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Transformation of a branch of a credit institution into a bank operating as a joint stock company in the Polish legal system based on the proposal of the amended Banking Law Act

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*Transformation of a branch of a credit institution into
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Przekształcenie filii instytucji kredytowej w bank działający jako spółka akcyjna
w polskim systemie prawnym w oparciu o wniosek znowelizowanego Aktu o Prawie Bankowym

Introduction

The Banking Law Act in force was enacted by the Sejm of the Republic of Poland on 29th August, 1997 and entered into force on 1st January, 1998. According to the legislator's intention, the act was to put an end in normative terms to the transitory period in the development of the Polish banking system and launch a new phase of its operation. After it was passed, it was assessed – both by officials and in expert publications – as “ensuring high compliance” with regulations of the European Union.

Having joined the European Union, the Republic of Poland, being its Member State, is obliged to ensure and enable a credit institution licensed by a relevant supervisory authority of another member state to enjoy the freedom to provide financial services within its own territory. In view of the above, an act dated 23rd August, 2001 regarding the amendment of the Banking Law Act and other acts was adopted in 2001, regulating the above-mentioned issues.

1. Conducting business activity in Poland by credit institutions through a branch

The concepts of a credit institution and a branch of a credit institution are defined in Article 4 par. 1 subpar. 17 and 18 of the Banking Law Act in force. Pursuant to

Article 48i of the Banking Law Act a credit institution may run business activity in Poland via a branch or within the framework of its cross-border activity. A branch of a credit institution does not have to obtain a permit of the Polish Financial Supervision Authority. Nevertheless, competent supervisory authorities of the home Member State of a credit institution are required to submit a relevant notification to the Polish Authority. According to Article 141c par. 1 of the Banking Law Act, the activity of a credit institution in Poland is basically supervised by competent supervisory authorities of the home Member State of an institution. Pursuant to Article 141c par. 2 of the Banking Law Act the Polish Financial Supervision Authority is obliged to exercise supervision of branches of credit institutions with respect to compliance with relevant cash flow liquidity by a branch. Additionally, the Polish Financial Supervision Authority has specific response measures at hand specified in Article 141a of the Banking Law Act to be applied if a credit institution conducting business activity in Poland via a branch or engaging in cross-border activity does not observe the Polish legal regulations.

In order to provide an answer to the question about advantages and disadvantages of conducting business activity via a bank or a branch of a credit institution it is necessary to analyze the following issues¹:

1. Principles and rates of tax burdens, it is also necessary to attach great importance to the principles of creating allowances / provisions for receivables and recognizing them as tax deductible costs in terms of taxes.

2. Principles concerning the minimum reserves; a bank and a branch of a credit institution operating in Poland are both obliged to comply with the requirements of the National Bank of Poland with regard to minimum reserves. Moreover, according to the guidelines of the European Central Bank branches located outside the Eurozone, which applies in case of Poland, are not subject to the minimum reserve system of the Eurosystem, whereas branches of credit institutions operating in the Eurozone which do not have a seat within its territory are subject to the minimum reserve system of the Eurosystem.

3. Payments made to the benefit of supervision authorities and the deposit guarantee scheme; the European Union observes the principle of home country supervision and guarantee. The amount of payments made to the benefit of supervision authorities and guarantee authorities differs in respective countries, and in consequence, the payment made by a specific bank / branch of a credit institution depends on the affiliation to the specific system, e.g. deposit guarantee scheme.

4. Principles of consumer protection, including borrowers and the so called anti-usury regulations; in Poland the maximum amounts of interest and charges to be paid by a client refer both to banks and branches of credit institutions².

¹ M. Zaleska, *Bank czy oddział instytucji kredytowej*, „Bank” 2008, No. 5.

² A list of branches of credit institutions, specifying their identification numbers necessary to perform interbank settlements, is available on the Internet site of the Polish Financial Supervision Authorities in the list “Banks in Poland”.

2. Specific situation: transformation of a branch into a subsidiary

The purpose of the planned amendment is to introduce in the Banking Law Act in force regulations making it possible to transform a branch of a credit institution operating in Poland into a domestic bank operating as a joint stock company, specifying at the same time conditions, principles and procedures governing the transformation³.

Talking of the most important consequences of transforming a branch of a credit institution into a domestic bank a mention should be made of establishing a new domestic bank and parallel closure of a branch of a credit institution, universal succession of rights and obligations of a credit institution arising from business activity of a branch, taking over supervision of business activity of a branch converted into a bank by the Polish Financial Supervision Authority and entrusting the Bank Guarantee Fund with the guarantee of deposits accumulated during the branch activity.

