

UNINSURED DEPOSITOR RIGHTS PROTECTION IN BANK INSOLVENCY

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Abstract

The objective of the article is legal instruments protecting uninsured depositor in bank insolvency. The paper is focused and reviews issues relating to the unprofessional depositor with typology of insolvent Lithuanian bank “Snoras”. According to this view, the paper analyses legal aspects of the bank’s specific obligations to the depositor under Lithuania’s bank insolvency rules and regulations. The purpose is, by means of different methods, to investigate depositor’s rights protection concept covering uninsured bank’s product - deposit certificates. This paper reveals the content of legal norms regulating uninsured depositors in bank insolvency (laws, secondary legislation, especially court decisions of Lithuania), analyzes what problems arise in an attempt to ensure depositor rights and discusses the impact for uninsured depositor *ex ante* and *ex post* bank insolvency. The main issue of the paper: what are the legal techniques protecting uninsured depositor rights under bank insolvency frameworks? The issue based on the typology of insolvent bank “Snoras” which actively disseminated deposit certificates to the customers in order to improve the bank’s financial stability, without increasing the share capital of the bank, for that reason, bank misinformed the owners of deposit certificates that such a product is treated as insurance object. The paper is written from the Lithuanian law perspective.

Purpose – to investigate depositors’ rights protection terms covering uninsured bank’s product- deposit certificates.

Design/methodology/approach – Purposely to explore the actual meaning of legal norms and legislations as well as content and to analyze the literature and jurisprudence the systematic, analyses, synthesis, comparative methods were used.

Findings – all depositors have full interest to be treated as insured with the consequent of compensation. Deposit protection is designed to compensate some classes of depositors in case of bank failure. In Lithuania depositors protections scheme is limited to protecting small depositors (up to 100.000 EUR). On the other hand, it contains problems of “moral hazard” (set of incentives for the protected to behave differently- irresponsibly, carelessly or less conservatively- simply because of the existence of protection). However, before bank “Snoras” became insolvent, one class of depositors were misinformed about the terms and their rights protected by selling specific bank’s product – deposit certificates. For that reason, firstly they received treatment as uninsured creditors. On the other hand, legal principle “know your customer” is now a widely accepted obligation on banks. However, the legal principle “know your bank” or the principle “know your contract” applied to depositors or unprofessional customers have some specific rules

and is not applied directly. The rule - once customers sign a contract they are generally bound, even if they have not read its terms- is partly illegal. Yet banking contracts are still standardized in Lithuania. The securities laws nowadays should demand not only “formal” written agreements with the clear description and professional consultation before signing the contract with private customers (depositors) in areas such a fund management or deposit certificates. Even if the clauses are found to have been incorporated in a contract, they may be construed against a bank. *The contra proferentum* rule is applied in cases of ambiguity or where other rules of construction fail. If it is applicable, it results in a contract being construed against its makers. Exclusion clauses must explicitly state that they extend to a bank’s oral, as well as written, misrepresentations, include its failure to exercise reasonable care and skill and cover both direct and consequential losses.

Practical implications – The paper is focused on particular misleading legal interpretations of the unprofessional client in the context of insolvent Lithuanian bank “Snoras” typology. Another significant issue, analyses problematic aspects of the bank’s obligations, which are very specific in bank bankruptcy frameworks. Thus, bank insolvency affects not only public interest but private interests as well as. Customers' interests are also effected, for that reason, it is necessary to investigate the depositor rights protection area and the first question to consider is, what bank behavior is legally intolerated and unacceptable to depositor certificates holders in bank insolvency? The issue based on the fact that Lithuanian bank “Snoras” actively disseminated deposit certificates *ex ante* bank insolvency. So what happens *ex post* and is there any legal chances to treat deposit certificates as an insurance object with the compensation to depositors? The issue is relevant to Lithuania banks depositors, academic society as well as the jurisprudence of Lithuania.

