

LEGAL REGULATION OF BANKS IS A PART OF FINANCIAL MARKET LAW

PART 2

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Scientists in the field of financial law, in the framework of their scientific-teaching and publishing activity, constantly examine the subject of financial law - an important and in recent times one of the most dynamically developing branches of Slovakia's legal system. In this branch we find also legal regulation of the financial market, the largest component of which is the two-stage banking system.

The financial market

The essence of the institute of the financial market, its foundation, development and active use confirm the high increase in the intensification of the utilisation of monetary resources. Therefore it is only obvious that market economies must, along with the market in goods, services and labour, use also the financial market.

The real market in goods and services, consumer goods and means of production presumes also the redistribution of available financial resources, where, likewise as in the case of the market in goods and services, also the financial market focuses on the demand and supply of money and capital, creating the price for them, at which participants in the financial market are willing to perform the financial operations.

Economic entities experiencing a shortage of financial resources come to the financial market with the aim of acquiring funds. They will obtain them either in the form of loans from various entities of the financial market, or they can issue securities and through their sale obtain the necessary funds. On the other hand, economic entities holding a temporary surplus of financial resources, i.e. savings, come to the financial market with the aim of investing them. In this sense, investing means the purchase of assets that will appreciate in the future, bringing new money.

Based on these economic ideas it may be said that the financial market is a place where financial brokers ensure, by means of financial instruments, the movement of short-, medium- and long-term capital between individual economic entities. Naturally, this cannot stand for any statutory definition of financial markets.

There will be no harm in taking a short detour at this point to the field of terminological definitions of financial markets. T. S. Maness describes the financial market as "a mechanism by means of which the savings of one sector of the economy flow into another sector of the econo-

my".⁹ V. Beneš and P. Musílek reckon that "on the financial market the supply and demand of money and capital come together, creating the price at which financial market participants are willing to perform financial operations and transactions. The financial market expresses more specifically the unity of short-term and long-term transactions in the reproduction process of the modern economy."¹⁰

With regard to examining financial market law, the most accurate terminological definition of financial markets can be said to be the idea of F. Mishkin that "the financial market is a system of economic instruments, institutions and relations that concentrates, allocates and redistributes financial resources between economic subjects on a supply and demand basis."¹¹

Financial markets functions refer to the functioning of the financial market as a whole. As mentioned above, the basic function of the financial markets is to transfer financial resources. Naturally, this is only a most global view of the function of the financial market. With regard to the fact that financial markets form a part of the financial system, it is necessary to expand the functions by those which also comprehensively depict the functioning of the financial system as a whole. For the purpose of this article we can go along the functions given in the extensive book "Finančný trh" [The Financial Market].¹²

• **Deposit function** – the financial market, by means of institutions, creates room for people's savings and their depositing in relatively low-risk opportunities. The financial market here mobilises all savings in order that they may be used for various purposes.

⁹ Maness, T. S.: Introduction to Corporate Finance. Washington : University of Washington, 1980, pg. 17.

¹⁰ See Beneš, V., Musílek, P.: Burzy a burzovní obchody. Praha: Informatotium, 1991, pg. 12.

¹¹ See Mishkin, F.: the cited work..

¹² Chovancová, B., Jankovská, A., Hájniková, J., Majcher, M., Šturc, B.: Finančný trh. Bratislava : Eurounion, 1999, pg. 20.



• **Function of ensuring wealth** – finančný trh ponúka možnosť, ako uchovať bohatstvo. Kým pri investovaní do vecí – nábytok, automobily, strojné zariadenia, hodnota klesá, v prípade cenných papierov sa hodnota zvyšuje.

• **Liquidity function** – wealth in the form of various financial instruments can be quickly exchanged for cash with very low risk of loss.

• **Credit function** – the financial market is manifested in the form of providing credit for financing consumption and investment expenditure. The financial market thus allocates credit resources where they are needed most.

• **Payment function** – in the financial market a mechanism is established for realising payments for goods and services.

• **Function of protection against risk** – the financial market offers firms, consumers and governments protection against risk (life, supplementary pension, property insurance, etc.). Besides insurance policies it enables the creation of a diversified portfolio of assets as a security measure against potential future losses.

