation depending on the rate of growth of the average monthly salary in the SR thereby actually being dependent on the growth of the Slovak economy will apply up until Slovakia's accession to the EU.

Following Slovakia's accession to the EU the maximum possible amount of compensation to be provided to one depositor for unavailable deposits in one bank shall be raised to 20 000 EUR expressed in Slovak koruna. This calculation will be made according to the exchange rate declared by the National Bank of Slovakia as at the date when the deposits in the insolvent bank became unavailable.

Naturally, a requirement for the payment of compensation in the maximum possible amount is that one depositor had in the insolvent bank deposits at least high enough that 90% of the net nominal value of all the deposits of the one depositor in the insolvent bank (less any loans made to the depositor by the insolvent bank and also less any lapsed deposits of the depositor in the insolvent bank) is equal to at most the maximum possible amount of compensation. Where 90% of the net nominal value of all the deposits of the one depositor is in total an amount greater than the maximum possible amount of compensation, then the depositor shall get compensation at most in the amount of the maximum possible amount of compensation.

The same rules apply for the maximum possible amount of compensation paid to other authorised persons than depositors, for example for compensation paid to a depositor's inheritor.

### **Procedure in extending bank deposit protection**

From 1 December 2001 the system of bank deposit protection was extended in the case of bank deposits of natural persons as well as to those bank deposits of natural persons running a business and which are set up for the purposes of conducting business. This primarily concerns the bank deposits of sole traders, independent farmers, private medical doctors and bank deposits of similar small entrepreneurs set up for the purposes of conducting business. Until the beginning of September 2001, natural persons running a business had protected by statute exclusively those bank deposits which were not set up for the purposes of conducting business.

Similarly from 1 December 2001 the system of bank deposit protection has been extended also to include bank deposits of selected types of legal entities of a not-for-profit non-business nature. This concerns foundations, other than investment funds, not-for-profit organisations providing

services of general benefit, citizen associations and owner partnerships of apartments and non-residential premises.

On the accession of the SR to the EU the system of bank deposit protection is to be extended also to include bank deposits of other legal entities (for example to the bank deposits of business entities) with exceptions permitted by the EU.

From the system of statutory bank deposit protection are to be permanently excluded primarily:

- legal entities whose activity is focused on handling financial resources, but also certain other legal entities. This concerns banks, securities traders, central securities depositories, stock exchanges, commodity exchanges, assets management companies for collective investment including assets in mutual funds, insurance companies, additional pension insurance companies, postal businesses, operators of lotteries and similar games and the Export-Import Bank SR, as well as other Slovak legal entities or foreign legal entities (including their branches) having only partially the same line of business;
- all legal entities which by law must have the closing of accounts compulsorily verified by an auditor, this concerns for example joint-stock companies;
- the state, state funds, municipal authorities and towns, regional authorities as well as their budgetary organisations and contributory organisations;
- all bodies of public authority and all legal entities established by law, for example the National Bank of Slovakia and the Financial Market Office.

For completeness it is necessary to draw attention also to the unamended provision of the Deposit Protection Act, according to which compensation from the DPF does not appertain to any depositors validly convicted by a court for the partial or complete causing of the insolvent bank's inability to pay out deposits, or for the laundering of proceeds from criminal activities and on the basis of which they gained the deposits in the insolvent bank.

Naturally the Deposit Protection Act does not protect all bank deposits of natural persons nor all bank deposits of legal entities included in the system of statutory deposit protection. It protects only those bank deposits of natural persons and bank deposits of legal entities that fulfil the requirements prescribed by the Deposit Protection Act. No natural person nor legal entity has protected those bank deposits that the Deposit Protection Act excludes from the system of statutory deposit protection.

### **Bank deposits protected by the act**

The latest amendment to the Deposit Protection Act specified the definition of a deposit. For these purposes a deposit is considered to be a liability (debt) of a bank in respect of a depositor for the payment of funds which the depositor entrusted to the bank in a banking transaction performed on their own behalf and on their account or which the bank accepted as payment in favour of the de-

positor, and this including interest and other financial benefits (for example premium financial winnings) connected with the entrusting of such funds (i.e. with the deposits held). Here a deposit is also considered to be the share of a depositor in joint deposits of multiple depositors where the personal data of all joint depositors is recorded in the bank's records before the bank became insolvent and similarly a deposit is considered to be the share of a depositor in notarial safekeeping where the notary delivered to the bank in writing the personal data and data on the amount of the shares of individual depositors in notarial safekeeping before the bank became insolvent.