Originality/Value – Processes of bank insolvency are recurrent phenomenal. The banking industry has faced great legal and economic challenges in the last few years of financial crisis. Lithuania is not an exception. Two Lithuanian banks faced insolvency almost in a year. These cases require new legal viewpoint in the area of depositor rights protection and market discipline. Furthermore, due to the bank insolvency, not only public interests but the private interests as well as depositors are affected. Besides, recent new jurisprudence has formed in Lithuania courts, in the context of bank consumers (depositors) - unskilled, unprofessional and unpracticed on occasion specific bank products (certificate of deposit) – so it requires a new legal viewpoint in order to identify legal relations between secured and unsecured depositors.

Keywords: Bank insolvency, bank, uninsured depositors, deposit, deposit certificates.

Research type: research paper.

Introduction

Processes of bank insolvency are recurrent phenomenal. A noteworthy feature of banks insolvency that bank’s failure can postulate a country's legal and financial resources and risks. It is universally known that the bank sector had great legal and economic challenges in the last few years of financial crisis. Lithuania is not an exception. Two banks faced insolvency¹ cases almost in a year. These Lithuania banks insolvency

¹ The Republic of Lithuania, Vilnius district court decision, Civil Division, 12 December 2011, in the civil case Central bank of Lithuania v. AB bank “Snoras” (civil case No. B2-7791-611/2011).

cases have implemented social, economical and legal changes which require a new legal attitude. Furthermore, not only public interests but the private interests as well (as depositors) are affected in bank insolvency. It is widely known that banks traditionally borrow money from depositors (and others) which is typically repayable either on demand or on relatively short notice and then much of that money to a variety of borrowers¹. Moreover, deposit insurance has traditionally served two purposes: consumer protection and the prevention of bank runs. This article focuses on consumer (depositors) protections which is based on the new jurisprudence of Lithuania, in the context of bank depositor protection - unskilled, unprofessional and inexperienced. Following this the main issue of the paper is legally intolerable and unacceptable bank behavior which leads to the breach of depositor rights.

Basically, in the case of insolvent bank the interest of creditors is more complicated due to the existence of different types of depositors (insured and uninsured). Indeed, some lawyers argue that “*ideally the system should be designed to ensure that there are controls on the behavior of management while at the same time ensuring that those who deposit money in banks have to take some responsibility for their actions*”². On the other hand, the relationship of banker and customer is primarily that of creditor and debtor³. The amount deposited by a customer becomes part and parcel of the bank’s own money. Moreover, the behavior of bank “Snoras” management was potential fraudulent⁴.

To continue, depositors are often treated as a privileged class due to state support and insurance system⁵. Unfortunately, sometimes banks are faced with temporary liquidity problems which lead to the necessity of seeking assistance from the Central bank or necessity to provide high risk products into the market in order to keep their capital on required level. However, sometimes it leads to bank liquidation (bankruptcy). When the bank is liquidated in Lithuania it is reliable that all the creditors (depositors) will receive full payment of the amounts they are owed (in Lithuania up to 100 000 EUR equivalent⁶). Deposit insurance is nowadays needed because it is impossible to avoid a commitment to protect depositors. However, it is hardly reliable that those creditors who are uninsured can expect to implement their financial claim from the general asset pool. For that reason, naturally - all depositors have full interest to be treated as insured

2013 02 18 Central bank of Lithuania took decision No. 03-31 announcing insolvency of AB “Ūkio bankas” [interactive] [accessed 2013-03-13]. http://www.lrv.lt/Posed_medz/2013/130220/19.pdf

¹ Campbell A. 2006. Bank insolvency and the interests of creditors. *Journal of Banking Regulation*.UK: University of Leeds, 7 (1/2): 133-144

² Campbell A. 2006. Bank insolvency and the interests of creditors. *Journal of Banking Regulation*.UK: University of Leeds, 7 (1/2): 133-144

