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Co-operative Banks and Credit Unions – the Past and the Present

Abstract

The co-operative banking system holds a permanent place in all social-economic systems existing today. It has gained quite big popularity in market economies providing services for the sectors of production, services as well as agriculture. Scope of operations carried by co-operative financial institutions in particular countries tends to vary and they also have their specific features in different countries. It is due to conditions prevailing in these countries, which either promote or hamper the development of co-operatives. These conditions can be said to include, for instance, existing traditions of the co-operative movement, a climate favourable for co-operatives, legal, economic and other factors advantageous for their development. A long and rich history of the Polish co-operative banking system holds a permanent place in Poland's history. It is one of the oldest forms of co-operatives operating till the present time.

Co-operative banks and other co-operative entities operating in the financial market are characterised nowadays not only by their tradition but modernity as well. They benefit from rich and long traditions, but they also take into account the needs of communities, in which they exist.

Introduction

The systemic transformation of economy in the direction of free market principles exerts its impact on the co-operative sector and requires such concentration of the co-operative movement that would allow co-operative entities to be competitive in the market and simultaneously preserve their

specific characteristics. The most important change resulting from economic determinants for co-operatives is the necessity of adapting their mission, goals, strategies and organisational forms to requirements posed by the market, in which they operate. It refers also to co-operative banks. In order to preserve their co-operative character they have to aim at satisfying needs of their members and act in their interest. A means allowing to achieve this goal is generating profit by a co-operative in long term.

At the time when definite concepts of a liberal and co-operative market economy clash in forming the mission of the co-operative system in Poland it is necessary to create conditions for co-operatives allowing them to choose freely such organisational solutions, that could permit them to operate in such form and on such scale, which would correspond to their capabilities. The choice of a form and scale of activity should be verified through confrontation and competition with other entities. However, diversity of co-operative forms can be restricted by international co-operative principles, the co-operative law and acts regulating economic activity along general principles in the market of financial services.

Such source of restrictions for the co-operative banking is the banking law, the Act of Narodowy Bank Polski (National Bank of Poland), the Act of Restructuring Co-operative Banks and Bank Gospodarki Zywnosciowej (Food Economy Bank) as well as the Act of Co-operative Savings and Loan Institutions of 14th December 1995.

The main prerequisite underlying the establishing of co-operatives seems to be to achieve economies of scale in conditions characterised by a relative surplus of human factor and a search for a scarce capital through combining small capital resources (shares) of persons associating to accomplish a definite economic goal. Creation of capital potential from small but numerous shares is prompted by an economic necessity of protecting interests of social groups, which cannot cope individually with competition on the part of other economic units. Hence, a prerequisite of a market force of co-operatives (co-operative banks) is their membership, which should balance a high competition for capital by an alternative form of economic activity. It represents a challenge faced not only by traditional co-operatives but also by co-operative banks and other entities in the market of financial services such as, for example, Co-operative Savings-Loan Societies.

1. Outline of the co-operative banking development

Although co-operative ownership can be found in all social-economic systems, it has not assumed a dominant position in any one of them. It could be also added that this form of ownership does not receive too much attention in scientific literature, it is seldom an object of empirical studies, deliberations of theoretical character on this subject are missing and so on. Such is the case, because the co-operative ownership was recognised to be poorly effective losing ground definitely in this respect to capitalist ownership. This opinion consolidated for a long time is not accidental. It ensues from long years of experience connected with operation of co-operatives in many countries. A similar situation prevails in the banking sector. Co-operative banks or credit unions, owing to which credits are available more easily, restrict their services, however, to a separate sector of clients. Their competitiveness limited for capital reasons accounts for the fact that the co-operative ownership plays a marginal role in different social-economic systems. It could be added that it is an indispensable margin proving its importance in definite conditions or selected fields of economic activity. Operation of co-operative institutions results also – and it must be underlined – from demand for this type of joint ownership existing in society, for co-operative principles of democratic, self-government management of property. These elements can be perceived not only in traditional producers' co-operatives but also in the sector of financial services, where the first savings and loans associations called folk banks were established already in the 19th century. Principles of their operation were developed by Schultze from Delitsch in Germany in the 19th century. He bound, for instance, small traders and craftsmen, who were setting up credit organisations, to run their institutions by themselves and not to engage savings entrusted to them in risky (although potentially profitable) financial undertakings. The main principle accepted by Schultze was providing a loan from own funds and, thus, along mutual assistance lines. The idea of financial mutual assistance was shifted to villages later on by co-operative activist Friedrich Wilhelm Raiffeisen¹. „Raiffeisenian” companies operated according to partly different principles, as they introduced a principle of holding a share, although in a very small amount and laid emphasis on savings. The statutes of these co-operatives called also credit unions specified the goal of their activity: „The goal of an association is not so much to generate

