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Deposit Protection in the European Economic Community†

Laura Shea*

I. INTRODUCTION

The European Community (EC) Proposed Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to Deposit Guarantee Schemes1 (Proposed Directive) was published April 14, 1992. The final Directive on the subject should be published in 1993. Before commenting upon the Proposed Directive, it is useful to review the history of deposit protection and related EC banking Directives and proposals.2 This article will review the most important aspects of the United States and three Member State’s depository protection schemes. In addition, this article will compare these four depository protection schemes with the EC Proposed Directive.

Deposit protection schemes traditionally have been introduced as the result of some financial disaster. In the United States, the Federal Deposit Insurance Corporation (FDIC) was established in 19333 due to bank failures in the Great Depression. Most of the EC Member States did not introduce deposit protection schemes until the late 1970s or early 1980s. These deposit protection schemes were put in place, in part, as a reaction to bank failures in the individual or neighboring Member States. Also, in 1986, the Commission of the European Economic Community (Commission) made a non-binding recommendation that all Member States introduce deposit-guar-

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* The author would like to thank Advocat General of the European Court of Justice, Walter Van Gervan for his suggestions and counseling on this paper. Sources and materials for this article are on file with the author.
2 See id. at Annex II for a list of related EC banking Directives and proposals.
3 See generally R. M. PECCHIOLI, PRUDENTIAL SUPERVISION IN BANKING (1987).
antee schemes in order to improve "the functioning of the Euro-

179 ee internal market." 4

Failure of credit institutions 5 in the EC, which occurred before deposit protection systems were put in place, were fully covered. Thus, the full faith and credit of individual countries has de facto guaranteed private credit institutions established in their territory. This practice prevented failed credit institutions from contaminating healthy credit institutions and limited adverse economic repercussions in their individual financial markets. 6 This practice is expensive for the national governments and their taxpayers, and now the responsibility for insuring credit institutions has shifted to the individual credit institutions and to depositors. Most depositors do not realize their position and they should be informed of it.

II. THE SECOND BANKING DIRECTIVE AND RELATED DIRECTIVES

The Second Banking Directive introduced the principles of a single banking license and home Member State control of bank supervision. 7 Credit institutions established in one Member State may open branches in any other Member State without further authorization. 8 A credit institution is supervised by the authorities

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5 Credit institution is defined as "an undertaking whose business is to receive deposits or other repayable funds from the public and to grant credits for its own account." First Council Directive 77/780 of 12 December 1977 on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Credit Institutions, art. 1, ¶ 1, 1977 O.J. (L 322) 30 [hereinafter First Banking Directive]. The Proposed Directive refers only to credit institutions and their branches. Id. art. 2.

6 For example, on October 3, 1989, Luxembourg introduced the Association pour la garantie des depots, Luxembourg "AGDL." Previous to this deposit protection scheme, Luxembourg had an unwritten agreement to fully guarantee banks. Also, in the United Kingdom, before the Statutory Deposit Protection Scheme came into effect on February 19, 1982, the Bank of England contained solvency and liquidity problems without any loss to depositors. In the early 1970s at the end of a property boom, the Bank of England initiated "Operation Lifeboat." The purpose of the operation was to restore liquidity to secondary banks. Over £1.2 billion was lent to 26 companies that did not have enough liquid assets to cope with withdrawals. In the early 1980s, Johnson Matthey Bankers Ltd. became insolvent. The Bank of England in consort with the major clearing banks, put together a rescue package to save that institution from bankruptcy. In all of the cases cited, none of the depositors with the troubled institutions lost any money.


8 Id. tit. V., art. 18.
and follows the laws of the Member State in which it is licensed and has its head office.9 The same Directive states, however, that supervision of the liquidity of the credit institutions’ branches shall be the responsibility of the host Member State.10 Yet, a credit institution shall be wound up according to the law of the home Member State.11 The Proposed Directive requires the home Member State to insure that credit institutions participate in the deposit protection scheme in force in their territory which “shall cover the depositors of branches set up by such institutions in other Member States.”12 Thus, the responsibilities for supervising, winding-up, and guaranteeing deposits are spread among the Member States, making it essential that communications between Member States remain open and that Member State banking regulations be similar.

Most of the deposit protection schemes available in the EC are similar in that they have limited guarantees.13 The limited guarantees make certain exclusions and offer a fairly low level of protection to depositors.14 The participating credit institutions that fund the deposit guarantee schemes argue that full guarantees would erode market discipline. The healthy credit institutions would be guaranteeing weak institutions which would be able to fund high risk investments with low cost funds.

Of course, limited guarantees also result in a lower level of con-

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9 “[H]ome Member State’ shall mean the Member State in which a credit institution has been authorized in accordance with Article 3 of Directive 77/780/EEC,” (i.e. the First Banking Directive). Second Banking Directive, supra note 7, tit. I, art. 1, ¶ 7. Title II of the First Banking Directive refers to “credit institutions having their head office in a Member State and their branches in other Member States.” First Banking Directive, supra note 5, tit. II. Article 3 of Title II lists requirements for establishing a credit institution. Id. tit. II, art. 3.