• **Selective function** – the financial market functions in order to bring into balance savings and real investments, where concurrently it supports the development of prospective and viable businesses and accelerates the expiry of non-prospering ones.

• **Political function** – the financial markets have become the main channel for effecting government policy.

The financial market should not be seen as some monolith of money. It can be divided according to various aspects. In both theory and practice the most frequently used is that according to the first criterion. This concerns the division as regards special financial products traded in the financial market, where we distinguish:

(a) the market for short-term financial assets – the money market,

(b) the market of long-term financial assets – the capital market.

The economic literature in the case of this division also speaks of the time aspect and division in terms of the funds' purpose.¹³

The financial market is entered also by those who are experiencing a transitional shortage of financial resources and need to borrow. Capital markets are intended for financing long-term investments according to the needs of entrepreneurs, governments and households.

Both the main sections of the financial market can be further divided according to the specific financial instrument traded, that is from its material aspect, i.e. into the market for credit, securities, foreign exchange, precious metals, where within this division there can be further division into the market for short-term credit, long-term credit,

the insurance market, market in treasury bills, debentures, mortgage loans, shares, bonds, mutual fund certificates, etc.

It is natural that no clear dividing line can be placed between the individual parts of the financial market. Often it all concerns a mutual interlacing of instruments, subjects, operations, ownership, etc.

Another criterion for the division of the financial market is that according to the method of participants' entry to the financial market. Financial markets in this case are divided into the primary and secondary market. The primary one is intended for trading new issues of securities, i.e. securities that are on the market for the first time. The secondary market deals in securities already issued. Its main task is to ensure liquidity for securities investors, thus increasing the attractiveness of secondary markets, and since they also set the price, they accelerate trading also in the primary market. Secondary markets may be organised primarily as stock exchanges.

Still more financial market classifications may be found in professional literature, for example physical markets and OTC markets, markets with continual trading and markets with auction trading, markets in supplies and flows, etc.

As is clear, there are various criteria for dividing the financial market. Mostly they are subject to the purpose of examining a certain section of the financial market, and therefore cannot be uniform.

The financial market system, as one of the important elements of the economy of any state nowadays, confirms the considerable impact on the viability of the society. Not only does it ensure the accumulation of spare resources and their introduction into circulation, but also represents a distribution mechanism of financial capital. It is also a key element of the budgetary and payment mechanism of the economy of a country.

The existence of the created system of a new financial market and its law, governing the activity of the market is an essential pre-condition for the success of economic reforms in Slovakia currently under way and to continue for a long time yet.

These standards have brought to the forefront the urgency of the issue to separate financial market law into an integrated sub-branch and, on the other hand, not to restrict it only to the legal regulation of banking as some sort of banking law.

Financial market law as a sub-branch may be shaped on the basis of the following facts:

1. Societal need and state interest in creating legal regulation of financial market, given by the importance of the financial market for making economic reforms.

The specific importance of financial market subjects, the existence of societal need and state interest in crea-

¹³ See the cited works in footnote 8, pg. 25, and footnote 9, pg. 21.



ting separate legal regulation of financial market activity, are given also by the fact that the activities of the financial market subjects – commercial banks, insurance companies, asset management companies and other financial market subjects – has a direct influence on the performance of state economic policy. In Slovakia this thesis has received also a normative form in individual laws on banks, on the insurance industry, and on collective investment.

2. The existence of the subject of legal regulation itself, given by the particularities of the given area of societal relations.

We can speak of the financial market law as a sub-branch in connection with the fact that, similarly as in other examples of human activity, the legislator here, too, has specifically regulated the separate type of activity, in this case financial market activity. The subject of financial market law though does not end with relations arising in the course of the activity of financial market subjects. This subject also comprises relations arising in the process of regulating the financial market from the side of the National Bank of Slovakia, the Financial Market Authority and other bodies of general government with the view of ensuring the interest of all natural and juristic persons.

In the final result the conclusion may be reached that the subject of financial market law is formed by those socio-economic relations which arise in the process of the functioning of the whole financial market system in Slovakia.