¹ *Blizsza kasa niż bank (A savings society closer than a bank)*, Gazeta Wyborcza, 10th September 2002.

profit but rather to support economically weak people and ensure their spiritual and moral development”².

The first Polish financial entities operating along co-operative principles and on the basis of legal regulations pertaining to co-operatives were established in the second half of the 19th century, although their activity tended to vary depending in which part of partitioned Poland they operated. The history of Polish co-operative banking³ dates back, however, to the Medieval Ages, when prototypes of present savings and loan societies appeared. They were called merchant guilds, religious bank or the so-called widow societies. The main reasons why they were established was self-defence against usury and financial mutual assistance. Later on the social-economic foundation for their expansion was development of capitalism.

Operation of co-operative units was based on principles followed today as well: common character of membership, equality of votes, selling products only for cash, refunds from purchases proportional to the extent of benefiting from a co-operative as a company (distribution of profit); a dividend limited to the amount of shares, indivisibility of the reserve fund.

Practical implementation of the co-operative programme in Poland had its roots in Catholic milieus and primarily in the clergy. Its precursor was priest S. Staszic, who set up „Hrubieszow Agricultural Society of Saving One Another Jointly in Calamities” in 1816. The actual cradle of the Polish co-operative system, especially with regard to organisational forms, on a mass scale was Wielkopolska (Central-Western Poland), which was mainly due to initiatives and huge efforts made by priests: A. Szamaszewski, P. Wawrzyniak and S. Adamski. Unity of co-operatives and moral, social-economic and national goals achieved by them under successive leaders radiated onto territories of the remaining partitions.

The first credit co-operative on Polish territories was established in Poznan in 1861. It was called „Loan Society for Industrialists from City of Poznan”. It is practically from that date that the history of Polish co-operative banking starts. Further co-operatives appeared in the following years and their propagators were the then pioneers and activists of the co-operative movement. The first decade of the 19th century witnessed its dynamic development. The main goal of this movement, similarly to other European countries, was protection of the poorest social strata against exploitation. The Polish co-operative movement, although organised after the western model, was

² J. Ossowski, *Raiffeisen: Apostoł biednych (Raiffeisen: Apostle of the poor)*, “SKOK – magazyn spółdzielczych kas oszczędnościowo-kredytowych”, No. 3/15, 1995, p. 5.

³ There can be also met such term as “banking co-operative system.”

characterised by its own original solutions and specific characteristics⁴. The fact that the movement was formed at the time Polish territories were occupied by foreign powers accounted for its national and patriotic features. At that time co-operative organisations represented the main form of struggle for the Polish identity and preservation of the Polish state of possession. Co-operative ideas were propagated, among other persons, by F. Stefczyk. It was on his initiative that the first savings and loans co-operative on the Polish territories called „Savings and Loans Company” was set up at Czernichow near Cracow in 1890. The activity of these companies was not restricted only to taking deposits and granting loans, as they were involved actively in social and economic processes taking place in rural areas. They collaborated closely with different types of agricultural co-operatives, financed joint purchases of products for agricultural production, supported construction of housing districts, schools and so on.

The dynamic development of the loan co-operative system was interrupted by the First World War. During the war the property of many co-operatives was destroyed or plundered, and many of them were closed down. After the regaining of independence the co-operative movement had to solve many difficult economic and social problems. The operation of co-operatives was hindered by conditions prevailing in Poland at that time and namely: low and unequal economic potential, inflation, unemployment, overpopulation of villages and complicated political situation.