10 A “host Member State’ shall mean the Member State in which a credit institution has a branch or in which it provides services.” Second Banking Directive, supra note 7, tit. I, art. 1, ¶ 8. Additionally, “[h]ost Member States’ shall retain responsibility . . . for supervision of liquidity of branches of credit institutions pending further coordination.” Id. tit. IV, art. 14, ¶ 2.


12 Proposed Directive, supra note 1, art. 2, ¶ 1.

13 There are some exceptions. For example, certain deposits in Danish savings banks are fully guaranteed. See Lovtidende A., lov nr. 850 (16 Dec. 1987) § 3, ¶ 2 [hereinafter Danish Law on Deposit Guarantee Fund].

14 See Proposed Directive, supra note 1, at Annex III. Portugal and Greece do not have deposit protection schemes in place—thus these countries are not listed on the chart. See id.
tribution from individual institutions.\(^{15}\) Standing funds of individual protection schemes do not need to be highly capitalized. This is particularly true if there are either no failures of credit institutions or limited guarantees on failures.\(^{16}\)

Eroded market discipline and weak credit institutions do not result from full guarantees on deposits. If market discipline and weak credit institutions are a concern, better supervision and higher capital requirements are needed, not limited guarantees. Adequate supervision requires that appropriate regulations be followed and competent authorities be provided with confidential information which will allow them to monitor the financial institutions. The Commission is developing guidelines for regulations by submitting proposals and recommendations on supervision of credit institutions to the Council of the European Economic Community (Council).\(^{17}\) The Member States thus are aware of subjects before they become the topic of a Directive. As Member States implement Directives, appropriate regulations will be applied throughout the EC.

An issue arises as to whether improved supervision of credit institutions should be incorporated into the Proposed Directive. The Second Banking Directive and two related Council Directives\(^ {18}\) already set out fundamental capital-based supervisory standards. Annual on-site examinations and independent audit reports also would improve supervision and encourage market discipline.\(^ {19}\) There is no Community-wide supervision or deposit insurance in the way that

\(^{15}\) Some deposit protection schemes make this quite clear. For example, the United Kingdom Banking Act of 1979 states:

\[ \text{[i]f it appears to the Board that payments in any financial year . . . are likely to exhaust the Fund, . . . the Board may . . . levy special contributions from contribu-
\text{tory institutions. . . . No contributory institution shall be requested to pay a further}
\text{or special contribution if . . . the amount of that contribution, together with previous initial, further and special contributions made by the institution . . . amounts to more}
\text{than 0.3% of the institution's deposit base.} \]

Banking Act 1979, § 28(1),(3) (Eng.) \[hereinafter 1979 U.K. Banking Act\].

\(^{16}\) See Proposed Directive, \textit{supra} note 1, at Annex III for a list of how Member State deposit protection schemes are funded.

\(^{17}\) See, e.g., Commission Recommendation 87/62 of 22 December 1986 on Monitoring and Controlling Large Exposures of Credit Institutions, 1987 O.J. (L 33) 10 \[hereinafter Recommendation on Exposures\]. The Recommendation on Exposures proposes that credit institutions provide data to competent authorities concerning exposures at least once a year and “more frequent reporting in line with normal prudential requirements.” \textit{Id.}


\(^{19}\) See generally \textit{Modernising the Financial System—Recommendations for Safer, More Competitive Banks} \[hereinafter U.S. Treasury Rep.\].
there is federal supervision and protection of credit institutions in the United States.\textsuperscript{20} The Second Banking Directive even allows Member States individually to conclude cooperation agreements with third countries.\textsuperscript{21} One could argue that banking is an area which would be serviced better by an EC Treaty with third countries,\textsuperscript{22} rather than each Member State negotiating its own treaty.

In an effort to harmonize the deposit protection schemes in the EC, the Proposed Directive can be used as the lowest acceptable system.\textsuperscript{23} The ninth ‘whereas clause’ in the Proposed Directive states that “for economic reasons, it is undesirable to introduce throughout the Community a very high level of protection which is liable to encourage the reckless management of institutions. . . . Contributions to the funding of the scheme could become too burdensome for the member institutions.”\textsuperscript{24} The Member States are free to grant coverage above the EC minimum.\textsuperscript{25}


\textsuperscript{21} Second Banking Directive, \textit{supra} note 7, art. 6, ¶ 3.

\textsuperscript{22}The Treaty Establishing the European Economic Community (EEC Treaty) provides a legal basis for the EC to negotiate treaties with third countries. \textsc{Treaty Establishing the European Economic Community [EEC Treaty]} art. 113. Also, implied powers to negotiate treaties with third countries are found when the EC has issued Directives on the subject. \textsc{See Case 22/70, Commission v. Council, 1971 E.C.R. 265, ¶ 15, 17.} For example, the European Road Transport Agreement (ERTA) was an act \textit{suis generis} not falling into any EEC Treaty category. \textsc{See id.} The European Court of Justice (ECJ), in a case relating to ERTA, stated:

[t]o determine . . . the Community’s authority to enter into international agreements, regard must be had to the whole scheme of the Treaty no less than to its substantive provisions. . . . In particular, each time the Community, with a view to implementing a common policy envisaged by the Treaty, adopts provisions laying down common rules, whatever form these may take, the Member States no longer have right, acting individually or even collectively, to undertake obligations with third countries which affect those rules.