³ E.P. Ellinger et al. 2006. Ellinger’s Modern banking law, New York: Oxford University press, p. 118

⁴ The review of bank “Snoras” bankruptcy process made by Central bank of Lithuania and presented to the Republic of Lithuania Seimas [interactive] [accessed 2013-03-13]. http://www.lb.lt/seimo_posedyje_ab_banko_snoras_bankroto_proceso_apzvalga_1

⁵ Campbell A. 2006. Bank insolvency and the interests of creditors. *Journal of Banking Regulation*.UK: University of Leeds, 7 (1/2): 133-144

⁶ Republic of Lithuania Law on insurance of deposits and liabilities to investors. *Official Gazett* . 20 June 2002, No IX-975

deposits (with the right to compensation). Though, some creditors of a bank received special treatment as secured and some of them were misinformed about the terms and their rights on previous contracts of deposit.

General legal framework of bank deposits and insured bank products in Lithuania

First of all, analyzing depositors' interest to be treated as insured depositors, it should be taken into account that under the most basic service bank can provide as a depository for depositors' money. This is the essence of commercial banking. It provides a legal definition for banking¹. Accordingly, it is described as *a bank - customer relationship*. In general, a customer is regarded as an uninsured general creditor, whose claim is subordinate to those of preferential claim holders (insured depositors) and to those of insured creditors. As a general creditor, in case of bank insolvency, the uninsured customer acquires a dividend based on the amount of the surplus remaining after the settlement of insured and preferential claims. Usually, the public generally holds its deposits with banks in the form of accounts, others as a form of long-term or short-term deposits, or derivative financial instruments (e.g. deposit certificates). However, multifunctional banks in Lithuania hold the public's money in other forms as-in various collective investment schemes, funds, and insurance products² as deposit certificates.

Secondly, most developed countries (included Lithuania) have established schemes that protect depositors from the possibility that their bank will become insolvent. It should be noted, that *“deposit insurance and regulatory intervention (i.e., the bail-out and closure policy) are standard regulatory instruments employed to avoid systemic banking crises”*³. It is necessary to focus that deposit insurance provides a guarantee to depositors that their claims will be repaid (generally up to a maximum) and so eases depositors' fears in times of perceived financial weakness, but what happens with the similar products⁴. Deposit insurance as well as other prudential measures does not completely eliminate the instability in banking or defaults made by bank. To illustrate, *“bank runs may still occur from the wholesale side, from uninsured depositors, or from short-term creditors that terminate their roll-over contracts or demand additional collateral”*⁵. Nevertheless, borrowers could induce severe “moral hazard” (set of incentives for the protected to behave differently- irresponsibly, carelessly or less conservatively- simply because of the existence of protection). In fact, as it is mentioned in scientific literature

¹ Cranston R. 2008. Principles of banking law, Second edition, New York: Oxford university press, p. 159

² Campbell A. 2006. Bank insolvency and the interests of creditors. *Journal of Banking Regulation*.UK: University of Leeds, 7 (1/2): 133-144.

³ Marinc M. and Vlahu R. 2012. The Economics of Bank Bankruptcy law. Berlin: Springer – Verlag Berlin Heidelberg.1-53

⁴ Marinc M. and Vlahu R. 2012. The Economics of Bank Bankruptcy law. Berlin: Springer – Verlag Berlin Heidelberg.1-53

⁵ *ibid*

“deposit insurance could even undermine stability by encouraging banks risk-taking, due to decreased market discipline from depositors”¹