Description of financial market law

At the root of a description of financial market law it is necessary to work from several assumptions. These concern in particular the following:

1. The need for specific methods of legal regulation

The particular nature of financial market law is given by the specific features of social relations, which form the subject of this law, namely those financial, commercial, civil and administrative. In this case importance lies in the question of the systematic classification of standards governing the financial market. If we want to speak of the system of a certain phenomenon, and the system of legal standards is undoubtedly such a phenomenon, we must bear in mind on the one hand a certain unity, and a certain differentiation on the other. The system of law is then the result of a systematisation, based on processing the substance of sources law by legal science as regards certain aspects.¹⁴ Financial market law uses simple methods of legal regulation, but also complex methods which sometimes represent a set of simple methods.

¹⁴ See Veverka, V., Boguszak, J., Čapek, J.: *Základy teorie práva a právní filozofie*. Praha : CODEX, 1996, pg. 79 et seq.

A complex method of the financial market law regulates mixed legal relations, arising in the functioning of the financial market system, and can be characterised as a set of imperative and non-mandatory procedures of legal activity, which appear in concentration in the legal status of financial market subjects. Financial market law also contains primary methods – where these depend on the nature of the relation which they regulate. They may be found in various variants. They are affected by specific forms, in particular those of legal standards – authorisation, prohibition, obligation.

2. Existence or need for specific sources of law.

This is provided in the form of the “legislation” of financial market law, which thus becomes its source. More specifically it concerns laws regulating financial market instruments, i.e. bonds, bills of exchange, cheques, credit, shares, mutual fund certificates, etc., law regulating financial market subjects, i.e. banks, insurance companies, pension funds, asset management companies, and, lastly, laws concerning regulation of the financial market, i.e. banking supervision, or other authorities of the financial market regulation such as the Financial Market Authority in Slovakia. Financial market legislation, and thus also its sources, must cover such law as the law on securities, on bills of exchange and cheques, commercial and civil codes regulating individual institutes of obligation such as deposit, credit, etc., laws on banks, on the insurance industry, on collective investment, on stock exchanges, on building society savings, on saving and credit cooperatives, on pension funds, on the central bank and on other institutions regulating the financial market (e.g. the Financial Market Authority in Slovakia), etc. This specific legislation governing the sphere of societal relations understood by us is manifested by the efficiency of the legal norm as a relation between the results of its operation actually achieved and the social objectives for the achievement of which the legal standard was adopted.¹⁵ The social objective in this case is the legal regulation of relations originating in the framework of the financial market's functioning.

3. Constitutional codification of principles of the given branch of law.

The Constitution of the Slovak Republic, in its third part, provides for the economy of the Slovak Republic, the basic principle of which is the market economy, where from the wording of the Constitution the Slovak Republic shall protect and promote economic competition (Article 55 of the Constitution of the SR). This general principle is authoritative also for financial market law which “covers” instruments and financial market subjects as an inherent part of a market economy. Besides this, the Constitution of

¹⁵ See Ottová, E., Vaculíková, N: *Úvod do právnického štúdia*. Bratislava : Vydavateľské oddelenie PF UK, 2002, pg. 66 et seq.



the SR contains a specific article – Article 56 governing the position of the National Bank of Slovakia as an independent central bank of the Slovak Republic and the backbone of the whole financial market.

4. Existence of a specific system of terms and categories.

The essence of this requirement financial market law is a legal sub-branch representing a set of legal standards governing relations arising in the process of the construction, establishment, functioning and development of the financial market system on the one hand, and the regulation of the financial market by the central bank, other regulatory authorities, or other bodies of general government on the other hand.

Subject of financial market law

Socio-economic relations originating in the process of the financial market activity, in particular in the functioning of its instruments and individual subjects, have a relation to the constitutional, civil, commercial, administrative, financial and other socio-economic, or in this case, already legal relations.¹⁶

At the same time however, in the process of financial market functioning legal relations arise that cannot unequivocally be assigned to the mentioned relations originating in the mentioned “primary” legal branches. These relations form a specific group, falling exclusively in the competence of the financial market law, so in this regard they create a specific subject of law. The issue of whether it is time to lay the scientific basis for the “financial market law” category has already passed, and the need for action is now pressing. Based on this, we take the relations of financial market law as social relations regulated by financial market law norms and legal norms of other legal branches, which represent a comprehensive form of social relations, where their participants have available mutually conditions rights and obligations and realise orders and specific authorisations contained in these standards, with the emphasis on the overall efficient activity of the financial market. Relations of financial market law have the following specific features:

1. Financial market law relations arise in the process of activity of financial market subjects. The fact that the legislator, in creating norms has determined and defined financial market activity as a specific type of human activity worthy of legal regulation, is an important argument in favour of financial market law as a relatively independent branch of law.