Despite these difficulties the number of small loan institutions in Poland reached 3,500. They had about 1.5 million members⁵. They played an invaluable role in developing the sector of services and small entrepreneurship in reborn Poland. It also became necessary to carry out some reforms in the co-operative banking system. The first attempt made to standardise the system was the Act of Co-operatives, which was passed by the Polish Parliament on 29th October 1920. The reform carried out by Treasury Minister Grabski in 1920 introduced the Polish currency: zloty replacing the mark. The Polish zloty strengthened the Polish co-operative system. An expanded network of baking co-operatives appeared at that time, but they had to depart from the financial self-sufficiency principle and seek credits in public banks. Consequently, their operation was dependent upon requirements posed by their creditors. Large organisations grouping certain co-operative unions were established in 1924. They included the Union of Co-operative Societies in Poland and the Union of Agricultural

⁴ H. Cyganik, J. Skrobot, *100 lat Krakowskiego Banku Spółdzielczego (100 years of the Cracow Co-operative Bank)*, Oficyna Wydawnicza ABRYS, Cracow 1999, p. 19.

⁵ *Blizsza kasa niz bank*, op.cit.

Co-operatives Associations⁶. In the years 1918–1939 co-operatives were divided into the Union of Consumers Co-operatives „Spolem” and the Union of Agricultural and Commercial Co-operatives. During the war occupation the output of the co-operative banking system, just as the entire economy, was largely devastated.

The union co-operatives were merged with the Inspection Department of „Spolem” at the Co-operative Congress in Lublin in 1944, with the inter-war traditions of the co-operative movement being preserved. The merger led to the establishment of the Central Society of Agricultural Companies and the Co-operative Bank „Spolem”⁷. The first years after the liberation were a very difficult period not only for the co-operative banking system. In 1946 there operated 962 savings and loans co-operatives and their number increased to 1,327 in 1949. The Co-operative Bank „Spolem” operated in the form of a loan co-operative with limited liability and it performed functions of the central co-operative bank for co-operatives operating in that city. The Central Society of Agricultural Co-operatives performed functions of the central financial co-operative institution for different forms of co-operatives operating in rural areas. Major changes took place in the banking and loan system between 1948 and 1949, which affected the activity of financial co-operative units. The changes, which were started with the bank reform decree of 25th October 1948, including liquidation of the Co-operative Farming Bank and the Economic Union of Co-operatives „Spolem”, establishment of eight co-operative central institutions of community-sector character and the Central Co-operative Association, as well as introduction of an obligation saying that each bank should belong to one of eight central institutions. These changes aimed at incorporating the co-operative system effectively in the centrally planned economy system, which resulted, however, in a lower autonomy and self-government of co-operatives and restricted an influence, which could be exerted on the management of a co-operative by its members.

Further changes in the co-operative banking system took place in 1956 and, in particular, in its economic and social activity. They consisted in restoring certain forms of co-operative democracy and autonomy. In accordance with the new system of national economy management, there was expanded autonomy and responsibility of co-operatives. A possibility was also created for co-operatives to provide loans for their members from their own funds. A very important role was played in that period by the Co-operative Committee appointed by the Board of Supreme Co-operative Council on 25th June 1956.

⁶ T. Wyszomirski, *Wczoraj, dziś i jutro spółdzielczości bankowej w Polsce (The past and the present of the co-operative banking system in Poland)*, Warsaw 1986, p. 14.

⁷ Ibidem, p. 23.

A more dynamic development of the co-operative banking system started from that time.

A structural crisis of the socialist system in the seventies led to the introduction of different reforms aimed at improving the performance of economy. One was then setting up Bank Gospodarki Żywnościowej – BGZ (Food Economy Bank) replacing the Central Association of Savings and Loans Co-operatives and Bank Rolny (Agricultural Bank). BGZ took over financial and credit services for the Polish agriculture, forestry, agricultural-food industries, agricultural companies and associations. All savings and loans institutions were renamed co-operative banks, which were sole providers of loans for private farms, private housing construction in rural areas and small crafts along monopolist principles. The eighties were a period of animated discussions and intensifying conflicts, which did not omit the co-operative milieu including the co-operative banking system. The Second National Congress of Co-operative Banking Delegates in 1981 passed a resolution about preserving an integrated co-operative banking system based on BGZ, maintenance and development of banking services in accordance with co-operative management principles⁸.