Due to Lithuanian law on insurance of deposits and liabilities to investors, depositor is understood and should mean *“a natural or legal person holding a deposit with a bank, a branch of a bank or a credit union, with the exception of the entities whose deposits under this Law may not be covered by insurance”²*. To add to, insurance event legally should mean the moment when *“institution of bankruptcy proceedings against a bank or taking of a decision of a supervisory authority on discontinuation of banking activities, acceptance of deposits or provision of investment services where the bank is not able to settle with creditors”³*. The object of insurance according to Lithuania law is treated as deposit insurance coverage which should be provided for depositors’ deposits in Litas and in a foreign currency. However, *“insurance coverage may not be provided to the debt securities (deposit certificates) issued by the same insured or the liabilities arising out of own acceptances and promissory notes, the mortgage bonds issued under the Republic of Lithuania Law on Mortgage Bonds and Mortgage Loans, also the deposits of or liabilities to the following entities: 1) the Bank of Lithuania; 2) insurance undertakings; 3) credit institutions; 4) financial brokerage firms; 5) the insurance undertakings operating under the Law on Insurance; 6) pension funds; 7) management companies; 8) the undertakings engaged in leasing (financial lease); 9) collective investment undertakings”⁴*.

To consider, there were a few cases analyzing the legal issues of deposit certificates in Lithuania court practice under the framework of bank insolvency. One of the major victory for bank “Snoras” deposit certificate holders was a decision of the Lithuania Court of Appeal⁵, announced in 2013 01 10. The case investigated the legal relationship between deposit certificates, deposit and depositors rights in bank insolvency. It should be noted that, the idea that bank insolvency law must align itself with modern bank insolvency practice and principles, the customer in this research is understood as depositor- unprofessional client. To continue, the article pays attention to the impact of legal relationship between banks and their customers (depositors).

Deposit v. Deposit certificate. Delimitation of insured and uninsured deposits.

Bank “Snoras” typology and consequences of deposit insurance. First of all, we should consider the principal justification for deposit insurance - “know your customer”,

¹ ibid

² Republic of Lithuania Law on insurance of deposits and liabilities to investors. *Official Gazett* . 20 June 2002, No IX-975. Article 2, clause 4.

³ Republic of Lithuania Law on insurance of deposits and liabilities to investors. *Official Gazett* . 20 June 2002, No IX-975. Article 2

⁴ Republic of Lithuania Law on insurance of deposits and liabilities to investors. *Official Gazett* . 20 June 2002, No IX-975. Article 3.

⁵ The Republic of Lithuania, Court of Appeal, Civil Division, 10 January 2013 ruling of the board of judges in the civil case V. M. M. v. insolvent bank “Snoras”(civile case No. 2-145/2013).

which is now a widely accepted obligation on banks. However, the principle “know your bank” or the principle “know your contract” for bank’s depositors *ex ante* have some specific rules. When the specific provisions of nonperforming loans were increasing a lot of insolvency problems were considered naturally in bank “Snoras”, in the end 2009. The capacity rate decreased up to 7,19 %, meanwhile the capacity of other bank reached 13, 5 %. 2011 12 07 bankruptcy was announced to AB “Snoras”¹. Secondly, in view of these points, it is known that, bank “Snoras” actively disseminated deposit certificates² to the customers in order to improve the bank's financial stability, without increasing the share capital of the bank. Deposit certificates were treated by the bank and presented to potential depositors as means equivalent to the terms of deposits. To add to, in order to sign the contract, more than market value interests were suggested to the clients³. Thus, in fixed deposits the rate is usually higher in long-term deposits⁴ than in short-term deposits or in deposits payable “at call” (meaning “on demand”). Furthermore, the rate may depend on the deposited amount but not on uncertain bank’s targets. From the practical point of view, the bank’s profit is, principally, the difference between the interest that it pays to its customer and the amount which it earns by investing the amounts deposited with it.