2. Financial market law relations are regulated by its norms, but also by standards of other legal branches

(constitutional, commercial, civil, administrative, financial, etc.). In terms of its content, financial market law is complex, and thus represents a specific group in the system of law, where from the aspect of its complexity there is no obstacle for financial market law to use also legal standards of other legal branches, in particular basic ones such as constitutional law, civil law, etc. Thus, financial market law has in its field or in the field of its subject of legal regulation a certain integrational nature.

3. Financial market law relations are of a mixed nature – public-legal as well as private-legal.¹⁷ This is the result of the worldwide trend of strengthening public law to the detriment of private law. This is also connected with the expansion of state interventions, paradoxically into the economy, in particular by administrative-legal standards and regulations of an imperative nature, by regulating ownership relations by the state.

These phenomena and trends then sweep away borders between public and private law and lead towards the origin of new integrated legal branches and institutes, in which the norms of public and private law mutually interleave and mix.

4. Financial market law relations originate in particular due to the regulation of relations connected with finance, or are a manifestation of finance and financial relations by means of money. However, in contrast to financial-legal relations, which always arise in consequence of money, financial market law relations can, besides the above, arise for example also in consequence of the existence and functioning of securities and a whole range of financial market instruments. On the basis of this it can be assumed that these relations are broader than financial law relations which concern only financial resources. It can also be said that a typical feature of financial market law relations is the ownership-legal relation. In this way relations of financial market law come closer to civil-legal, commercial-legal as well as financial-legal relations, etc.

5. One of the parties to the relation of the financial market law is always one of the financial intermediaries – a bank, insurance company, pension fund, or a body of financial market regulations – the central bank, other regulatory authority, etc. The existence of a body of financial market regulations is in these relations a manifestation of the presence of the state, and thus confirms the mixed nature of financial market law's relations and its inclination to both the field of private law as well as the sphere of public law.

6. While civil-legal relations are ownership-voluntary relations in which subjects can autonomously and independently express their will, financial-legal relations on the other hand confirm the state-power nature of legal

¹⁶ See Tosunjan, G., Vikulin, A., Ekmaljan, A.: Bankové právo ruskej federácie všeobecná časť. Moskva : Jurist, 2002, pg. 22 et seq.

¹⁷ For more details see Prusák, J.: Teória práva. Bratislava : Vydavateľské oddelenie PF UK, 1999, pg. 251 et seq.



relations where the voluntary side of parties to the relations is strongly pushed to the background. In financial market law relations we see a combination of both the situations defined above, because parties to these relations have their autonomous will, however the latter is limited by standards, for example, besides the legal frameworks also by standards, or individual legal acts of financial market regulation bodies.

The subject of financial market law, and thus the subject of legal regulation, comprises social relations arising in the process of the position and activity of individual elements of the financial market and its individual instruments. This concerns socio-economic relations relating to:

- legal regulation of individual financial market instruments,
- the financial market system and its individual subjects, their origin, responsibilities and powers, organisation and structure, competence, relations and activities,
- the rights and obligations of natural and juristic persons in relation to individual financial market subjects,
- financial market regulation laws.

Under the system of financial market law we can thus understand the internal division of financial market law into integrated sets of legal norms with regard to their content and to the proximity of relations regulated by them.

Slovak financial market law in its internal structure must be divided into:

- a set of legal norms regulating the standing, powers and activity of individual elements – financial market subjects,
- a set of legal norms regulating individual instruments of the financial market,
- a set of legal norms governing financial market regulation,
- a set of international legal norms adopted in the European Union affecting associated countries of the Central and Eastern Europe, i.e. also the Slovak Republic, which are oriented on the completion of the transition process of Slovak financial market operators over to the international standards.