It was accompanied by a parallel work on the Act about Banking Law. Passing the new banking law by the Parliament was preceded by implementation the banking law act of 1975 passed by the Parliament in 1981⁹. The new Act about Banking Law was adopted on 26th February 1982¹⁰. The new statutes of a co-operative bank were worked out on the basis of this act and resolutions passed by the Second National Congress. On the basis of the statutes co-operative banks designed their own statutes adopted at general meetings in the first half of 1982. It took a longer time to adopt the statutes of BGZ. They were not adopted until the Third National Congress of Co-operative Banking Delegates, which was held between 24th and 26th June 1984. BGZ operated as a banking company, and it was simultaneously a central financial, organisational and auditing institution for co-operative banks grouped in it.

⁸ J. Ozdowski (ed.), *Spółdzielczość bankowa (Co-operative banking system)*, Warsaw 1990, p. 109

⁹ Official Gazette of 1981, No. 17, item 193.

¹⁰ Official Gazette of 1982, No. 7, item 56.

2. The period of transformations in the co-operative banking system in market economy direction

Deregulation of the co-operative loans system took place in 1989 (Act about Banking Law of 31st January 1989), when co-operative banks became universal banks. However, they were not prepared for their new role, made numerous mistakes and were unable to fulfil requirements of NBP (National Bank of Poland) and banking supervision in the field of necessary capital, solvency index or obligatory reserves. Therefore, it became necessary to restructure the co-operative loan system. The new act of law passed on 20th January 1990 „About changes in organisation and activities of the co-operative system,” among other things:

- introduced a three-tier structure of the co-operative loan system (co-operative banks, regional banks, Bank Gospodarki Zywnosciowej – BGZ);
- reduced the range of services offered by these banks and areas, in which they operate;
- introduced solutions guaranteeing solvency and liquidity of co-operative banks;
- defined sources of financing losses incurred by this sector;
- decided that co-operative banks should be passing a part of their funds to regional banks free of charge as well as a part of their deposits;
- stated that all banks grouped in a regional bank are responsible jointly for a bank risk and liquidity.

The reforms carried out in the early 1990s afforded an opportunity for co-operative banks to operate in an unrestrained way. The vast majority of them were small banks without branches. They appeared to be insufficiently prepared to operate in conditions of a market economy and they entered the period of economic transformations as entities suffering from a shortage of capital. Their situation was due, among other things, to weaknesses deriving from the past and primarily constraints created for co-operatives in the period of central directives and allocations, which resulted in severing economic ties between the interests of their members and activity of banks. Another determinant inherited from the past was lack of interest in raising a bank's capital¹¹. Precaution regulations issued in 1990 concerning, among other things, principles and procedures of bank activity connected with granting loans, were to enable co-operative banks to upgrade their

¹¹ W. Leksińska, *Konsolidacja banków spółdzielczych w ramach zrzeszenia regionalnego* (Consolidation of co-operative banks with their regional association) Prawo Bankowe 1998, No. 1, p. 97.

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management methods, choose their operation model and their own development strategy. Co-operative banks needed in that period such legal solutions, which would produce long-term financial effects linked with a market economy mechanism ensuring their autonomy and financial safety.

However, the beginning of reforms was not favourable for the co-operative sector. A difficult economic situation of farmers, loss of solvency by many newly-established economic units credited by co-operative banks were the main causes of a crisis in many co-operative institutions. Economic and financial situation of a big part of co-operatives deteriorated and many of them had to restrict their activities or were even closed down. Financial standing of most co-operative banks being dependent directly upon agricultural resources and material resources of rural population worsened.

The situation was due, among other things, to shortcomings and errors in banks themselves. Namely, gaining a considerable autonomy they were deprived simultaneously of control, which with a frequent underestimation of a supervisory role played by a bank self-government and lack of adaptation of management to new conditions created by a market economy resulted in disturbances in a safe operating of banks. The fiscal policy pursued by the State in the years 1990–1991 was also unfavourable for co-operative banks. Namely, alongside a high income tax co-operative banks have to pay taxes on incomes receivable but not received, that is, the interest on irregular credit receivables. Negative effects were produced also by the fact that most target reserves for bad debts could not be included in costs of incomes. Consequently, hundreds of co-operative banks found themselves in a dramatic financial situation.