\textsc{Id.} The Community also may have implied powers to conclude international agreements. \textsc{See} Opinion 1/76, 1977 E.C.R. 741, ¶ 4. The Commission asked the ECJ whether an EC agreement with third countries establishing a European laying-up fund for inland waterway vessels was compatible with the EEC Treaty. \textsc{See id.} The ECJ stated:

[T]he power to bind the Community vis-à-vis third countries . . . flows by implication from the provisions of the Treaty creating the internal power and insofar as the participation of the Community in the international agreement is, as here, necessary for the attainment of one of the objectives of the Community.

\textsc{Id.}

\textsuperscript{23} “. . . it is indispensable to ensure a harmonized minimum level of deposit protection wherever in the Community deposits are located.” Proposed Directive, \textit{supra} note 1, art. 4, ¶ 1. The Proposed Directive recommends ECU 15,000 per depositor. \textsc{Id.; see also id. at Annex III.}

\textsuperscript{24} \textsc{Id.} art. 6, ¶ 13.

\textsuperscript{25} \textsc{Id.} art. 4, ¶ 3.
schemes, however, will not be eliminated. These arrangements, by their very nature, offer the least amount of protection to depositors.

By imposing minimum requirements on the Member States, the Proposed Directive follows the path of least resistance. Such a Directive can be adopted without much objection. This type of framework Directive is becoming more popular than regulatory Directives. A framework Directive relies upon spontaneous harmonization to transpose Community policy into national laws. They also allow the European Court of Justice (ECJ) more room to interpret EC law. 26

III. DEPOSIT PROTECTION SCHEMES

A. United States of America

The United States FDIC guarantees a general coverage of $100,000 for each deposit. Over the past ten years so many banks, such as thrift savings and loans, have gone bankrupt or are going bankrupt in the United States, that the Bank Insurance Fund has been depleted and needs to be recapitalized. In many cases, the United States Government covered the losses and compensated depositors. In December, 1991, Congress authorized the FDIC to draw on a $30 billion appropriation to the Treasury Department. Changes must be made in the deposit protection scheme, and the U.S. Treasury, House Banking Committee, and Senate Banking Committee all are offering proposals. The law on deposit protection has not changed yet. Certain suggestions have been proposed such as reducing the scope of deposit protection. Thus, for example, pass-through insur-

26 The ECJ has been widening the scope of the EEC Treaty through its interpretation of Directives and the Treaty itself. The landmark case beginning this trend is Van Gend en Loos v. Nederlandse. 1963 E.C.R. 1, 1 C.M.L.R. 105. In that case, which is also the cornerstone of supremacy of EC law, the ECJ found direct effect of EC Treaty law. See id. The Treaty article must be clear, precise, and unconditional in order to have direct effect. See id. An article which is directly effective needs no further implementing rules at the Member State level. Id. This decision was made in spite of the fact that half of the Member States in the Community objected to the decision. The objecting Member States were Germany, Belgium, and the Netherlands. The EC only had six Member States at that time. Article 189, paragraph 3 of the EEC Treaty states: "[a] directive shall be binding as to the result to be achieved, upon each Member State to which it is addressed, but shall leave to the national authorities the choice of form and methods." EEC TREATY art. 189, ¶ 3. Thus, Directives should be transposed into the written rules of national law, providing legal certainty, in order to be binding. The ECJ, however, determined that when a Member State has not introduced implementing regulations before the expiration of the time limit provided for in the Directive, individuals may enforce the Directive as against the Member State. Becker v. Finanzamt Munster-Innenstadt, 1982 E.C.R. 53, 1 C.M.L.R. 499; Case 152/84, Marshall v. Southampton & South West Hampshire Area Health Authority (Teaching), 1986 E.C.R. 723, 748.
ance for pension plan deposits may be eliminated in the future.\textsuperscript{27} Also, depositors, rather than deposits, will be insured. Other recommendations include increasing each bank's deposit insurance premium\textsuperscript{28} and improving capital supervision of credit institutions.\textsuperscript{29} Even with increased premiums and capital supervision, however, the Congressional Budget Office (CBO) estimates another 719 banks will fail by 1995 at a cost of $40 billion.\textsuperscript{30} Advertising the amount of coverage, $100,000 per depositor, will continue. None of the studies recommend reducing the $100,000 amount of deposit protection. The suggested changes to the U.S. deposit protection scheme summarized above indicate how a comprehensive protection scheme financed by taxpayers is being forced to change to one that requires better supervision and more contributions from banks,\textsuperscript{31} while offering less protection to depositors.

B. Denmark

The Danish Deposit Guarantee Fund\textsuperscript{32} (Danish Fund) is perhaps the most consumer-oriented of all schemes available in that it grants 100 percent coverage for special types of deposits.\textsuperscript{33} These are deposits which are put into certain categories of savings accounts. Savings

\textsuperscript{27} A pass-through account is a single deposit account in which a fiduciary such as an accountant, lawyer, or management group deposits funds on behalf of a large number of beneficiaries. Currently, the $100,000 deposit insurance passes through the fiduciary account to each of the beneficiaries.

