

## Some Selected Legal Aspects of the Activity Rules in Relation to the Financial Agent's Clients

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### Abstract

*The activities of financial agents deserve our attention as we can currently observe their growing share on the intermediation of financial services. The quantity of products and services offered by financial market segments requires a continuous education and the monitoring of the current legislation. Financial agents help their clients to find a financial product, which fulfills their specific needs. The client's decision depends on the extent of the information a financial agent provides to him. The legislator imposes an obligation to act when performing financial intermediation in compliance with the principles of fair business relations, with professional care and in the interest of rights and legitimate interests of a client. However, the legislation does not define these terms. This paper aims to outline and analyze procedures in order to perform financial intermediation in accordance with regulatory requirements.*

### Key words

*financial agent, professional care, fair business conduct, acting in accordance with the rights and legitimate interests of the client*

**JEL Classification:** K20, K23

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### Introduction

The recent development shows how financial intermediation gain its position on the financial market. This long journey began by unifying legislation regulating intermediation into a one legal frame. Prior to January 1, 2010, rules concerning the performance of financial intermediation were contained in several acts governing individual segments of the financial market, respectively had not been not regulated by rules of the financial law.

The different regulatory framework created unequal conditions for performing this business activity. In order to unify them, Act No. 186/2009 Coll. On Financial Intermediation and Financial Advisory and on amendments and supplements to certain laws, as amended (hereinafter only „Financial Intermediation Act”) has been adopted.

The contract for the provision of a financial service which is being defined by the Financial Intermediation Act means not only rights, but also obligations for the client. Many see the signing of this contract as something final, but it is only the beginning (Adam, 2008). Whether it is a sector of insurance and reinsurance, supplementary pension savings scheme, or old age pension savings, the spirit of the legislation in force

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calls for financial agents to recognize the high degree of responsibility that this kind of business brings. The scope of the information provided by the financial agent is crucial to clients when deciding on a particular product.

## **1 Methodology**

The paper is focusing on the analysis of selected concepts, namely financial intermediation and its performance in the interest of the client's rights and legitimate interests, with professional care and in accordance with the principles of fair business conduct. As there are no legal definitions of these terms in the current legislation, we have found the content of the concepts in question, in particular, by analogous application of the legal norms of commercial law, as well as in the context of legal theory and science. The goal is to provide an analysis how the terms in question can be interpreted.

## **2 Results and discussion**

The Financial Intermediation Act contains in its fourth part the activity rules in relation to clients<sup>2</sup>, establishing an obligation to pursue financial intermediation in the interests of the rights of the client, with professional care and in accordance with the principles of fair business conduct. The mentioned terms are not defined by the legislator in the Financial Intermediation Act. It is necessary to analyze the rules of financial law in connection with other rules from different legal sectors.

### **2.1 Acting in accordance with the rights and legitimate interests of the client**

In order to understand the rights and legitimate interests of the client, it is necessary to examine the needs of the subject. Whether from the point of view of a corporate entity, in the case when the client is a legal person or to examine situations in the life of a natural person. It is desirable to distinguish between needs and wishes. Needs and wishes supplement each other (Schmidt, 2011). For most clients, the need is to name the risk they want to cover (Schmidt, 2011).

Performing financial intermediation in the interest of the client's rights and legitimate interests requires a deep knowledge of the contract for the provision of a financial service. This is logically linked to the level of the legal awareness of a financial agent, who should ideally have an university degree in law. However, the legislator does not have the ambition to reserve this kind of business for lawyers. On the contrary, the regulation allows persons with secondary education /when sufficient practice on the financial market has been proved/ to work on the market. Everyone has access to this

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<sup>2</sup> Article 28 - 37a Financial Intermediation Act.

type of business after the legal conditions have been met. This legislation can be considered as in accordance with Article 35 of the Constitution of the Slovak Republic, conferring the right to free choice of profession, the right to prepare for freely chosen professions, the right to conduct business and the right to perform other gainful activity. This in connection with Article 51 par. (1) of the Constitution of the Slovak Republic, meaning these rights can only be called for within the limits of the laws which are in force (Drgonec, 2007).

Due to the relevance of the right to conduct business and to carry out other gainful activity, the Constitutional Court of the Slovak Republic paid repeatedly attention to this topic in its findings. In its finding from 16 June, 1998, it states the following: „The basis of the market economy and competition that is connected with it, is the freedom of market entry and equality of conduct on the market for all competitors. The market entry is part of the constitutionally guaranteed right to enter into business and carry out other gainful activities, since in the market economy it is essential to exercise the right under Article 35 par. (1)....“.<sup>3</sup>

The Financial Intermediation Act has defined requirements concerning the level of knowledge of financial agents. It is a combination of the following factors - institutional education, practice on the financial market, successful passing of the professional examination and special financial education. These must be met in a cumulative way. This is ensuring a proper standard of protection of the rights and legitimate interests of the client.