It became necessary to commence the process of restructuring. Bad quality of assets possessed by co-operative banks, big losses, low own funds and also receivables difficult to collect posed a threat for deposits in co-operative banks. All these factors pointed out that without a comprehensive reform of the co-operative banks sector including raising additional capital by them it would be impossible to overcome the critical situation. One of the first steps aimed at changing this situation was an amendment to the Banking Law (of 20th September 1991) oriented at increasing economic security of banks including co-operative banks. In September 1992 all Polish co-operative banks not possessing their own capital amounting to minimum 5 million ECU (about 70 billion of the then zloty) were bound to associate in one of banks grouping co-operative banks (BGZ, Wielkopolski Bank Gospodarczy S.A. in Poznan, Bank Unii Gospodarczej in Warsaw, Gospodarczy Bank Południowo-Zachodni in Wrocław)¹². These banks

¹² T. Tokarzewski, *Polskie Banki Spółdzielcze (Polish co-operative banks)*, Warsaw 1996, pp. 66–67.

recording big incomes did not have a regional character and they grouped co-operative banks from different parts of Poland. These were most frequently banks which did not have the best experience derived from co-operation with BGZ. Simultaneously, organisers of these associations benefited from financial assistance in the form of capital subventions. These subventions increased their own funds, that is, shares proposed by shareholders – co-operative banks. It created better conditions for their operation in the financial-credit market.

Alongside co-operative banks it became also possible to revive the already mentioned savings and loans societies. This task was delegated to the Foundation for Polish Credit Unions. A possibility of establishing credit unions operating in the form of co-operatives and realising the idea of co-operative mutual financial assistance appeared in Poland when the Act about Professional Associations came in force on 23rd May 1991¹³. The act created a possibility of establishing co-operative savings and loans societies operating solely within work establishments. These changes led to establishing the first co-operative savings and loans society by the staff of „Gdansk” Thermal Power Station on 31st August 1992.

3. Restructuring paths of the co-operative banking system in the years 1994-2002

A historical event in the latest history of the co-operative banking system was the Act about Restructuring of Co-operative Banks and Bank Gospodarki Zywnosciowej – BGZ and of Bank Guarantee Fund passed by the Polish Parliament on 24th June 1994¹⁴. The act in question created a new legal situation for the sector of co-operative banks in Poland outlining indispensable organisational changes, which had to be carried out in order to build a new three-tier structure of the co-operative banking system. In accordance with this act, this structure was to be based on independent co-operative banks preserving far-reaching autonomy, regional banks and the national bank. The act deprived BGZ of its central co-operative bank function and its right to control the whole sector. Co-operative banks became independent but most of them were not prepared as regards their capital or personnel to operate within the reformed economy. There

¹³ Trade Union Act of 23rd May 1991, Official Gazette No. 55, item 234 and Official Gazette of 1994, No. 43, item 163.

¹⁴ Act about Restructuring of Co-operative Banks and BGZ and of Changing Some Other Acts adopted on 24th June 1994; Official Gazette of 13th July 1994 along with amendments; Law Gazette, No. 95.142.704; Law Gazette, No. 96.106.496; Law Gazette, No. 97.121.770; Warsaw, 13th July 1994, No. 80, item 369.

was started a process of setting up independent regional banks, in which co-operative banks were to be associated. The latter despite their autonomy did not have sufficient rights to conduct such activity, which hampered their development and did not permit to choose a model of operation and own strategy connected with planning long-term financial effects compatible with the development mechanism of a market economy and financial security. Restrictions concerned, for instance, provision of banking services exclusively within a given administrative commune, in which a co-operative bank had its seat. They were deprived of a possibility of performing certain banking operations admitted by the Banking Law. The legal restrictions concerned, for example, an obligation of consulting a regional bank when appointing a president of a co-operative bank by the supervisory board. The law in question created additional legal frames restricting operations of co-operative banks, which finds reflection in imposing an obligation of being associated in regional banks on co-operative banks. This obligation results from scarcity of capital in almost all co-operative banks and, in particular, from their inability to raise the basic capital required by a decree passed by the president of Narodowy Bank Polski by an individual bank.

