

Anna Jurkowska-Zeidler

University of Gdańsk, Poland

e-mail: anna.jurkowskazeidler@prawo.ug.edu.pl

ORCID: 0000-0002-4316-6073

PUBLIC INTEREST IN THE BANKING SYSTEM REGULATION

Abstract

This paper deals with issues related to public interest and Polish banking system regulation. It brings several general arguments regarding the actual legal regulation of the banking system, raises questions about the reasons for such detailed regulation, and discovers the public interest in the banking system law. In addition, the author explains what has changed in the architecture of the entire financial market after the global financial crisis of 2008. In the middle part of the paper, several important facts about the functioning of the banking safety net can be found. To be more precise, the activity of the central bank, financial supervision, bank deposit guarantee system, as well as protection of consumers are mentioned and analyzed.

KEYWORDS

financial stability, banking law, banking system, financial safety net, central bank, financial supervision, bank deposit protection

SŁOWA KLUCZOWE

stabilność finansowa, prawo bankowe, system bankowy, sieć bezpieczeństwa finansowego, bank centralny, nadzór finansowy, ochrona depozytów bankowych

I. INTRODUCTION

The changes in financial market regulation and supervision that took place more than a decade after the global financial crisis of 2008 led to a paradigm change in the functioning of the banking system and the entire financial system, at an international, European, and national level.¹ In view of the ongoing process of the cross-border integration of international financial markets and the creation of a single European financial market, systemic risk has become a threat on a previously unknown scale. One of the crucial goals of the state's activity in the field of banking operations is to ensure the safety of funds derived from the public that have been accumulated in the banking system. Systemic risk has taken on a cross-border dimension and has given rise to concern that the uncontrolled failure of institutions that are too big to fail will put financial systems and the entire global economy at risk. The bankruptcy of one financial institution can produce a kind of 'domino effect'; moreover, the failure of the financial system has serious external effects that 'spill over' (a contagion effect) far beyond the entities directly involved in it. For this reason, strict regulation of the financial market is necessary.

Currently, banking law is a very dynamically developing field of law and, at the same time, an important component of the financial market law.² Financial crises, in particular, but also irregularities in the financial market have greatly influenced the increasing legal interference of states in the market mechanism. The amount of funds entrusted by depositors and investors to institutions operating on the financial market, in combination with various types of risk (the risk of loss of entrusted funds, asymmetry of information, the risk of poor management of entrusted funds, and the risk of imposing unfair contract terms on clients that violate those clients' interests), risks connected with financing services by way of those funds, the complexity of those institutions, as well as the complex structure

¹ A. Jurkowska-Zeidler, *The architecture of the European financial market: legal foundations*, Gdańsk-Warszawa 2016, pp. 53-70.

² The need to subject the financial market to a separate and specific legal regime is particularly recognized in the context of the functioning of the European Union financial market. See more C. Kosikowski, *Financial Law of the European Union*, Białystok 2008, pp. 193-227.

of banks themselves and of the relationships emerging on the financial market, make it in the public interest to ensure the safety and stability of that market.³

Financial market safety is a crucial element of financial stability (the stability of the financial system). The legal protection of the financial market safety is ensured by the financial safety net, which at an institutional level is traditionally provided by the existence of a central bank (as the lender of last resort), financial market supervision institutions, and a deposit guarantee system.⁴

II. FINANCIAL SAFETY AND STABILITY AS A PUBLIC INTEREST

The overall goal of the public interest in the financial system is the stability of the system itself, i.e., financial stability. The term ‘financial stability’ is not legally defined, but it is broadly used in the legislation of the European Union and the policy of the European Central Bank as well. Financial stability can be found as a condition in which the financial system – which comprises financial intermediaries, markets, and market infrastructures – is capable of withstanding shocks and disruptions in financial balance.

Financial stability as a public interest is understood more broadly as fiscal, monetary, and financial market stability. From this perspective, it has now become the most important goal of financial architecture, the aim of which is the prevention of financial crises (crisis prevention) and crisis management if such crises occur. Central banks have long played a key role in responding to financial panics. As the lender of last resort, they are able to provide an unlimited amount of liquidity support to banks. But for the central bank, the money issue is only the starting point. The central bank determines money issuance by increasing or decreasing the supply of money in circulation in order to influence the level of inflation – that is, any change in the value of money, expressed in terms of goods and services – and the exchange rate. The money supply is increased and decreased via the banking sector, which operates under conditions determined by the central bank. Therefore, with the use of such channels and instruments of influence, monetary policy is of fundamental importance for the scale of lending, economic growth, and the stability of that growth. Failure of monetary policy to adapt to the conditions of a given economy may either lead to its ‘overheating’ and a financial crisis or it may cause an economic slowdown. An innovative phe-

³ T. Nieborak, *Creation and enforcement of financial market law in the light of the economisation of law*, Poznań 2016, p. 100.

