

Customary business practice regarding prolongation of the term of deposit contract



Article 14 (3) of the Republic of Armenia Law on Financial System Mediator establishes that in making a decision Mediator shall be based not only on the requirements of the Armenian legislation but also on the rules of business conduct and ethics, and customary business rules.

While reviewing a claim filed against one of the banks operating in Armenia, the Office of Mediator identified a customary business practice. The description of the claim was as follows: citizen A concluded a deposit contract in favor of the third party (citizen B). The contract did not contain any provisions specifying any prolongation of the term of the contract. The bank's operational rules on deposit service, which is an indispensable part to the deposit contract, specify that, unless otherwise provided for in the contract, after expiry of the term of the deposit contract the amount of deposit shall be transferred on to the current account of the depositor; and in case of a deposit in favor of the third party the amount of deposit shall be transferred on to an intermediate bank account opening in favor of that third party, provided that the third party had voiced intention to use the depositor rights before the expiry of the term of the contract. After the term of the deposit contract in favor of the third party expired, citizen B went to the bank to take out the money which was invested on his behalf. The bank however declined to give the money by reasoning that this person did not announce his intention to use his depositor rights before the expiry of the term of the contract. Taking this matter into consideration, Mediator attempted to clarify how banks are supposed to handle situations like this.

Article 446 (1) of the Civil Code provides that a contract shall be in favor of the third party whereby the signatories have established that the debtor must fulfill his obligation not in favor of the creditor but rather in favor of the third party, whether or not mentioned in the contract, who has the right to require the debtor to fulfill his obligation in favor of him. Article 905 (4) of the Civil Code provides the following: where the depositor does not claim his deposit amount back after the expiry of the term of the deposit contract or, where circumstances under the contract have occurred, does not claim a return of the deposit invested on other terms, that deposit contract shall be treated as

prolonged on terms of a demand deposit, unless otherwise specified. Further, Mediator requested banks to also provide their professional opinion on the following:

a) Does the above-described circumstance infer that the prolongation of the term of a deposit contract as provided for in Article 905 (4) of the Civil Code is imperative to the bank, while the parties are able to determine terms/conditions other than the terms typical to the demand deposit, OR whether the dispositive nature of the standard covers prolongation of the term of the contract as well (making the point that the contract may establish that its term is not subject to prolongation)?

b) Do the bank's obligations under the deposit contract (including the one concluded in favor of the third party) terminate upon the expiry of the term or upon the execution of the deposit contract?

It should be noted that opinion received from banks did not generate a customary business practice as few banks responded and, besides, they had many different approaches on the subject matter. In particular:

1. Part of the banks believed that the obligations of the bank under a deposit contract concluded in favor of the third party terminate upon the expiry of the term, rather than the execution, of the contract; and that the deposit contract may stipulate that the rights and obligations of the parties shall terminate upon the expiry of the term of the contract.

2. Others supported an argument as follows: when concluding a deposit contract in favor of the third party, the bank assumes two obligations to: i) have the interest accrued on the deposit amount, and ii) have the deposit amount and interest returned to the depositor. The bank's obligation to have the interest accrued will only terminate as the deposit contract concluded in favor of the third party expires, and the bank's obligation to have the deposit amount and interest returned to the depositor will only terminate upon the execution of the deposit contract, i.e. when the deposit amount and interest is returned to the depositor or the third party, whichever is the signatory to the deposit contract. Banks supporting this argument mentioned that, once expired, the deposit contract would imperatively be treated the one with its term having been prolonged. However the parties would be able to determine terms/conditions other than specified in the deposit contract.