Through the legal institute of professional competence and special financial education as one of its components, an „image of the profession“ of a financial agent is being created. A client meeting with a person in the financial services industry, should know clearly what qualifications and other requirements this person has met (Seegmüller, 2008). Broadening awareness about this type of business, clients when meeting a financial agent should associate the idea that the competence of these persons has been verified, inter alia, through a professional examination.

The verification of professional competence is required periodically, every four years.<sup>4</sup> Since financial intermediation means in practice "working for people and with people" we also perceive the subjective factor - the honor, the conscience and the willingness of the individual to do the maximum for clients.

A certain standard in this area is being ensured by ethical codes that are accepted by either financial agents individually or issued at the level of associations. An ethical code is a set of rules that embodies ways of correct behavior and exposure to clients, as well as to competitors on the market. It can be simply called a "fair play" document. In summary, we consider that the performance of financial intermediation in the interests of rights and legitimate interests is the process by which a financial agent fully, correctly, truthfully and professionally informs the client of the nature of the financial service. The financial agent should not only inform about the advantages, but also about the disadvantages.

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<sup>3</sup> II. ÚS 70/97. Finding 16 June, 1998. Collection of Findings and Rulings of the Constitutional Court of the Slovak Republic 1998, p. 328.

<sup>4</sup> Article 22 par. (2) Financial Intermediation Act.

## 2.2 Acting with Professional Care

Financial intermediation is a business activity. This fact must be considered, when interpreting the term professional care. This cannot be perceived only from the perspective of the Financial Intermediation Act. This term must be seen in the context of further legal norms regulating the business environment. A set of such standards undoubtedly represents Act No. 513/1991 Coll. Commercial Code, as amended (hereinafter only „Commercial Code“). The Commercial Code uses the term professional care in the second ("partnership, companies and the cooperative") and in the third part (the "commercial obligations"). In the second part it is used to impose obligations on selected bodies of capital companies and cooperatives. In the third part this term is being used in relation with the different types of contracts, especially when speaking about the rights and obligations arising from them. We will pay attention to the second part of the Commercial Code. In its enumeration, the legislator defines the obligations that must be met in order to fulfill the requirements of profession care by the statutory bodies of capital companies.

The executive director of a limited liability company is obliged to exercise competences with professional care and in accordance with the interests of the company and all its associates.<sup>5</sup> It is, therefore, an objective aspect requiring that the executive director takes into account all objectively possible and available information relating to the subject matter of the decision (Patakyová et al., 2016). Other areas that constitute the content of professional care can be summarized as the duty of confidentiality regarding confidential information and an obligation to act in the company's interest, meaning not to favor own interests, interests of selected partners or third parties.

Members of the board of directors of a joint stock company are required to exercise their functions, among other things, with due diligence.<sup>6</sup> The term due diligence is broader than professional care. Including loyalty to the joint stock company and its shareholders, as well as professional care (Patakyová et al., 2010). Due diligence can be defined as decision-making with knowledge of a subject in the business's object, which can be considered as sufficient in the objective sense (Patakyová et al., 2010). The professional competence framework includes the obligation to maintain confidentiality about confidential information (Patakyová et al., 2010). A member of the board of directors of a joint stock company cannot conduct in a way that causes damage that may result in damage or threat to the interests of the company or shareholders (Patakyová et al., 2010).

If a financial agent wants to perform financial intermediation with professional care, the Commercial Code's rules should be applied by analogy and the requirements laid down by the legislator for the activity rules in relations to clients should be met.

When applying the rules of the Commercial Code by analogy, a subject is acting with professional care during the financial intermediation (as the regulation of the Financial Intermediation Act requires),

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<sup>5</sup> Article 135a par. (1) Commercial Code.

<sup>6</sup> Article 194 par. (5) Commercial Code.

- when the financial agent is being fully informed - about the contract for the provision of a financial service, about the subject matter of the financial institution, so that the client's attention can be drawn to any imbalance in the contract,

- when the financial agent maintains confidentiality about sensitive data - it is clear from the nature of financial intermediation, that the business is linked with access to sensitive data at the stage of analyzing the client's needs for the purpose of identifying a suitable financial product, such as data on the wage of the client, the income of members of his household, family budget, preferences for leisure activities. If the client is a legal person the financial agent gains information about the turnover, profit, or loss. Based on this, confidentiality appears to be a necessity and one of the essential prerequisites. The duty to maintain confidentiality also includes the protection of personal data. This implies that in case of natural persons it is necessary to perceive regulation resulting from Act No. 122/2013 Coll. On the Protection of Personal Data and on Amendments to Certain Acts, as amended by Act No. 84/2014 Coll.

### 2.3 The principles of fair business conduct

The regulation imposes an obligation to conduct financial intermediation in accordance with the principles of fair business conduct. However, the legal framework does not further explain to the addressees of the regulation how to proceed in order to fulfill the principles of fair business conduct. It is therefore necessary, for the purpose of defining the content of the term in question, to seek for the answer in the legal environment of Slovakia and in theory. Again, our attention is paid to commercial law rules.