\textsuperscript{28} See \textit{American Bank; Fanny for Some}, \textit{ECONOMIST}, Apr. 11, 1992, at 96. FDIC Chairman William Taylor announced on April 7, 1992 that an increase in premiums from 23 cents per $100 of insured deposits to 27–30 cents will be put off until 1993. \textit{Id.} Also, starting in 1993, premiums will be risk-weighted. \textit{Id.} Thus, well-capitalized banks could get a 10% discount on their premiums while weaker banks would be charged more. \textit{Id.}

\textsuperscript{29} See generally U.S. Treasury Rep., \textit{supra} note 19. There are also legislative proposals from the Senate and House of Representatives and there has not been a finalized version published yet. \textit{Id.} The only aspect of the current U.S. deposit which certainly will remain is the $100,000 coverage. \textit{Id.} This probably will change from $100,000 per deposit to $100,000 per depositor. \textit{Id.} This is untouched because of fear of public reaction if the amount were lowered. \textit{Id.} Eliminating the scope of protection is less evident to the public. \textit{Id.} at 16, Part II.

\textsuperscript{30} \textit{Id.}

\textsuperscript{31} United States banks function in the same way that EC credit institutions function.

\textsuperscript{32} Danish Law on Deposit Guarantee Fund, No. L42 (Dec. 10, 1987) [hereinafter Danish Fund]. When settling upon an appropriate deposit guarantee scheme, the Danish Banking Association and the Savings Bank Association were asked for suggestions. The Danish Minister of Industry, Mr. Nils Willhelms, wanted an unlimited guarantee on all deposits. Finally, a compromise was worked out so that certain accounts now are covered in full. These include: capital pension accounts, personal pensions annuity accounts, pension installment accounts, child savings accounts, housing savings contracts, education savings accounts, deposits in the clients' accounts of lawyers, deposits administered by approved trust departments under the
accounts where a fiduciary relationship exists between the credit institution and beneficiary, such as trusts administered by the credit institution, pension accounts, child savings accounts, and education accounts, are insured 100 percent. Ordinary depositors are covered for deposits up to DKR 250,000 (U.S. $40,320). The scope of deposit protection is reduced by not covering managers, directors, and shareholders owning 10 percent or more of the credit institution.

The Danish Financial Supervisory Authority (Finanstilsynet) requires that a total of DKR two to three million be kept in the Danish Fund. The Danish Fund also is backed partially by the State, and the fund may take out a loan guaranteed by the State if its resources have been depleted, and claims of depositors cannot be covered. The Danish law also requires foreign branches of deposit-taking institutions in their territory to participate in the Danish Fund. 34

C. United Kingdom

The United Kingdom Deposit Protection Scheme (U.K. Scheme) protects 75 percent of the first £20,000 (U.S. $36,000) deposit. 35 Foreign currency accounts are not included in the U.K. Scheme. A notice from H.M. Treasury Press Office states "protection has been limited to 75 percent in order that there should be incentive to prudence on the part of the depositor before deciding with which institution to place his funds." 36 Certain categories of deposits are not covered at all and are excluded from protection. These include, for example, secured deposits, deposits with a maturity of more than five years, certificates of deposit, and deposits from the director, controller, or manager of the institution or close relatives of such a person. 37 All recognized banks and licensed institutions taking Sterling deposits must contribute to the Deposit Protection Fund (stand-
ing fund). Thus, branches of credit institutions with home offices in other countries also will contribute to the U.K. Scheme regardless of whether they are covered by a similar scheme in their home country. The standing fund should remain at a level between £5–6 million (U.S. $9–10 million). If the standing fund is depleted and special contributions have been called already, the Bank of England as lender of last resort will lend money to the standing fund. Unused special contributions, however, will be returned pro rata to contributing institutions in the same financial year they are called. Contributions are tax deductible, but repayments to contributing institutions are taxable.

D. Belgium

The Belgian deposit guarantee scheme is a private agreement rather than a national law. It offers coverage of BF 500,000 (U.S. $14,700) for each deposit. The following is a description of the agreement.

An “Intervention Fund” has been formed with yearly contributions from participating banks. The contributions are based upon the Belgian franc deposits, fixed deposits, and bonds of each participant. There is no lender of last resort, insurer, or emergency contribution scheme provided if the Intervention Fund is depleted. Rather, the agreement specifically denies reimbursement under any circumstances once the assets of the Intervention Fund are drawn down. What is disturbing about this agreement in particular, is that

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38 This was a change made by the Amendment to the U.K. Banking Act in 1987. 1987 U.K. Banking Act, supra note 35.
39 Id. § 54, ¶ 1. Section 54 states that further contributions may be levied at the end of the Board’s financial year if the Fund’s resources have been reduced below Sterling three million, or, at any time, to give effect to an increase in the size of the Fund as a result of an order by the Treasury approved by both Houses of Parliament. Id.
40 Special contributions may be required of participants to the deposit protection scheme in the event that the Fund is expected to exhaust its reserves by the end of the year. There is, however, an overall limit of 0.3% of an institution’s deposit base which may be called. 1987 U.K. Banking Act, supra note 35, §§ 54–56.
41 Id. § 64. Section 64 allows the Board to enter into arrangements to borrow funds in order to carry out its obligations. Id.
42 Agreement Regarding the Bank Deposit Protection Scheme Between Institut de Reescompte et de Garantee and Association Belges des Banques (Jan. 1, 1985) [hereinafter Agreement Regarding Bank Deposit Protection].
43 Id.
44 Id.
the Intervention Fund is not highly capitalized.\textsuperscript{45} In fact, the agreement returns all contributions to participants after ten years.\textsuperscript{46} From this, one can conclude that private arrangements to provide deposit protection schemes need guiding principles that will encourage them to give adequate protection to depositors.