⁴ A. Jurkowska-Zeidler, *Bezpieczeństwo rynku finansowego w świetle prawa Unii Europejskiej*, Warszawa 2009, p. 166.

nomenon since the global financial crisis of 2008 has been a greater reliance on macro-prudential supervision to prevent systemic risks in advance. It should be remembered that when the financial crisis entered its subsequent phase, the situation of many countries, especially in the eurozone, deteriorated significantly and there was the so-called ‘feedback loop’ between the public finance crisis and the banking crisis.

The aim of the banking and financial law is to protect individuals (depositors, investors, and policyholders) to ensure the smooth operation of the business (fair, efficient, and transparent markets) and to safeguard the payment system and the stability of the financial system at large, thus preventing and containing systemic risk and systemic crises. Historical experience suggests that governmental banking regulation was not a ‘natural’ product but a reaction to crises and conflicts. Though the specific aims of banking law are the safety and soundness of the financial system, their ultimate goal is to safeguard confidence and trust.⁵ Knowledge of the legal mechanisms of banks’ operations and their institutional environment has become more and more necessary in order to understand the complexity of the phenomena and events that make up banking activity. In a market economy, banking law plays an important role. It regulates the functioning of a key fragment of the financial market, relating to the creation, organization, and operation of banks as well as state supervision over their activities, and to the regulation of legal relations between banks and their clients.

III. POLISH BANKING SYSTEM: SAFETY NET

The national financial safety network in the Polish banking system consists of: the central bank – Narodowy Bank Polski (NBP); the integrated financial supervision authority – the Polish Financial Supervision Authority (KNF); the financial market regulator – the Ministry of Finance; the resolution authority and the deposit guarantee system – the Bank Guarantee Fund (BFG); banking services; customer protection institutions – the Office of Competition and Consumer Protection (UOKiK); the Polish Financial Supervision Authority; and the Financial Ombudsman.⁶ A characteristic feature of the Polish banking system is its dispersion in many legal acts from various periods. The legal basis for the functioning of Polish banking system includes an extensive and very complex set

⁵ R. M. Lastra, *International Financial and Monetary Law*, second edition, Oxford 2015, p. 114.

⁶ A. Jurkowska-Zeidler, *Financial market law*, (in:) A. Dobaczewska, A. Drwiłło (eds.), *Polish financial law*, Warszawa – Gdańsk 2019, pp. 53-73.

of legal acts of various levels of importance.⁷ Banking law has not been codified. The dispersion of various regulations also intensifies the parallel application of the standards of European banking law.⁸ In the field of regulation of the European financial market, the integration of law is increasingly based on unification through maximum harmonization of directives and regulations.⁹ A special role in the regulation of the banking market is played by acts of ‘soft law’, which supplement the norms of generally applicable law and fill in those areas that have not been regulated in detail by the legislator.¹⁰

The National Bank of Poland¹¹ is responsible for ensuring monetary stability; it acts as the lender of last resort, the activities of which also include measures promoting financial stability; and it is closely involved in macro-prudential supervision.¹² In order to understand the current functions and aims of the NBP, it is essential to understand the evolving nature of the worldwide central banking. In the traditional role of the lender of last resort, a central bank, by providing financial support to banks, ensures that a crisis of liquidity does not become a solvency crisis. The evolution of the role of central banks after the financial crisis, above all, has consisted in the closer integration of the functions of ensuring monetary stability and financial stability, in a deeper awareness of the global dimension of the tasks of central banks and in introducing stronger safeguards for the increasingly fragile independence of a central bank.¹³ In the process of

⁷ The legal framework of the Polish banking system is contained in the Act of 29 August 1997, the Banking Law. The Act lays down the rules for conducting banking activities, establishing and organizing banks, branches and representative offices of foreign banks, as well as branches of credit institutions, and the rules relating to banking supervision, reorganization, liquidation, and bankruptcy. Z. Ofiarski, *Prawo bankowe*, Warszawa 2017, p. 39.