No other financial liabilities of a bank in respect of depositors, primarily financial liabilities from damage caused and financial liabilities from contractual penalties, are considered as a deposit and therefore the DPF may not pay out compensation to anyone for such financial liabilities of a bank.

The Deposit Protect Act however does not protect all depositors' deposits. The bank deposits of a natural person are protected by the act exclusively in the case where the bank according to its records – which must be administered also prior to the occurrence of the bank's insolvency – maintains these deposits in favour of at least the name, surname, birth ID no. (or date of birth) and the permanent address of the natural person who is the depositor. The bank deposits of a legal entity included in the system of statutory bank deposit protection is protected by law only in the case where the bank according to its records – which must be administered also prior to the occurrence of the bank's insolvency – maintains these deposits in favour of at least the title, identification number (where this has been assigned) and the address of the registered office of the legal entity included in the system of statutory bank deposit protection and which is the depositor. In this the bank's register according to records administered by the bank also prior to the occurrence of the bank's insolvency must be stated the name, surname and permanent address of the natural person or natural persons who form the statutory body or who are members of the statutory body of the legal entity.

Apart from this, the Deposit Protect Act explicitly excludes from the system of statutory deposit protection various types of bank deposits regardless of who is the depositor and what data the bank has recorded in its register on the depositors of these deposits. From the system of statutory bank deposit protection are excluded primarily:

- all bearer deposits, namely in particular all bearer deposit books, but also all bearer deposit certificates, bearer certificates of deposit and bearer treasury bills;
- all deposits in the form of publicly tradable securities (i.e. securities traded on the stock exchange) or in the form of bonds, bills and cheques (even where this concerns registered securities);
- all joint deposits where there are not, prior to the bank's becoming insolvent, recorded in the bank's register the personal data of all joint depositors, as well as all no-

tarial deposits for which the notary has not delivered in writing the personal data and shares of individual depositors in the notarial deposit prior to the bank's becoming insolvent.

For completeness it is necessary to draw attention also to the provisions of the Deposit Protection Act, according to which compensation from the DPF does not apply to any lapsed deposits, nor to any deposits of depositors who according to the Banks Act were among persons with a special relationship to the bank at any time in the period of one year prior to the bank's becoming insolvent – this concerns primarily deposits of the highest representatives and large shareholders of the insolvent bank.

The DPF may not pay out compensation to anyone for bank deposits and other financial claims excluded from the system of statutory deposit protection. The claim for these deposits and other financial claims may however be applied against the insolvent bank for example in bankruptcy court proceedings for the assets of the insolvent bank.

### Proving the right to compensation

The amendment to the Deposit Protection Act has partially changed also the rules for proving the right to the payment of compensation from the DPF for unavailable bank deposits protected by law and held in an insolvent bank. A change to these rules was necessary, since from 1 December 2001 the act has been extended also to selected types of legal entities.

Each natural person and similarly each legal entity which requests payment of compensation from the DPF for unavailable bank deposits must prove that they have the right to payment of the requested compensation for bank deposits protected by law and held in the insolvent bank. This right is proven in particular through a document on the deposit relationship between the applicant and the insolvent bank (e.g. through presentation of a deposit book in favour of the applicant), or through a decision of the court or other relevant public authority (e.g. through a decision on inheritance according to which the applicant inherited the bank deposits protected by law).

For payment of compensation for deposits, the payment of which was tied (pledged) to the consent of a third party (i.e. an entity other than the depositor) or which served as a letter of credit in favour of the third person it is necessary to also submit the written consent of the authorised third party with their officially attested (verified) signature.

A natural person requesting compensation, besides proving their right to the payment of compensation, must also prove their identity. Identity is proven through a valid document of identity, namely an ID card, or valid passport, diplomatic passport or service passport, and a foreigner may prove their identity also by an official document of residence in the SR. Any representative of the applicant must prove their identity by a valid document of identity and to submit a document on their authorisation to repre-



sent the applicant, for example a legally valid decision of the court on their appointment as guardian of the applicant, or a mandate for representing the applicant in the matter of the application for payment of compensation and in taking receipt of the compensation with an officially attested (verified) signature of the applicant. A parent who requests compensation for their child and who has not been exempted of parental rights must present their valid ID card or other valid document of identity and at the same time hand over the original or officially attested (verified) copy of the child's birth certificate.