In part, because it is the capital of the EC, many non-EC credit institutions established their head offices in Brussels, rather than a financial center such as London. For example, there are now twenty-three Japanese banks with head offices in Brussels. Most of these banks have been set up in the past three years in anticipation of the single market and the easy access to other Member States.\textsuperscript{47} Thus, a large number of credit institutions have their home office in Belgium. The Belgian Intervention Fund should reflect this by requiring a higher minimum level of capitalization.

\section*{IV. \textbf{PROPOSED DIRECTIVE}}

\textbf{A. \textit{Home Country Versus Host Country Control}}

The systems of the Member States outlined above illustrate the great differences in the scope and amount of deposit protection available in the EC.\textsuperscript{48} The Proposed Directive specifically aims at unifying the banking deposit system within the EC. The sixth ‘whereas clause’ in the Proposed Directive uses the home country control provisions in the Second Banking Directive as a reason for changing deposit protection of branches to home country control. Article 2,  

\textsuperscript{45} \textit{Id.} art. 27. Article 27 states:

\begin{quote}
[t]he Institute shall allocate a total amount of 200 million (Belgian) francs ($6,000,000) to the intervention scheme. This amount shall be split between the banks' and the savings banks' funds proportionately to the volume of the Belgian franc deposits, fixed deposit receipts (bon de caisse), and bonds they hold on 30th September 1984.
\end{quote}

\textit{Id.} art. 27. This means that there would be $3,000,000 to draw from in case of failure of a credit institution. This is the lowest amount that shall be held in the Intervention Fund. Thus, reimbursements to participating banks cannot draw down the fund below this amount.

\textsuperscript{46} 1987 U.K. Banking Act, \textit{supra} note 35, art. 18. Article 18 states: “[c]ontributions that were not called by the Institute under Article 13, within 10 years period, are repaid to the (participating) bank.” \textit{Id.} art. 18.

\textsuperscript{47} It is unclear how many of these banks are credit institutions. Some of the Japanese banks have home offices in Brussels because the clients they serve are there. For example, Mitsubishi Bank (Europe) S.A., the fourth largest bank in Belgium, has a large client base in Brussels. The Nihonjinkaiasbl, Avenue Louis 279, Bte. 6, 1050 Brussels has a list of all Japanese banks and companies located in Belgium.

\textsuperscript{48} Portugal and Greece, which are the only two Member States without guarantee schemes, are not mentioned.
paragraph 1 makes home country deposit protection of branches compulsory.

Deposit protection is one area of banking which should be left under host country control. The main reason is that there is no centralized deposit protection system in the EC. In fact, the Maastricht Treaty specifically forbids the European Central Bank to act as lender of last resort or to participate in insurance schemes. Member State financial markets continue to be insulated and segregated from each other. National Central Banks only are interested in acting as lender of last resort when there is a possibility of a collapse of their own national financial market. Since the financial markets in the EC are segregated still, a central bank in the home country may decide that the collapse of one credit institution and its branches is inconsequential to its national interest. The host country, in contrast, may see complete disruption of its financial market because of the collapse in its territory of the branch.

In Belgium, a country with a low protection scheme and a very large number of credit institutions, the collapse of a credit institution with a branch in Denmark may be of little consequence to its own financial market. Since there are very few credit institutions in Denmark, however, the collapse of a major branch may have severe repercussions on its national financial market. Under host country deposit protection, the Danish financial market would feel less of a shock because the protection would be higher and a lender of last resort would be available.

A consumer protection argument offers further support for host country control of deposit protection. Under home country control, twelve different protection schemes possibly could be available in one Member State. This confuses depositors. Advertising deposit protection schemes may reduce the confusion of the consumer. Even an especially prudent depositor would find it difficult to digest and understand twelve different deposit schemes. Article 2, paragraph 2 does offer the possibility of coinsurance for deposits. It is not likely, however, that branches will join the host country protec-

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50 Proposed Directive, supra note 1, art. 2, ¶ 2.
tion scheme if they already are contributing to the home country protection scheme.

B. Non-EC Credit Institutions

Article 3 does not require branches of non-EC credit institutions to participate in deposit-guarantee schemes in the EC. This is potentially dangerous as many countries do not extend protection of domestic institutions abroad. If the final Directive does not make participation of these branches compulsory, there is a possibility that they will not be covered by any deposit protection scheme. It is unlikely that institutions voluntarily will pay more to join a scheme that reduces profits and makes them less competitive. Article 3, paragraphs 2 and 3, however, require non-EC branches to inform depositors whether or not deposits are protected by a guarantee scheme. This should encourage the branches to participate in a deposit guarantee scheme. All credit institutions in the EC are required to provide depositors with information concerning their deposit guarantee scheme under article 6 of the Proposed Directive. This important provision will benefit consumers.