⁸ C. Kosikowski, *Publiczne Prawo Bankowe*, Warszawa 1999, pp. 52-55.

⁹ A. Jurkowska-Zeidler, *EU financial market law: from minimal harmonization to federalization*, (in:) M. Radvan and others (eds.), *The financial law towards challenges of the XXI century: (conference proceedings)*, Brno 2017, pp. 379-393.

¹⁰ In this sense, they are essential for the proper functioning of financial market entities. In a formal sense, soft law is not binding, but it often significantly influences the evolution of generally applicable legal regulations, as well as the behavior of financial market participants. M. Fedorowicz, *Nadzór nad rynkiem finansowym Unii Europejskiej*, Warszawa, p. 150.

¹¹ In the Constitution of the Republic of Poland of 2 April 1997, basic principles are regulated that shape the status of the National Bank of Poland (NBP) as the central bank of the state and the legal position of the two of its three bodies – the President of the NBP and the Monetary Policy Council. The third body of the central bank – the NBP Management Board – is only mentioned. The NBP performs the tasks specified in the Constitution of the Republic of Poland, the Act on the National Bank of Poland, and the Banking Law. These legislative acts guarantee the independence of the NBP from other state authorities.

¹² The NBP performs three basic functions: that of a bank of issue, of the bank of banks, and of the central state bank. E. Fojcik-Mastalska, *Bank centralny*, (in:) E. Fojcik-Mastalska, R. Mastalski (eds.), *Prawo finansowe*, Warszawa 2013, p. 513.

¹³ R.M. Lastra, *The Evolution of the European Central Bank*, *Fordham International Law Journal*, Spring 2012, pp. 4–10. At the same time, the aim of ensuring financial stability, especially

constructing a new, post-crisis architecture of regulation and supervision of the financial market (at an international, European, and national level), the mandate of central banks has been strengthened and supplemented by adding a duty to act in support of the stability of the financial system.¹⁴

The model of Polish macro-prudential supervision is based on the dual structure of the new Committee for Financial Stability (Komitet Stabilności Finansowej), which is the entity responsible for macro-prudential supervision and crisis management in the national financial system.¹⁵ It is interesting to note that the four institutions involved in the financial safety net – the President of the NBP, the Chair of the Commission for Financial Supervision, the President of the Board of the Bank Guarantee Fund, and the Minister of Finance – belong to the Committee for Financial Stability. Work of the Committee in the area of macro-prudential supervision is overseen by the President of the NBP (and the NBP ensures the servicing of the Committee); in the field of crisis management, it is overseen by the Minister of Finance (and the Ministry of Finance ensures the servicing of the Committee).

In the field of micro-prudential supervision, an integrated model has been used in Poland since 2006.¹⁶ Banking supervision was originally located within the central bank. This model functioned in Poland until 2008. Currently, the Polish Financial Supervision Authority exercises supervision over the banking sector, the capital market, insurance and pension markets, payment institutions and payment service offices, electronic money institutions, as well as the cooperative credit union sector.¹⁷ Supervision over the KNF is exercised by the Prime Minis-

neglected during the construction of the European Central Bank has taken on a much greater role. T. Knepek, *Rola Europejskiego Banku Centralnego w zapewnieniu stabilności rynku finansowego Unii Europejskiej*, Warszawa 2017, p. 99.

¹⁴ That is why for more than a decade we have observed the process of giving central banks new functions in the area of supervision of the financial market and of adding that supervision to structures of macro-prudential supervision and resolution procedure. See more D. Calvo *et al.*, *Financial supervisory architecture: what has changed after the crisis?*, *FSI Insights on policy implementation*, 2018, No. 8, p. 2.

¹⁵ See more M. Fedorowicz, *Nadzór makroostrożnościowy w Polsce*, Poznań 2019, pp. 1-328.

¹⁶ It should be remembered that in the European Union, financial supervision is characterized by the features of ‘complementarity’ and ‘multiple levels’ – since 2011, micro-prudential supervision has also existed at the EU level with the European Supervisory Authorities (the EBA: the European Banking Authority; the ESMA: the European Securities Market Authority, and the EIO-PA: the European Insurance and Occupational Pension Funds Authority), and macro-prudential supervision with the European Systemic Risk Board.