It must be emphasized that the possibility of transformation into a domestic bank is especially vital in case of branches of credit institutions which have gained a significant share on the Polish market or have had a relatively high scale of operation measured with the volume of assets or deposit or credit portfolio, and run a banking company, having infrastructure at its disposal allowing to launch an independent activity as a bank. Such branches may generate a substantial risk on the part of a credit institution itself as well as the Polish financial market. It follows from the fact that in such cases it may become difficult to ensure efficient supervision of business activity carried out by a branch of a credit institution – being appropriate to the scale of the activity, in particular during the period of turbulence on financial markets. In this context it is necessary to point out that solutions put forward in the proposal can make a positive contribution to maintaining financial stability on the domestic market, representing an instrument of the so called anti-crisis package. Considering the fact that a branch is placed under direct supervision of the Polish Financial Supervision Authority and deposits accumulated by a branch are subject to guarantee of the Bank Guarantee Fund, transformation can offer benefits to clients of a branch of a credit institution, and in particular to depositors who entrusted a branch with their money. The proposed solution can also offer an alternative to a credit institution as transformation of its branch into a domestic bank allows to expand the scale of operation in Poland by bolstering confidence of the local market and clients on the one hand, and by gaining additional funds earmarked for development via recapitalization of the bank (subscription of shares of the new issue) by the strategic partner on the other. In case of disposal of shares after establishing a bank, the instrument providing for transformation of a branch into a domestic bank can be treated as a method (way) allowing a credit institution to abandon its activity on the Polish market.

³ Proposal of the act amending the Banking Law act, corporate income tax act and Tax Ordinance available in the Public Information Bulletin of the Finance Ministry.

In the proposal of the amended act it should be pointed out that its objective is to eliminate the different legal treatment of two options (manners) allowing an interested entity (investor) to enter the market of banking services in Poland – i.e. establishing a new bank and taking over control of an existing bank (e.g. via acquiring the majority shareholding of the bank). As opposed to taking control of a bank, in case of establishing a bank, it is not possible for the founder to make commitments regarding the bank being set up or prudent and sound management of the bank, and in consequence, the Polish Financial Supervision Authority cannot take them into account while preparing an evaluation drawn up in connection with the procedures relating to a banking authorisation. There is no doubt that it can make it difficult for potential bank founders to prove that they meet the requirement mentioned in Article 30 par. 1 subpar. 2 of the Banking Law act, i.e. “giving adequate guarantee of the sound and prudent management of the bank” and as pointed out by the Financial Supervision Authority, it can thereby constitute an unjustified obstacle to establishing new entities on the market of banking services.

The main purpose of the amendment is to enable a credit institution conducting a banking activity in Poland via a branch to transform the branch into a domestic bank. The transformation is to consist in establishing by a credit institution a domestic bank operating as a joint stock company by contributing all assets of the branch intended for conducting business activity by the branch, provided that they constitute one (banking) company or its independent organisational unit. A company within the meaning of the proposed regulations is to incorporate a group of all intangible assets and fixed assets intended for conducting business banking activity in Poland via a branch. It will include in particular fixed assets and financial means used for conducting business activity and receivables and liabilities resulting from the activity, and in particular deposits. Therefore, only a branch running a banking business, with infrastructure and operational preparation making it possible to conduct an independent activity as a bank may undergo transformation into a domestic bank.

A credit institution could be the sole and exclusive founder of a bank established as a result of branch transformation. The regulation would be specific in relation to Article 13 par. 1 and 3 of the Banking Law Act. It is to ensure that in economic terms the establishment of a bank will involve only a change of the form under which a given credit institution conducts banking operations in Poland, and will not entail setting up of a new entity (for such cases there is an ordinary procedure regulating the establishment of a domestic bank). However, it is evident that after the transformation is completed, the bank will be subject to the same regulations of the companies’ law as other banks operating as joint stock companies.

Establishing a bank as a result of branch transformation would ensue according to the principles governing the “ordinary” process of setting up a bank and would be directly subject to the regulations of chapter 2 of the Banking Law Act, barring application of Article 30 par. 2 and 4 and Article 36. The exclusion of application of Article 30 par. 2 and 4 of the Banking Law Act relating to the limits of in-kind contributions

to the initial capital results from the construction of the proposed transformation, according to which it is to take place by making in-kind contributions to the full initial capital of a newly established bank in the form of all assets intended for conducting business activity by a branch of a credit institution. However, it must be noted that exclusion of application of Article 36 related to issuing an authorisation from the Polish Financial Supervision Authority to launch activity by the newly established bank is connected with the necessity of ensuring business continuity of the entity. The bank is established on the basis of a branch of a banking company already in operation, and on the one hand, there is no need to grant an additional authorisation to launch operational activity, but on the other hand, such a requirement would have to lead to periodic suspension of operational activity conducted by a branch, and subsequently a bank during the period from its registration (corresponding with the cancellation of the branch entry in the register) to issuing an authorisation to launch operational activity.