The law came in force on 13th August 1994. It divided co-operative banks into two groups: privileged banks and non-privileged banks. The main goal of this law was to establish the first co-operative bank holding in Poland. It was the law-maker's intention that this holding would create a safe, strong and uniform banking structure able to render a full range of banking services mainly for Polish villages and economic and administrative entities providing services for villages but operating also in other sectors of the national economy. As an internally consolidated banking organisation with national coverage, the co-operative banking holding was to become a sufficiently strong and efficient organisation able to operate in a market economy in conditions of domestic and foreign competition and, in particular, in competition with banking and financial organisations within the European structure and in conditions of progressive integration of the Polish economy with the European Union's economy. The implementation of these plans started simultaneously the privatisation process of BGZ as a long-term objective. Long years of work on amendment of „Co-operative Law” were finished on 7th July 1994 with passing the Act about Banking Law Change and some other acts. It was prompted by the necessity of creating and upgrading conditions for development of co-operative banks and services provided for their clients particularly from rural areas, participation of co-operative banks in the process of restructuring agriculture through services provided for structural and regional projects implemented by means of funds obtained from the EU. Co-operative banks, which had been traditionally providing their services for entities linked with the food economy needed technical and organisational support necessary for structural transformations in agriculture and multifunctional

development of rural areas being not only of economic but also of social importance. Co-operative banks sought such support in regional banks operating in the form of joint stock companies, whose shareholders were just co-operative banks. The support concerned, among other things, the restructuring of bad debt by means of treasury bonds, provision of financial means for ensuring their liquidity, effective management of funds left at their disposal, organisation of training for bank staff. Regional banks were, however, frequently preoccupied with building their own potential basing it simultaneously on co-operative banks. There could be frequently perceived divergent interests concerning allocation of funds, which co-operative banks were bound to deposit in regional banks.

Effects of the restructuring law were more and more visible in 1995 in the form of unequal treatment of co-operative banks. The number of these banks in Poland decreased as a result of bankruptcies and mergers. An intensive work on changes in the Act about Banking Guarantee Fund and the New Banking Law was carried in 1996 and at the beginning of 1997. Since 1st January 1998 there has been in force the Act about Banking Law of 29th August 1997 harmonising the Polish banking system with that in the EU countries¹⁵.

On 5th August 1998 the Banking Supervision Committee passed a resolution pertaining to principles of equipping co-operative banks with equity capital,¹⁶ which could not be lower than the equivalent of 300,000 ECU. In practice it meant that co-operative banks had to increase their own capital to this level. In May 1999 all regional banks, BGZ and certain co-operative banks received a draft of the Act about Operation of Co-operative Banks and Association of Associating Banks and about amendment of some other acts. The submitted government project of the act regulating the operation of co-operative banks was received negatively by associating banks and co-operative banks. A critical attitude of co-operative banks resulted from the content of the act, which changed fundamentally the organisation of Polish banking co-operatives. The draft of this act proposed capital thresholds: 300,000 euro till 2000, 500,000 euro till 2002 and 1 million euro till 2004. For many banks these thresholds were and are impossible to accept. Passing the next Act about Operation of Co-operative Banks changed the level of minimal thresholds¹⁷. The law came in force on 28th January 2001.

¹⁵ Law Gazette of 21st November 1997, No. 140, item 939.

¹⁶ Law Gazette, NBP No. 19, item 44.

¹⁷ A co-operative bank, which has associated itself with an associating bank is bound to increase its own capital to the level not lower than: 1) an equivalent of 300,000 euro – till 31st December 2001; 2) an equivalent of 500,000 euro - till 31st December 2005; 3) an equivalent of 1,000,000 euro – till 31st December 2010; Act about Operation of Co-operative Banks, Their Association and Associating Banks of 7th December 2000, Law Gazette No. 119, item 1252, Warsaw, 28th December 2000.