According to Article 265 of the Commercial Code, the exercise of a right which contradicts the principles of fair business conduct is not granted legal protection.

The basic principle of private law is prohibiting the abuse of rights, which is specified in the Article 265 of the Commercial Code (Ovečková, 2011). In summary, we can state that by incorporating the provision in question into the Commercial Code, the legislator follows the categories of morality and ethics, which must also be reflected in the area of business relations.

The principles of fair business conduct are a concept that substitutes accepted principles of morality for the needs of economic relations (Čečotová, 2005). The content of accepted principles of morality is broader than the principles of fair business conduct. Therefore every breach of the principles of fair business conduct is a breach of accepted principles of morality, but not every breach of accepted principles of morality is a breach of the principles of fair business conduct (Ovečková, 1993). These two terms are not synonyms. In practice, cases will occur when there will be an overlapping. Meaning the breach of the principles of fair business conduct will be a breach of accepted principles of morality. But it will be a matter of assessing an individual case. A general application of the definition of accepted principles of morality on the principles of fair business conduct can be considered as an inappropriate consolidation.

In the legal environment of financial intermediation, we conclude that the principles of fair business conduct are connected with professional ethics. Professional ethics represent a set of rules of conduct considered to be minimum standards of fairness. If

a financial agent exercises his rights in a way that is harming the interests of the client or in way that is abusing the clients' goodwill, it is a breach of the principles of fair business conduct. This is the so – called „bullying“, when the law is not exercised in order to pursue own economic interests which, but it is an attempt to exercise the right in a way to cause a disadvantage and harm to the other party (Ovečková, 2011). If a financial agent would exercise rights in this way, legal protection would not be granted. In the event of a dispute, the court would reject the right with reference to a violation of the principles of fair business conduct.

Despite the absence of a definition, we can say that the principles of fair business conduct fulfill a normative function (Hurdík, Lavický, 2010).

## 2.4 Some selected aspects of the regulation of advertising of financial intermediation

The regulation of advertising means a legal restriction on the freedom of expression that is necessary to protect rights of others. Advertising must be fair, true and prepared with a sense of responsibility (Jakab, 2010). The reason for public intervention in this area is to protect addresses of advertisements trying to sell products and services, often without regard to the truth of the information provided or other social value (Chaloupková, Holý, 2009).

A *lex generalis* in this area is being represented by the Act No. 147/2001 Coll. on advertising and on amendments and supplements to certain laws as amended (herein after „Act on Advertising“). The Act on Advertising will be applied only subsidiary, when the advertisement is realized through television and radio. In these cases the *lex specialis*, the Act No. 308/2000 Coll. on the broadcasting and retransmission and on the amendment of the Telecommunications Act No. 195/2000 Coll. as amended will be applied. For advertisement intended for broadcasting in cinemas, Act No. 40/2015 Coll. on audiovisual and on amendments to certain Acts will be applied.

The Act on Advertising contains a taxative enumeration of attributes that the ad can not contain.<sup>7</sup> It is logical and obvious that financial agents are looking for opportunities to promote their business, but they must not omit the specific requirements imposed by the legislator on these activities. Therefore, we believe that the Financial Intermediation Act is a *lex specialis* to the Act on Advertising, specifically supplementing the requirements for the content of advertising and promotion. If in practice a financial agent creates outputs containing a proposal to conclude a contract, as well as a form or other mechanism of responses, it is necessary to incorporate a range of data corresponding with the requirements set by the valid regulation required. Advertising and promotional information must also be consistent with other data that will be made available to the client in the future. In designing advertising campaigns and strategies, it is necessary to proceed in such a way that the result does not constitute an aggressive business practice, misleading behavior or deceptive omission or unfair competition. Financial agents as advertisers and promoters are required to comply with a set of legal norms arising from the legislative environment. However, we believe that these are a

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<sup>7</sup> Article 3 Act on Advertising.

regulatory "minimum", because we perceive the advertising issue in a wider context in which we also find it appropriate to adhere to moral and moral standards.

In the case of financial intermediation, the "path of success" begins with a market survey and client wishes. The results of the research, together with the assessment of the macro-environment and the micro-environment, form the basis for identifying market position, reviewing the mission, and setting goals, further elaborated on strategies that can be implemented through marketing tools (Medved', Tkáč et al., 2013).

## Conclusion

Financial agents form a connection between a financial institution and a client. They help their clients to get an orientation in a wide range of products and they also help to meet the needs of an individual. Their services are independent of those provided by financial institutions and are of particular importance.

We have paid attention to selected legal aspects of regulation of the activity rules in relation to financial agent's clients. We focused on the analysis of selected concepts, namely the performance of financial intermediation in the interest of the client's rights and legitimate interests, with professional care and in accordance with the principles of fair business conduct. As there are no legal definitions of these terms in the current legislation, we have found the content of the concepts in question, in particular, by analogous application of the legal norms of commercial law, as well as in the context of legal theory.

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