De iure, as it was mentioned, deposit certificate is not insured bank product according to Lithuania law (*chapter D*). Such a bank’s product is understood as securities, specifically, “a bank certificate is a written bank document containing a statement on the monetary contribution and granting the depositor the right to receive that contribution and interests subject to the time-limits stated therein”⁵. On the other hand, *de facto* such deposit certificates were supplied and presented to the customers (depositors) in the Lithuania market as equivalent to the bank “Snoras” deposit instruments. Contracts were included terms with the obligation that the deposit is insured and un-professional customers are treated with the highest level of legal protection. Moreover, the contracts of deposit certificates misinformed the customers (depositors), disclosed some unfair terms and lead to sign a contract associated with a high risk terms⁶. Bank “Snoras” was not suspected as unreliable. To continue, it should be considered these main breaches of depositors rights according to Lithuania bank “Snoras” typology .

Depositor rights protection. Disclosure of information in the contracts of deposit certificates. Deposit certificates contracts were signed under the legal framework of

¹ The Republic of Lithuania, Vilnius district court decision, Civil Division, 12 December 2011, in the civil case Central bank of Lithuania v. AB “Snoras” (civil case No. B2-7791-611/2011).

² *ibid*

³ Public information of the association of bank „Snoras“ depositors. www.indelininkai.lt [interactive] [accessed 2013-03-10]

⁴ A deposit that can be withdrawn only after a specified period of time; for example, a three month deposit or a six-month deposit. These deposits pay interest at close-to-market rates and are also known as fixed deposits.

⁵ Civil Code of the Republic of Lithuania. *Official Gazette*. 18 July 2000 No VIII-1864, 1.107 article, unit 1.

⁶ The Republic of Lithuania, Vilnius district court decision, Civil Division, 12 December 2011, in the civil case Central bank of Lithuania v. AB “Snoras” (civil case No. B2-7791-611/2011).

service agreement¹. According to the Lithuania law, consumers “*means a natural person, who expresses his intention to buy, buys and uses goods or services to meet his own personal, family or household needs are outside his business or profession*”². Additionally, contract of deposit is legally understood as public contract. Furthermore, due to Lithuania Civil Code which regulates obligation of the provider of services to furnish information before the contract for services is entered into force, the provider of services is bound to provide the client with detailed information concerning the nature of the services that are provided, the terms of their provision, the price of the services, the schedule for the services, possible consequences, and any information which may have an influence on the client’s determination to enter into the contract. Eventually, on the basis of the service contract bank as the entity of financial broker, providing the client with investment services, the client is treated as an unprofessional client category³.

Certainly, *ipso facto* the obligations to the bank goes from Lithuania Law on Markets in Financial Instruments, which regulates the safeguard of investors also defines “*non-professional client (a customer who is not attributed either to professional clients or to eligible counterparties)*”⁴. Furthermore, “*a financial brokerage firm must clearly and comprehensible supply to clients and potential clients all the required information on the basis whereof they would be able to understand the essence of the investment services and financial instruments that are being offered as well as the risk typical thereof and to take investment decisions on an informed basis. The information may be provided in a standardized format. Besides, a financial brokerage firm must supply the information about financial instruments and proposed investment strategy, including guidance on and warning of the risk which is typical of certain investment strategies or investments in certain financial instruments*”⁵.

Alternatively, similar position is followed in opposite law systems, as in Common law Jurisdictions. A signature of a document is a formal device there, and means that parties can treat a contract as concluded. The Rule is the subject to a number of limited exceptions; *non est factum*; fraud and misrepresentation; undue influence and unconscionability; and that document did not appear to be contractual. Nevertheless, it may also be that there is an exception where the signature was otherwise written in circumstances in which it did not signify the customer’s assent to be bound. An absent signature, however, customers (depositors) may be able to argue that the bank’s written terms have not become part of the contract. The bank has to establish that customers

¹ The Republic of Lithuania, Vilnius district court decision, Civil Division, 12 December 2011, in the civil case Central bank of Lithuania v. AB “Snoras” (civil case No. B2-7791-611/2011).

² The Republic of Lithuania Law on consumer protection. *Official Gazette*. 10 November 1994, No I-657.