Considering the accepted capital thresholds the law affects, to a different degree, strong and weak banks both with regard to their capital and market share. The new regulation of geographical coverage of a co-operative bank was in compliance with postulates advanced by a big part of members of co-operative banks. In accordance with Article 5 #1 of the law „a co-operative bank operates within an administrative district, in which its seat is located and in administrative districts, in which its branches performing banking services are located on the day the law comes in force”. Moreover, in accordance with Article 5 #2 „a co-operative bank with approval of an associating bank, with which it has concluded an agreement on association, can carry operations also in neighbouring administrative districts as specified in # 1”, and with approval of the Banking Supervision Committee also in other districts. By way of comparison it is worth adding that the Act of 24th June 1994 states that „A co-operative bank carries its activity in an administrative commune, in which its seat is located and with approval of a regional banks also in a given region or its part”¹⁸. A comparison of these two regulations reveals significant changes. Firstly, we are dealing with a common regulation covering all co-operative banks (excluding those whose funds exceed the equivalent of 5 million euro). Secondly, the law does not make any distinction between banks with regard to their membership in definite associating banks. Thirdly, the main area, in which co-operative banks operate, is widened considerably (an administrative commune was replaced with an administrative district depending on branches located there). Fourthly, a co-operative bank can carry its activity on the whole territory of Poland provided it has an approval of the Banking Supervision Committee. Fifthly and finally, when co-operative banks operating in different areas merge, the area of a taking-over bank is enlarged automatically by the area of a taken-over bank on the date of a merger. The regulation in question changes considerably the situation of many co-operative banks from the viewpoint of their market. Geographical distribution of banks shows that up to six co-operative banks compete with one another in particular administrative districts having their seats or branches there. In connection with costs involved by consolidation processes of co-operative banks and these are costs forced out, to a much bigger extent, by external regulations than objective needs of the market, the analysed law introduced a new solution. First of all, there is established the restructuring fund of co-operative banks within the Bank Guarantee Fund as a target fund. The act of 2000 creates a one-time source of financing the restructuring fund of co-operative banks and imposes a qualitatively new and quantitatively expanded function of the Bank Guarantee Fund (BGF). BGF within limits of its financial means and for purposes described above in

¹⁸ Act about Restructuring of 24th June 1994..., op. cit.

accordance with Article 35 #1 „...can provide for co-operative banks, in which the risk of insolvency does not exist, a refundable financial assistance on more favourable terms than general terms applied for co-operative banks”¹⁹. Such assistance can be provided when the situation of a co-operative bank does not carry a threat for repayment of a loan and, moreover, such bank has to provide an appropriate collateral. Powers to fix forms, procedures and detailed conditions of providing assistance are passed by the act in question to the BGF’s Council.

The quoted regulation along with other fragments of Articles 35 and 36 of the law seem to indicate that the terms of granting a loan from the restructuring fund, that is, at least the interest and the commission should be more favourable than in the case of other forms of financial assistance provided for co-operative banks by BGF. In a systemic approach it would be less justified to extend the period of using such assistance beyond the previous limit of 10 years or also a grace period exceeding a half of the period for which a loan has been given.

The law in question contains in Article 2 #2 a catalogue of associating banks including 12 entities (9 regional banks, 2 associating banks and BGZ S.A.), and it creates simultaneously a possibility for these banks to merge. However, maintaining the status of an associating bank has two conditions. Firstly, there is a requirement that at least one co-operative bank should be associated and, secondly, an associating bank has an obligation of possessing its own capital at the level of minimum 20 million euro (temporarily 10 million euro during the first six months from the act’s entry in force, an equivalent of 15 million euro till 31st December 2003 and 20 million euro till 31st December 2006). In fact, the requirement concerning the minimum capital for associating banks is a determinant of their number. In turn, taking into account the function performed by an associating bank, an estimate of the number of co-operative banks during the target period appears to be of big importance (for instance, till 2006 or 2010). Relevant estimates for own capital of co-operative banks allow to estimate the number of these banks at about 300, and with more favourable financial results in the coming years at 350 to 380 banks. It corresponds, anyway, to the number of administrative districts and their capital towns in Poland. Taking into account trends in bank technologies and costs of their operation, the number of associating banks for 300–380 co-operative banks is definitely too big considering functions attributed to them.

Analysing statutory tasks of an associating bank contained in Article 19 of the law in question, it is possible to formulate a conclusion that it is primarily

¹⁹ Act about Operation of Banks of 7th December 2000 ..., op.cit.

a link facilitating performance of its regulatory functions in relation to co-operative banks: it runs current accounts of associated co-operative banks, on which their obligatory reserves are kept; it calculates and keeps the reserves of associated co-operative banks on its account with NBP; it runs a separate account, on which assets of associated co-operative banks are deposited constituting a cover of the protection fund of guaranteed financial means; it carries out information duties in the name of associated co-operative banks towards NBP and BGF; it monitors compliance of associated co-operative banks with provisions of the association agreement, laws and statutes, and in justified cases it can request the Bank Supervision Committee to apply disciplining or repressive measures. The law-maker envisaged also for an associating bank a function of a representative of associated co-operative banks in external relations in the case of issues resulting from the association agreement and performance of other functions stipulated in the agreement.