The decision of the Polish Financial Supervision Authority on issuing an authorisation to establish a bank as a result of branch transformation must be preceded by a supervisory audit to be held in the branch. The audit is to be subject to the regulations related to financial supervision audits in banks, and in consequence the audit is to be comprehensive and is to be used to verify the actual present financial standing of the branch, and to prepare for conducting operating activity via a bank being formed. Thus, while performing control activities, it is necessary to exclude regulations specifying the scope and division of powers of relevant supervision bodies and the Polish Financial Supervision Authority with regard to exercising supervision of a branch of a credit institution.

The proposed provisions of the amendment define the start of the activity by the bank formed as a result of transforming a branch of a credit institution as the date of the bank's entry in the business register. As the bank's registration is completed, the entry of the branch of a credit institution in the business register becomes automatically cancelled. The purpose of the regulation is to ensure that the bank being established starts its activity upon acquisition of legal personality, and to avoid a situation in which due to different dates of the bank's business registration and deregistration of the branch two entities would conduct business activity acting as the same company. The mentioned regulation plays a special role with regard to next articles of the proposal, dealing with universal succession.

Transformation of a branch into a bank involves universal succession – the newly established bank by operation of law takes over all rights and obligations of a credit institution arising from the branch activity. Universal succession was regulated in the proposed law by analogy to the succession that ensues upon merger of companies effected on the basis of Article 494 of the Code of Commercial Companies. It involves in particular transfer of all liabilities (including e.g. deposits or credit cards held) or receivables (e.g. credits) and related rights (mortgages and securities) to the bank, whereas the transfer of rights disclosed in the land and mortgage registers or other registers to the bank is effected in the registers after the bank applies for it.

According to the amendment, it is proposed to introduce a requirement for the bank established as a result of transforming a branch of a credit institution to maintain the solvency ratio on the minimum level of 12% during the first 18 months of the bank activity. This regulation excludes thereby application of Article 128 par. 1 subpar. 3 of the Banking Law Act with regard to a bank formed as a result of transforming a branch of a credit institution, according to which a bank launching its operations is obliged to maintain the solvency ratio on the minimum level of 15% during the first 12 months of its activity, and at least 12% during the next 12 months.

2. Transformation vs. the Polish Deposit Guarantee Scheme

A transformed branch of a credit institution would to some extent “by default” fall under the Polish deposit guarantee scheme. Given the above, it would be necessary to consider whether an entry fee should be charged upon transformation of a branch of a credit institution into a domestic bank and placing the deposits accumulated in the branch of a credit institution under the guarantee of the Polish Bank Guarantee Fund. What would be the best solution in such a situation?

It appears that given the stability of the domestic deposit guarantee scheme it would be advisable to determine the fee based on the accumulated volume of contributions to be hypothetically paid by the branch of a credit institution if it was a member of the Polish deposit guarantee scheme from the start of its operations in Poland. Considering the fact that now the European Union does not offer such solutions, it seems necessary to introduce appropriate domestic solutions, which would impose an obligation on a domestic bank established as a result of transforming a credit institution to pay a one-off entry fee. The above-mentioned solution would secure the financial means of the Bank Guarantee Fund and would be neutral with regard to the level of the coverage ratio of the deposit guarantee scheme.

The proposed amendment of the European Union solutions relating to deposit guarantee schemes with regard to institutions switching to another deposit guarantee scheme during their business activity offers a relatively similar (though not the same) solution. The idea of the recommended solution is to transfer some contributions paid to the deposit guarantee scheme under the activity conducted so far to the deposit guarantee scheme taking over the coverage.

However, it is necessary to analyze whether it is justified to draw analogies with the proposed amendments of the directive on deposit guarantee schemes with regard to the proposed imposition of the obligation to pay a one-off entry fee upon joining the domestic deposit guarantee scheme by a newly established bank. In the current wording of the proposal of the directive on deposit guarantee schemes prepared by the Hungarian Presidency it is stated in Article 12(3) that in case of switching to another deposit guarantee scheme the contributions paid during the 12 months prior to joining another deposit guarantee scheme, with the exception of the extraordinary

contributions mentioned in Article 9(3), are reimbursed (Article 12(3) – *If a credit institution ceases to be member of a scheme and joins another scheme, the contributions, with the exception of the extraordinary contributions according to Article 9(3), paid during the 12 months preceding the withdrawal of membership shall be transferred to the other scheme. This shall not apply if a credit institution has been excluded from a scheme pursuant to Article 3(3).*).