C. Compensation

Article 4 outlines the amount of compensation that should be allowed to depositors rather than deposits. The deposits are aggregated and the total amount is protected up to ECU 15,000 per depositor (approximately U.S. $18,700). Article 4 sets a minimum amount of compensation, but also allows Member States to offer a higher amount of protection. Most credit institutions would like to

51 Id. art. 3.
52 See id. at Annex IV for a chart that lists OECD countries that do not extend protection to deposits at branches abroad of domestic institutions. The basic information was extracted from R. M. Pecchioni, supra note 3.
53 For example, the U.S. Treasury Report recommended that foreign deposits of U.S. credit institutions or banks neither be insured, nor subject to insurance premium assessments. See generally U.S. Treasury Rep., supra note 19.
54 Proposed Directive, supra note 1, art. 3, ¶ 2, 3.
55 Id. art. 6.
56 The provisions requiring information concerning the deposit protection schemes was added to the final draft of the Proposed Directive by the Commission’s Division of Consumer Policy Services. Id.
57 The deposit scheme in the United States is also changing from protection for each deposit to protection for each depositor.
58 Id. art. 4, § 1.
59 Id. art. 4, ¶ 3.
place a higher burden on depositors by requiring a mandatory ceiling on amounts Member States may protect.\textsuperscript{60} As a matter of public policy, the more consumer oriented Member States would not take this suggested change seriously.

Even minimum compensation amounts may not be realized, however, if the insurance fund is not capitalized adequately, extraordinary calls cannot be made on participating banks, and no lender of last resort is available. Such requirements would avoid the hazards of a system such as Belgium's, which does not pay any compensation to depositors once the Fund is drawn down completely. There are no requirements for such safeguards in the Proposed Directive.

Article 4 also allows a Member State to limit the amount of compensation to a percentage of deposits guaranteed.\textsuperscript{61} Although this is not a requirement, it accepts the U.K. model which limits compensation to a percentage in order to provide an incentive for "prudence on the part of the depositor."\textsuperscript{62} In fact, the U.K. came under heavy criticism for its use of percentages when BCCI failed in 1991. By the percentage method, small depositors carry the heaviest burden if a credit institution fails.

The scope of protection under the Proposed Directive does not include certain deposits which may be excluded and left unprotected completely.\textsuperscript{63} The individual Member States may determine which, if any, of the listed deposits will be excluded. The only controversial exclusion is deposits of pension or retirement funds. Since the Member States are not required to adopt the exclusions,

\textsuperscript{60}The EC Committee Financial Services Subcommittee of the American Chamber of Commerce in Belgium which is made up of European companies of American parentage, published a position paper on coordination of deposit guarantee schemes on April 16, 1992. On page two the paper states the following:

\textit{[t]}he EC Committee believes that a mandatory maximum should also be set both in order to prevent excessive distortion of competition and as a way to maintain market discipline. . . . The possibility to limit compensation to a certain percentage of the deposit guaranteed should be supported as it introduces an element of market discipline. In fact, a system of declining percentages could be used as an alternative to a mandatory maximum amount.

This report is on file with the author.

\textsuperscript{61}Proposed Directive, \textit{supra} note 1, art. 4, ¶ 4.

\textsuperscript{62}The Proposed Directive raises the amount of compensation for British depositors to 90\% of the total guaranteed deposits. \textit{See id.} The United Kingdom and Ireland are the only Member States that have a system which limits compensation to a percentage of guaranteed deposits. Ireland uses a convoluted formula which starts compensation of deposits at the rate of four-fifths of deposits up to 5,000 Irish Pounds and ends at one-half of deposits over 10,000 but less than 15,000 Irish Pounds. \textit{See The Banking Act of 1989, Ch. 5, § 55 (1989) (Ir.).}

\textsuperscript{63}\textit{See} Proposed Directive, \textit{supra} note 1, art. 4, ¶ 2.
it should be of little concern to a country such as Denmark which grants 100 percent protection for pension funds. Danish pension fund managers should be put on notice not to make deposits in branches which do not participate in the Danish Fund. Member States which have excluded deposits not listed in article 4 as excludable deposits, will need to amend their laws. For example, the United Kingdom excludes certificates of deposits and pass-through accounts. Since neither one of these categories of deposits is listed under excludable deposits, they should be protected.

D. Advertising

All previous drafts of the Proposed Directive included a no-advertising requirement. In its review of the draft proposal, the Commission Consumer Policy Services division objected to the no-advertising provision. Discussing an advertising provision is relevant since a no-advertising provision possibly may be reinstated before the Proposed Directive is enacted.

Any no-advertising requirement in the Proposed Directive would run counter to the principles of the EC. The principles of the EC are stated in the Treaty Establishing the European Economic Community (EEC Treaty). The EEC Treaty states in pertinent part, "[t]he Community shall have as its task, by establishing a Common Market and progressively approximating the economic policies of Member States . . . an accelerated raising of the standard of living and closer relations between the States belonging to it."64 Thus, by including the no-advertising provision in the Proposed Directive, the Commission is going against the very foundation of the EC.