A legal entity requesting compensation must besides proving its right to the payment of compensation also submit an extract from an official register or other official records in which it is entered, this being not older than of one month prior to the application of the right to compensation. From such an extract it is among other things apparent also whether the applicant legal entity is among the legal entities included in the system or excluded from bank deposit protection and who is the statutory body of the applicant legal entity that may under the act automatically represent it also in an application for compensation and in taking receipt of the compensation. The representative of the applicant legal entity must prove their identity by a valid document of identity and must submit a document on their authorisation to represent the applicant legal entity. If however the applicant legal entity is not represented by its statutory body, but by another representative, this representative must submit also a mandate or proxy to represent the applicant legal entity with an officially attested (verified) signature of the statutory body of the applicant legal entity.

### **Other changes to the Deposit Protection Act**

The latest amendment to the Deposit Protection Act with effect from 1 December 2001 changed also various previously valid provisions of the Deposit Protection Act.

From the point of view of clients of an insolvent bank it is necessary to point out firstly the fact that from the moment when deposits in the bank become unavailable up until the ending of compensation payments for deposits there is under the act directly suspended deposit handling in the insolvent bank, the advancement of receivables against the insolvent bank, as well as the setting off of mutual receivables between the insolvent bank and other entities. For the same period the insolvent bank is prohibited from accepting further deposits, providing loans, bank guarantees and letters of credit and from concluding other transactions by which the receivables or liabilities of the insolvent bank in respect of their entities would be increased. The insolvent bank is also obliged to immediately "freeze" handling with bank payment cards issued in respect of accounts in the insolvent bank. It is necessary however to draw attention to the fact that in no way is there stopped or interrupted the repayment of loans and interest on loans which the insolvent bank provided to its clients.

Through the latest amendment to the Deposit Protection Act there are also changed certain provisions governing mutual relations between banks and the DPF, and similarly certain provisions governing the workings of the DPF, for example provisions on the bodies of the DPF and on the cooperation of the DPF with institutions for the protection of bank deposits in other countries. Chiefly however, the upper limit has been raised for ordinary contributions and extraordinary contributions, which the banks are obliged to pay into the DPF. The upper limit of the ordinary contribution has been raised from 0.3% to 0.75% and the upper limit of the extraordinary contribution has been raised from 0.3% to 1.0% of the total amount of protected bank deposits held in individual banks.

The amendment has also explicitly defined that the provisions on liability according to the Civil Code apply to legal relations between the DPF and an insolvent bank for which the DPF paid out compensation for unavailable deposits, unless the Deposit Protection Act governs these relations differently. In connection with this it is necessary to mention also the previous amendment to the Deposit Protection Act, which is published in the Collection of Laws of the SR under no. 397/2001 and which came into effect on 5 October 2001. This previous amendment altered simply the wording of the provision on receivables of the DPF in respect of insolvent banks and for which the DPF paid out compensation for unavailable deposits. The aim of this amendment was to exclude the possibility that relations between the DPF and insolvent banks in the future may use a tendentious decision, such as which was accepted by one of the senates of the Supreme Court of the SR in a dispute between the DPF and Dopravná Banka, and for which the DPF paid out compensation for unavailable deposits.

### **Conclusion**

It is necessary to draw attention to the fact that claims for compensation and the amount of compensation for deposits held in banks that went bankrupt prior to 1 December 2001 are to be assessed and ascertained exclusively in accordance with those provisions of the Deposit Protection Act which applied up to 1 December 2001. For this reason no legal entity has a claim for compensation for deposits in banks that went bankrupt prior to 1 December 2001 (e.g. for deposits in Devín Banka). It does however mean that for deposits protected by law in banks that went bankrupt prior to 1 December 2001 (e.g. for deposits protected by law in Devín Banka) the DPF shall pay out compensation to natural persons in the amount of 100%, not only in the amount of 90% of the nominal value of the deposit. Naturally it implies here that the maximum possible amount of compensation provided to one depositor for unavailable deposits in individual insolvent banks may not exceed thirty times the average monthly salary in Slovakia that was statistically known as at the date when these banks became insolvent.