³ Civil Code of the Republic of Lithuania. *Official Gazette*. 18 July 2000 No VIII-1864, article 6.719.

⁴ Republic of Lithuania Law on Markets in Financial Instruments. *Official Gazette*. 18 January 2007, No X-1024, article 3.

⁵ Republic of Lithuania Law on Markets in Financial Instruments. *Official Gazette*. 18 January 2007, No X-1024, units 22, 24, 25 section 2 and 3.

were given adequate notice of them. This is a question of fact and a court will give attention to all circumstances of a case¹.

Essentially, in the particular case of bank “Snoras”, it was identified that service agreement on deposit certificates and contracts’ description (annexes) part were not reasonable in order to make the decision that the bank informed the customer rightly about all potential risks. One of the major legal arguments is the fact that the risks and the characters of financial instruments which were regulated in the bank “Snoras” contract’s annexes were made and introduced by the bank to the costumers, appointed to the professional clients as well as to the unprofessional clients (unskilled and unqualified). Overall, the court made the positive decision to the deposit certificates owners based on these arguments: i) if the client is not directly, explicitly informed about deposit certificates as financial market instruments it should be treated as insurance object ii) The Court noticed that deposit certificates is not insured by the state insurance system and the bank “Snoras” did not clearly disclosed all necessary information under the consumers rights protection which was required in order to sign the contract. In such a circumstance background, extraordinary situation formed, and after bank insolvency it was declared that the owners of deposit certificates have no right to insurance object (bankruptcy administrator refused to fulfill such a creditor's claim). Lastly, the Court announced that deposit certificates should be treated us objective of insurance.²

Unfair actions and specific terms in deposit certificates. Due to service contracts regulation, which is regulated by the Republic of Lithuania Civil code³, it is required that the parties would treat each other with fair behavior not only during performance and execution of the contract but also before signing the contract. It means that parties should disclose all information (included negotiation process), which is fundamentally important and significantly or relevant in order to make an agreement. Therefore, Lithuania Court of Appeal made a reasonable decision based on the facts that the bank “Snoras”, before signing the contract, needed to disclose all the information he had about the specific bank product- deposit certificate. Also, he had the obligation to collect and evaluate the information about the client's investment experience and capacities or abilities understand the risks and make a decision - sign or refuse to sign on financial instrument agreement. It means the bank should identify and make more reasonable and detailed decisions whether the investment instrument is suitable for the client or not.

Up to a point, when a depositor who has been granted and qualified as unprofessional client category, is left by his own to evaluate independently of all potential and possible risks of financial instrument, in such scenario, the client is not applicable for such customer information and the situation should be treated as a law breach according

¹ Cranston R. 2008. *“Principles of banking law”*, Second edition, New York: Oxford university press, p.145.

² The Republic of Lithuania, Court of Appeal, Civil Division, 10 January 2012 ruling of the board of judges in the civil case V. M. M. v. insolvent bank “Snoras”(civil case No. 2-145/2013).

³ Civil Code of the Republic of Lithuania. *Official Gazette*. 18 July 2000, No VIII-1864, article 1.5 and 6.158

to the client’s knowledge, skill and experience levels. Furthermore, the ability to carry out a proper evaluation of investment risk independently is significant as well¹.

It should be taken into account, that conditions of deposit certificate contracts should be considered deeply, in details, should be individualized with the separate confirmation of signature which should be made by the owner of deposit certification. In that particular case, a customer is denying that description or annexes of the contract were presented by the bank properly, to add to he have never had the experience with financial instruments before. It is presumed, due to the jurisprudence and law of Lithuania, that the obligation of the bank is to provide the court or FSA (*Financial Services Authority*) with the evidences about the proper implementation of obligations in disclosing all necessary information to the client. Particular information includes the clauses about the contribution of the risk inherent (granting of the deposit certificate) and information about the performance of the contract. Also, it should be noted, that the bank as a subject, which bears the obligation of proving a circumstance related to his duties, falling due to execution of the contract. Consequently, the bank must assume the obligation of risk factors and means of evidences, as well as to disclose terms of contract content properly.