Since each Member State deposit protection scheme must cover deposits placed in branches set up in other Member States,65 up to twelve credit institutions in one Member State may be participating in a different scheme. How can one expect prudence on the part of the depositor if the depositor does not know whether the credit institution insures accounts, and what percentage of deposits are protected in case of failure. If the informed public patronizes credit institutions which participate in a more favorable scheme, the public and domestic credit institutions themselves will exert pressure on the Member States to harmonize with or approximate the policies of neighboring Member States. This process is known as spontane-

64 EEC Treaty art. 2.
65 Proposed Directive, supra note 1, art. 2, ¶ 1.
ous harmonization. Spontaneous harmonization occurs when there is competition. Public knowledge is necessary for spontaneous harmonization to occur. Such public knowledge is attained through advertising.

If there is a prohibition on advertising, a Member State with a pro-consumer deposit protection scheme, such as Denmark, may object to the entry into their territory of branches of credit institutions from other Member States with lower protection. The Member State might even refuse entry of such branches in the interest of the "general good." The concept of the "general good" appears three times in the Second Banking Directive. A Member State may require a branch of a credit institution to comply with its laws, in the "interest of the general good." Again, once the branch begins to conduct business, the host Member State may prevent or punish it for acts contrary to rules adopted "in the interest of the general good."

The meaning of "in the interest of the general good" can be found in the case law of the ECJ. There are certain exceptions to the EEC Treaty policy of free movement of goods. These exceptions allow

66 See Second Banking Directive, supra note 7, art. 19, ¶ 4, art. 21, ¶ 5, 11. Article 21 states:

[n]othing [in] this Article shall prevent credit institutions with head offices in other Member States from advertising their services through all available means of communication in the host Member State, subject to any rules governing the form and the content of such advertising adopted in the interest of the general good.

Id. art. 21, § 11.

67 See id. art. 19, ¶ 4. Article 19 states:

[b]efore the branch of a credit institution commences its activities the competent authorities of the host Member State shall, within two months of receiving the information mentioned in paragraph 3, prepare for the supervision of the credit institution in accordance with Article 21 and if necessary indicate the conditions under which, in the interest of the general good, those activities must be carried on in the host Member State.

Id.

68 Id. art. 21, ¶ 5.

69 See W. Van Gerven, The Second Banking Directive and the Case-Law of the Court of Justice, 10 Y.B. EUR. L. 57, 63–70 (1991). Advocate General of the Court of Justice, W. Van Gerven stated: "how must the phrase 'in the interest of the general good' be understood? In my view there is no possible doubt: this expression refers to the conditions recognized by the Court of Justice as justifying national rules which constitute an obstacle to the free movement of goods or services." Id. at 65.

70 EEC Treaty art. 36. The four freedoms encompassed by the EEC Treaty are free movement of goods, persons, services, and capital. See generally EEC Treaty. Non-tariff barriers to trade relating to goods are not permitted. Article 30 states: "Quantitative restrictions on imports and all measures having equivalent effect shall, without prejudice to the following
a Member State to enforce a national law which may impede free movement. The key to the exception is in the second sentence of article 36 of the EEC Treaty, which provides that there may not be "arbitrary discrimination" or "disguised restrictions on trade."71 Under the discrimination analysis, the ECJ determines whether the national law in question is neutral as applied to domestic and foreign products.72

The case law relating to free movement of persons and services is not as developed as that of the law relating to the free movement of goods.73 There is, however, some parallelism between the two.74 By analogy, the competent authority of, for example, Denmark, may require branches of Member State credit institutions to advertise the extent of their deposit protection policy. The authority even may require that certain deposits be covered completely in the "interest of the general good."75 The Danes could argue that this is a con-

provisions, be prohibited between the Member States." EEC Treaty art. 30. Article 36 provides non-economic exceptions to article 30. Article 36 provides:

[the provisions of articles 30 to 34 shall not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of industrial and commercial property. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary discrimination or a disguised restriction on trade between Member States.

EEC Treaty art. 36; see also EEC Treaty art. 100(a). ¶ 4.

EEC Treaty art. 36.

72 See Case 158/86, Warner Brothers, Inc. v. Christiansen, 1988 O.J. (C 159) 4. This is a copyright case in which the ECJ agreed with a Danish law that stated that the right to rent out a video is not exhausted when a video is sold. See id. The Danish law states that there is a separate right of the proprietor to hire out a video. Since domestic and foreign videos are required to follow the Danish regulation, the Court did not find either disguised discrimination or a violation of article 30 of the EEC Treaty. Id.


74 See Case 262/81, Coditel SA v. Cine-Vog Films SA, 1982 E.C.R. 3381, 1 C.M.L.R. 49 (1983). In that case, the ECJ suggested that article 36 of the EEC Treaty also applies to restrictions on the freedom to provide services. See id. at 3390-97.