It must be stressed that the obligation to reimburse the contributions is imposed on the deposit guarantee scheme of the country where a given credit institution has so far conducted its operations. In case of transforming a branch of a credit institution into a domestic bank and switching subsequently to another deposit guarantee scheme, it would be the deposit guarantee scheme the branch has belonged to so far – and not the entity undergoing transformation – that would be responsible for reimbursing the contributions.

It is worth pointing out that the proposal of the Directive dated 16th July 2010 submitted to the European Parliament clearly lists the principles that should apply to the process of switching to another deposit guarantee scheme. In the justification of the proposal, under item 7.6 related to cross-border cooperation it was stressed that banks reorganising themselves in a way that causes their membership of one deposit guarantee scheme to cease and entails membership in another deposit guarantee scheme will be reimbursed their last contribution so that they can use these funds to pay the first contribution to the new deposit guarantee scheme. At the same time it was stated in Article 9 that one-off entry fees for admitting into a system may not be charged (*Article 9(1) – Member States shall ensure that Deposit Guarantee Schemes have in place adequate systems to determine their potential liabilities. The available financial means of Deposit Guarantee Schemes shall be proportionate to these liabilities. Deposit Guarantee Schemes shall raise the available financial means by regular contributions from their members on 30 June and 30 December of each year. This shall not prevent additional financing from other sources*).

Conclusion

In the context of the Polish formal and legal solutions it is not possible to clearly state which form of activity is more favourable. It is also difficult to clearly identify the advantage of conducting business activity as a bank over carrying out business activity via a branch of a credit institution. Despite the fact that the European Union solutions provide some instruments, it is not groundless to take a different stance and approach to the issue of switching to another deposit guarantee scheme. According to the European Union proposals upon “acquisition” of a new institution into the domestic deposit guarantee scheme in first place we have to do with acquiring a new member of the scheme and future payer of contributions and not only with transfer of potential risk and the problem of insolvency. Furthermore, it should be considered if potential

introduction of an additional entry fee into the Polish legal regulations to be paid to the Bank Guarantee Fund by a domestic bank formed as a result of transformation could be believed to represent competition distortion. Accession of an established domestic bank to the deposit guarantee scheme does not involve only new additional risks on the part of the Fund, but it also poses a specific risk to the bank joining the Fund. A domestic bank established as a result of branch transformation, joining the domestic scheme, has not paid any annual fees to the Bank Guarantee Fund before. However, in case of bankruptcy of other domestic banks it would have to – if need be – participate in covering pay-outs due to depositors under the established fund for protection of guaranteed deposits, equalling the volume of deposits held. Summing up, the risk connected with joining the Bank Guarantee Fund is distributed over two parties – the Fund and the domestic bank formed as a result of branch transformation. According to the Author, the best solution would involve preparing a proposal of standards regulating the above-mentioned issue on the European Union level in the context of planned solutions with regard to the Deposit Guarantee Schemes and Resolution.

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W wyniku przystąpienia do Unii Europejskiej Polska jako kraj członkowski zobowiązana jest zapewnić i umożliwić instytucji kredytowej mającej uprawnienia udzielone jej przez właściwe władze nadzorcze innego kraju członkowskiego korzystanie z usług finansowych w obrębie jej własnego terytorium. Pojęcia instytucji kredytowej oraz filii instytucji kredytowej określone są w Art. 4 par. 1, podpar. 17 i 18 obowiązującego Aktu o Prawie Bankowym. Celem planowanej nowelizacji jest wprowadzenie do obowiązującego Aktu o Prawie Bankowym przepisów umożliwiających przekształcenie filii instytucji kredytowej prowadzącej działalność w Polsce w bank krajowy funkcjonujący jako spółka akcyjna, wraz z jednoczesnym określeniem warunków, zasad i procedur kierujących tym przekształceniem. W odniesieniu do polskich rozwiązań formalnych i prawnych nie jest możliwe stwierdzenie, która forma działalności jest bardziej korzystna. Trudno jest również jasno określić, czy korzyści wynikające z prowadzenia działalności biznesowej jako banku przeważają nad korzyściami wynikającymi z prowadzenia filii instytucji kredytowej. Przekształcenie dotychczas prowadzonej działalności bankowej w filię instytucji kredytowej pociąga za sobą określone problemy, nie przynosząc równocześnie żadnych konkretnych korzyści. Przekształcona filia instytucji kredytowej, zostałaby objęta – do pewnego stopnia „poprzez niewywiązywanie się ze swych zobowiązań finansowych” – Programem Gwarancji Polskiego Depozytu (the Polish Deposit Guarantee Scheme).