¹⁷ The scope and principles of this supervision are specified in the Act on Financial Market Supervision of 21 July 2006, and the Banking Law of 29 August 1997. The purpose of supervision over the financial market is to ensure the proper functioning of this market, its stability, security, and transparency, to ensure confidence in the financial market, and to ensure the protection of the interests of market participants both through providing reliable information on the functioning of the market and by achieving the objectives set out in sectoral acts regulating supervision that is subject to organizational integration as part of financial supervision. Nadolska A., *Komisja Nad-*

ter. The body that manages the early anti-crisis mechanism, both from the point of view of protecting financial institutions threatened with insolvency and also guaranteeing payments to depositors, is the Bank Guarantee Fund.

Within the Polish legal system, the tasks of guaranteeing the deposits held in banks and cooperative credit unions, as well as of carrying out the resolution of financial institutions threatened with bankruptcy have been entrusted to a separate institution – the Bank Guarantee Fund. The rules, instruments, and procedures for the resolution of banks are also set out in the Act of 10 June 2016, on the Bank Guarantee Fund, the deposit guarantee system, and the resolution. Currently, deposit guarantee and resolution systems are indispensable elements of the safety net in a developed financial system.¹⁸

The crisis of confidence in financial markets and the need to rebuild it have resulted in many legislative actions in the last decade, both at the national and the European level. They are aimed at strengthening the protection of the consumer (customer) of financial services.¹⁹ In Poland, the protection of consumer rights is secured by a provision of the Constitution. Article 76 of the Constitution imposes on public authorities the obligation to protect consumers, *inter alia*, against actions threatening their safety and against unfair market practices. The most important institutions of the financial safety net and the protection of banking market customers are the Office of Competition and Consumer Protection (UOKiK), the Polish Financial Supervision Authority, and the Financial Ombudsman (Rzecznik Finansowy). The Office of Competition and Consumer Protection and the Polish Financial Supervision Authority (KNF) take actions in the interest of all consumers, and the Financial Ombudsman represents the interests of individual clients in respect of financial market entities. It should be emphasized that in the European Union, the legal protection of consumers of financial services has been given a strategic character, one that conditions the development of the cross-border provision of financial services and is crucial for economic security.²⁰

zoru Finansowego w nowej instytucjonalnej architekturze europejskiego nadzoru finansowego, Warszawa 2014, p. 190.

¹⁸ M. Janovec, A. Jurkowska-Zeidler, *The EU bank resolution framework: institutional changes of the financial safety net in Poland and the Czech Republic*, (in:) G. Hulkó, R. Vybíral (eds.), *European financial law in times of crisis of the European Union*, Dialóg Campus, 2019, pp. 201–214.

¹⁹ J. Monkiewicz, E. Rutkowska (eds.), *Ochrona konsumenta na polskim i międzynarodowym rynku finansowym*, Warszawa 2019, pp. 1–416.

²⁰ D. Cyman, *Nowy model ochrony konsumenta*, (in:) A. Drwiłło, A. Jurkowska-Zeidler (eds.), *System prawnofinansowy Unii Europejskiej*, Warszawa 2017, p. 366.

IV. CONCLUSIONS

Practical experiences (systemic risk, financial crises, consumer protection) require detailed legal regulation of the financial system for many reasons and the public interest is one of the most important ones. In the case of the banking systems analyzed in this paper, banks are still a key element of those financial systems. All banks are subject to special regulations and to the supervision of public authorities. Their activities are strictly regulated by the state, which is reflected in the administrative procedure of licensing and supervising banking activities.

Respecting the complexity of legal relationships in the financial system and the general inequity of a subject entering legal relationships in knowledge and possession of information, it is necessary to put public law requirements onto the primarily private law relationships to ensure fairness in the relationship between the financial institution and its possible client.

The general public interest in the financial system regulation and at the same time the most essential goal of this regulation is to ensure financial stability. Therefore, the most important reason for the regulating banks and the financial system as a whole is the state's interest in a well-functioning, secure, and stable financial system, in which there are no systemic risks caused, for example, by the failure of major financial institutions or the disruption of the financial services infrastructure. The legal guarantees of public trust towards banks include the legal framework for the activities and organization of banks and the banking system, as well as the institutional system of the financial safety net comprising the central bank, banking supervision, and a deposit guarantee system. The financial safety net plays a very important role in the stability of the banking system. The financial system requires a functional and systemic approach, and, above all, a guarantee of the effectiveness of the financial safety net.

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