In bank “Snoras” insolvency case, the bank did not provide any further evidences of such a fact, except the purchase agreement of the deposit certificate under detailed standard conditions (expresses the statements of deposit certificates owners, it declares “that he fully familiar with the description and agrees with its terms”²),.

Comparatively, in Britain, there were some cases where depositor said “some clauses which I have seen would to be printed in red ink on the face of the document with a red hand pointing to it before the notice could be held to be sufficient”³. That approach was applied in another leading Court of Appeal decision, where nothing was done to draw the customer’s attention to the relevant condition: it was merely one of four column’s width of conditions printed across the foot of the delivery note. Consequently, the court held that it never became part of the contract between parties.⁴

Standard terms in the agreements of deposit certificates. Contra preferentum rule. Standard terms also enable the bank to set parameters (or at least to attempt to do so). Thus, by terms which are usually represented by the counterparts and the confirmation that the written contract is the entire and final agreement between the parties is required. According to Lithuania law, “*standard conditions shall be such provisions which are prepared in advance for general and repeated use by one contracting party without their content being negotiated with the other party, and which are used in the formation of contracts without negotiation with the other party. Besides, standard conditions*

¹ The Republic of Lithuania, Court of Appeal, Civil Division, 22 November 2012, (civile case No. 2-2098/2012)

² The Republic of Lithuania, Vilnius district court decision, Civil Division, 12 December 2011, in the civil case Central bank of Lithuania v. AB “Snoras” (civil case No. B2-7791-611/2011).

³ Royal Courts of Justice, EWCA Civ 6, 12th November 1987, Interfoto Picture library limite v. Stiletto visual programmes limited, Case No. 480669,

⁴ Ross Cranston, Principles of banking law, Second edition, oxford university press, 2008, p. 146

*prepared by one of the parties shall be binding to the other if the latter was provided with an adequate opportunity of getting acquainted with the said conditions*¹. What’s more, it is agreed² (on the standard term implementation) that in case one part acceding the agreement so that standard contract terms are binding on the other party only if the standard contract developed party revealed the clauses to another party. Lastly, the fact that the other party has been properly introduced to the standard terms of the contract must be proved by the party which developed and prepared standard terms as a contract.

Rationality in the contracts of deposit certificates. Qualifying uninsured deposits as insured or whether there was a misunderstanding or not, the criteria of reasonableness is also applicable³ i.e. party claiming that it was wrong behavior must be considered in the considerations as prudent, careful person, under the same circumstances behavior (means that other normal and reasonable person, knowing the true statements of affairs in a similar situation would sign the same transaction)⁴.

Bank as more substantial part of deposit certificates contracts. The legislator indicated that the financial sector, which includes a significant part of the banking sector in Lithuania, is attributable to one of the most social sensitive sectors and the situation in this sector could have a significant impact on the country's economy, citizens trust and economic subjects trust and confidence in the country's financial system. It is declared in the Financial Stability Act general provisions⁵. In order to strengthen the use of the financial system, this system should be sustainable, therefore, it is necessary to ensure applicable and timely implementation of financial stability and effective remedy. Afterwards, these provisions indicate that the stability of the financial system is understood as public interest⁶.

To conclude, from the eighteen century banks have attained a high reputation as regards creditworthiness and honesty in dealings. The public trust is enhanced by the fact that banks are strictly controlled and supervised by the Financial Services Authority. In countries like Germany, the Netherlands, and Switzerland there are general business conditions for accounts and deposits, drawn up by associations of banks. In Britain banks have now adopted codes of practice when dealing with personal customers. ⁷However, due to Lithuania central bank law, there is no direct obligation to the Central bank of Lithuania to control the products of the banks and especially terms of contracts. To add to, association of banks in Lithuania also is not providing any particular

¹ Civil Code of the Republic of Lithuania. *Official Gazette*. 18 July 2000 No VIII-1864, Article 6.185.