The described functions show that the statutory capital threshold being an equivalent of 20 million euro is not linked with them in any way. If the policy adopted by the Bank Supervision Committee in the field of approving draft association agreements does not include any regulations connected with liability of an associating bank for possible financial losses of an associated bank (for example, resulting from carrying its activities in administrative districts neighbouring with districts, in which the seat of a co-operative bank or its branch is located, or also an approval for activities specified in Article 6 # 1 and 3–7 of the law), then the capital threshold in question does not find any justification apart from reducing the number of associating banks. Co-operative banks themselves face, on the other hand, dilemmas connected with their membership in a definite associating bank.

4. Prospects of the co-operative banking system

The co-operative banking system and problems connected with it concern not only the milieu of co-operative banks but also the rural milieu, in which these banks operate. This milieu and, thus, farmers, local communities and the commune authority appear to be linked with existence of the co-operative banking system. Attempts should be made to develop this milieu remembering about the target model of the Polish co-operative banking system and about the relationship between an associating bank and co-operative banks. The western model, which tries to preserve and strengthen the co-operative idea, shows that an associating bank is a service bank in relation to co-operative

banks, which are owners of this bank, and this is a condition for an agreement of interests of both sides and absence of conflicts.

Consolidation processes being a natural economic process should improve and next strengthen the position held by the co-operative banking sector. Such consolidation will also pave the way for capital reinforcement of co-operative banks. It should be noted, however, that this reinforcement does not have to mean that statutory capital thresholds will be met – too excessive taking into account the present situation and position held by co-operative banks – by associating banks supplementing own capital in co-operative and commercial banks. Consequently, it implies the liquidation of many co-operative banks and allows to question the whole formula of the co-operative banking system playing a significant role in solving the country's important and complex economic problems. It concerns job creation in less developed countries and especially in areas affected by unemployment. Forms of activity with preserving legal principles and economic rules have to be adjusted fully to needs and possibilities of a given community and farmers. The most important condition of activity is a clear specification of goals accomplished by co-operative banks. It is worth stressing once again the importance of co-operative principles, that is, catering for interests of associated members, mutual assistance, responsibility, equality, justice, reliability in activities, maintenance and development of democratic principles governing membership. These are permanent values and founders of the co-operative banking system attributed a fundamental importance to them. The co-operative banking system in Poland has a history of over 140 years. These banks are characterised by tradition and modernity and their main goal such is a new economic order and their adaptation to rules of a market economy and needs of the community. The co-operative banking system providing services for family farms and adjusts market rules to needs and capabilities of these farms. Co-operative banks operate as a durable element of the banking system along theoretically uniform principles binding all banks in Poland. Co-operatives follow not only the banking law and provisions of the co-operative law. An important feature of the co-operative movement is a broad co-participation of representatives of the community for which they provide services in assessing performance of budgetary entities and outlining development directions. Co-operative banks enjoy confidence of their clients and this strengthens ties between those providing services and their addressees. Today decisions are made through the economic policy oriented at rural areas and agriculture connected with it, which aim at development of various forms and types of economic activity serving liquidation of unemployment among agricultural population and improvement of living conditions. An important role in an economic area is played by services oriented at tourism and recreation. Changes occurring in the Polish agriculture should go in such directions as:

enlargement of farms, intensification of agricultural production, specialisation, economic growth, modernisation of techniques and technologies, development and modernisation of technical infrastructure in villages, and development of non-agricultural economic activity aimed at elimination of unemployment.

Co-operative banks cater for needs of every farm in the field of preferential credits. Tourism in rural areas is promoted by many farmers, which is accompanied by a growing interest in production of healthy food. These forms should be supported by credits to accelerate development of economic activity. The co-operative banking system with its services is situated closest to present and potential clients dealing with environment friendly activity in regions removed from main economic centres and the country's administration. Co-operation between Management Boards and Councils of Regional Environment Protection Funds and a regional banking organisation can result in launching joint projects in the field of environment protection, which can be beneficial for co-operative banks.

An important service in adaptation of co-operative banks to changing conditions of their environment can be counselling services for clients being the main element of banking marketing. Counselling banking services can be treated as a separate service provided irrespective of the fact whether a client uses other products of a bank or it can be combined with other products, for instance, a loan or a capital investment. The growing range of banking services and complex conditions, in which services are provided, cause that counselling can become a decisive factor, which induces clients to make use of a banking service.

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