75 Second Banking Directive, supra note 7, art. 21, § 11. As the national measure may not be disproportionate to the result desired, advertising may be the most suitable way of protecting consumers.
sumer protection requirement. They could argue that the require-
ment does not discriminate arbitrarily against credit institutions
from other Member States, since domestic credit institutions also
must comply with it.\textsuperscript{76}

Consumer protection is an area which should be given priority in
the Directives themselves. The EEC Treaty provides “the Commis-
sion, in its proposals . . . concerning health, safety, environmental
protection and consumer protection, will take as a base a high level
of protection.”\textsuperscript{77} The question is whether deposit protection schemes
are meant to protect the depositor-consumer or to protect the credit
institutions.

E. National Implementing Laws

The penultimate article in the Proposed Directive requires Mem-
ber States to “bring into force laws, regulations and administrative
provisions necessary to comply with this Directive. . . .”\textsuperscript{78} This article
would be stronger if it stated that only government deposit protec-
tion schemes are acceptable under the Proposed Directive. In the
interest of consumer protection, it is logical that the competent
authorities of a Member State who are answerable to the people be
responsible for developing a suitable deposit protection scheme.

Professional organizations are not answerable to the people and
cannot have the public interest in mind when developing a deposit

\textsuperscript{76} Using the reasoning of the ECJ presented in the landmark case Casis de Dijon, the Danes
could argue for consumer protection on the same level as provided for in Denmark. See Case
120/78, Rewe-Zentral AG v. Bundesmonopolverwaltung fur Branntwein, 1979 E.C.R. 649
[hereinafter Casis de Dijon]. Casis de Dijon used the rule of reason which can be invoked in
cases such as consumer protection or environmental protection where the exceptions of
article 36 of the EEC Treaty do not strictly apply. See id. The rule of reason argues that when
there are disparities or there is an absence of common rules and the rule in question does
not discriminate against other Member States and are thus applied without distinction, then
the rule is allowed. See id. The rule in question should result from mandatory requirements
of general interest and the restriction should be necessary and not disproportionate with its
objective. See id.

\textsuperscript{77} EEC Treaty art. 100(a), ¶ 3.

\textsuperscript{78} Proposed Directive, \textit{supra} note 1, art. 8. This is a change from Recommendation for
Deposit-Guarantee Schemes. The fourth ‘whereas clause’ in that document states:

Whereas a number of Member States have deposit-protection schemes which were
set up on a voluntary basis under the responsibility of professional organizations,
and which have proved just as suitable and effective as compulsory schemes set up
and administered on a statutory basis; whereas it is therefore necessary to safeguard,
in those Member States which do not yet have guarantee schemes, both private and
governmental initiatives.

On file with the author.
protection scheme. Their main interest must follow that of their members. In the case of credit institutions, the main interest should be profits. The fourteenth ‘whereas clause’ in the Proposed Directive addresses the issue of professional organization deposit protection schemes. The only problems the Proposed Directive finds with professional organizations relate to compulsory membership and exclusion from a deposit protection scheme. Exclusions from a protection scheme are possible only after certain steps are taken and the depositors are given a one-year notice.

Another problem with professional organizations which is not addressed by the Proposed Directive is the lack of safeguards needed to insure that there will be a means of providing the compensation of ECU 15,000 per depositor. These safeguards are adequate capitalization of the fund, ability to make extraordinary calls on participating banks, and a lender of last resort.

V. CONCLUSION

In conclusion, the Council drafted the Proposed Directive as part of a series of measures aimed at unifying banking aspects of the internal market. Its stated goal is to increase the stability of the banking system and to protect depositors. This will be accomplished by providing a minimum level of protection, depositor information, and home country control.

Advertising and information about the available deposit protection schemes are essential since depositors must share the financial burden of a failed credit institution. Depositors do not have the means of assessing or controlling the financial policies of credit institutions. They are expected to be prudent, however, when choosing a credit institution.

Home country control of deposit protection could be devastating for small financial markets accustomed to high levels of protection for depositors. The result is devastating because the financial mar-

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79 See Proposed Directive, supra note 1, art. 2, ¶ 1–2.
80 These are also important and realistic issues. The issues address a problem which occurred in Belgium. The professional organization in Belgium which administers the deposit protection scheme decided arbitrarily to exclude all deposits in a participating credit institution after the credit institution failed. The organization decided after the fact that no depositor should be reimbursed because there was a possibility that the credit institution was being used to funnel black money to Switzerland. Black money earned and not reported to the national tax authorities. Such a decision would not be allowed under the Proposed Directive.
81 Proposed Directive, supra note 1, art. 2, ¶ 3.
kets in the EC continue to be segregated. Furthermore, there is no community-wide deposit insurance. The Maastricht Treaty specifically rejects a proposal that the European Central Bank insure deposits or depositors in any way.

If private deposit protection schemes are allowed, the final Directive should include some basic requirements to act as safeguards. These safeguards should include the following: a minimum amount available in a standing fund based upon the number of participating credit institutions; ability to make extraordinary calls on participating credit institutions in case of emergency; and availability of a lender of last resort.

Some particularly vulnerable Member States may use the concept of the “general good” to force branches from other Member States to comply with stricter banking standards. When this occurs, those states most likely will seek an interpretation from the ECJ. The final Directive on deposit protection certainly will begin the process of harmonizing deposit protection standards. With competition, the standards should not become minimal.