² The Supreme Court of Lithuania, Civil Division, 25 September 2012 ruling the board of judges I.J. v. “Balticums draudimas” (civil case No. 3K-3-516/2006).

³ Civil Code of the Republic of Lithuania. *Official Gazette*. 18 July 2000 No VIII-1864, article 1.5).

⁴ The Supreme Court of Lithuania, Civil Division, 9 October 2000 ruling the board of judges L. L. v. V. L., D. B. L., I. B (civil case No.3K-3-974/2000).

⁵ The Republic of Lithuania Law on Financial stability act, *Official Gazette* .2009, 22 July, 2009 No. XI-393, general provisions.

⁶ The Supreme Court of Lithuania, Civil Division, 20 February 2012 ruling of the board of judges in the civil case A.P., D.V. v. DNB Nord bank (civil case No. 3K-3-58/2012.)

⁷ E.P. Ellinger et al. 2006. Ellinger’s Modern banking law, New York: Oxford University press, p.204 and 130-135

recommendations on the standard terms implementation e.g. contracts of the deposit certificates (except very general code of good banking practice which are not legally binding and with very general provisions¹). Regarding the law in Lithuania, the banks should take their own risks of their products included operational risk (information obligation, fair behavior of their employees etc.). Presumably, the customers must pay attention to uninsured deposits (especially deposit certificates) and their conditions themselves or take private consultants before signing the contract. It is recommended to apply an act the courts may well use them as a basis for implying terms into the bank-customer relationship.

Conclusions

Existing depositors insurance compensation system in Lithuania gives rise to “moral hazard”: there is no incentive for depositors take care in their choice of bank. For that reason they were not careful enough analyzing the contract terms of deposit certificates before signing the contracts. However, due to the Lithuania’s court practice, courts treated and defined the legal conditions, under which uninsured depositors could be treated as insured. Bank “Snoras” practice was unsafe, unsound and illegal banking practice. Such a misbehavior of the bank should require regulatory actions *ex ante* in order to avoid disputes *ex post*.

Even if the clauses are found to have been incorporated in a contract, they may be construed against a bank. *The contra proferentum* rule is applied in cases of ambiguity or where other rules of construction fail. If it is applicable, it results in a contract being construed against its makers.

Exclusion clauses must explicitly state that they extend to a bank’s oral, as well as written, misrepresentations, include its failure to exercise reasonable care and skill and cover both direct and consequential losses. Supervisory authority should draw new rules and obligate all Lithuania banks to keep them in order to control such banking product as deposit certificate. FSA should have the right to take sufficient formal actions *ex ante* bank insolvency e.g. standardizes bank’s contracts, restrictions of banking activities or banking license due to the misinforming the bank depositors with their rights.

Yet banking contracts are still standardized in Lithuania. The securities laws now should demand not only “formal” written agreements with the clear description and professional consultation before signing the contract with private customers (depositors) in areas such a fund management or deposit certification. It is recommended to apply an act or secondary legislation (e.g. by FSA) the courts may well use them as a basis for implying terms into the bank-customer relationship. One of the options is to draw the act which will ensure the detailed proves up to the signing the contract (e.g. annexes, detailed form of the contract’s description, video or audio records in electronic file or similar). Eventually, it will let to recognize the disclosed information to the customer).

¹ Lithuania association of banks. Good practice code of the banks. [interactive] [accessed 2013-03-13]. <http://www.lba.lt/index.php?-1720901939>

The rule - once customers sign a contract they are generally bound, even if they have not read its terms - is disputed. Justification for this rule focuses on form, not substance. It should be noted that the jurisprudence of Lithuania takes the right position protecting consumer (depositors) contracts as a weaker part in the context of bank insolvency.

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