On the basis of the outlined problem theses we can come to the following conclusion:

The subject of the financial market law are socio-economic relations originating in the process of the creation, functioning and development of the financial market system, in particular its manifold instruments and numerous subjects, which continue to

exist in the process of bodies of financial market regulations, as well as socio-economic relations originating in the framework of financial market regulation by other authorities of general government, in the interest of natural and juristic persons as well as in the interest of the state itself.

Despite the given outline of theoretical starting points for obtaining, for financial market law, a fixed place “under the spotlight” of legal science, it is still being discussed cautiously. In literature, including that of textbooks, authors have so far restricted themselves only to clarifying the term “legal regulation of financial market”.¹⁸ Slovak legal theory is beginning to see the appearance of opinions (where the author of these ideas is their vehement propagator¹⁹) on the establishment of financial market law as a legal sub-branch in the framework of financial law.²⁰

Sources of financial market law

The source of the Slovak financial market law are all forms of law determined by the state, in which appear financial market law norms as rules for conduct of operators. They are normative legal acts issued by the respective state authorities in the form of constitutional acts, laws, legal measures, government regulations, edicts and other generally binding legal norms.

Constitutional acts, laws and legal measures are original normative acts, since they are issued by the supreme authority of the state power, in the case of the Slovak Republic it is the National Council of the SR, by means of elections derived from the power of people.

Government regulations, edicts and other generally binding regulations are derived normative legal acts issued either by the Government, central bodies of general government, which naturally comprise, in the case of financial market law, the Ministry of Finance, but also the National Bank of Slovakia, Financial Market Authority, and indeed even the Stock Exchange.

The source of law, which with regard to the subject of regulation considerably influences also the financial market law, comprises international treaties. In this case this concerns in particular directives of the Council of the European Union.

Although the law sources are of temporal nature, and thus former standards lose force through the adoption of new legal standards, in our interpretation we rely on the given state at the beginning of 2005, which certainly will not become unchangeable, which is also a desirable development in this dynamic field.

The original sources of financial market law are in particular:

Act No 460/1992 Coll. – Constitution of the Slovak Republic,

¹⁸ See e.g. Bakeš, M. a kol.: Finanční právo. Praha : C. H. Beck, 2003, pg. 525 et seq.

¹⁹ See Balko, L.: Právo finančného trhu. Bratislava : EPOS, 2001, pg. 17 et seq.

²⁰ See Babčák, V., Balko, L., , Králik, J.: Finančné právo. In: Práca PP 12 – 13, 2001, pg. 16 et seq.



Act No 566/1992 Coll. – on the NBS, as later amended,
 Act No 483/2001 Coll. – on banks, as later amended,
 Act No 95/2002 Coll. – on insurance industry, as later amended,
 Act No 191/1950 Coll. – on bills of exchange and cheques,
 Act No 40/1964 Coll. – Civil Code, as later amended,
 Act No 530/1990 Coll. – on bonds, as later amended,
 Act No 513/1991 Coll. – Commercial Code, as later amended,
 Act No 310/1992 Coll. – on building society savings, as later amended,
 Act No 566/2001 Coll. – on securities, as later amended,
 Act No 202/1995 Coll. – Foreign Exchange Act, as later amended,
 Act No 118/1996 Coll. – on the protection of deposits, as later amended,
 Act No 80/1997 Coll. – on the Export – Import Bank of the Slovak Republic,

Act No 594/2003 Coll. – on collective investment, as later amended,
 Act No 429/2002 Coll. – on the Stock Exchange,
 Act No 96/2002 Coll. – on financial market supervision,
 Act No 747/2004 Coll. – on financial market supervision,
 Act No 650/2004 Coll. – on additional pension savings.

Besides the original, i.e. legal sources of financial market law, there are still a number of derived sources of financial market law, particularly in the form of government regulations, decrees, measures of the Ministry of Finance and those of the National Bank of Slovakia.

The third important group of sources of financial market law are those based on its international aspect. The most important of these, especially from the aspect of the integration of the Slovak financial market system into the European financial market system, are legal standards adopted in the framework of EU law.