# Peter Thiel bets on European deposit protection

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Cast your mind back to October 2008. The global financial crisis was upon us. The sky was falling. The end was near. And the Icelandic bank Landsbanki had just gone bankrupt.

That was a problem for Iceland, but also for hundreds of thousands of retail depositors in the UK and the Netherlands who had invested in savings products offered under Landsbanki's Icesave brand.

Who was going to compensate those people? The answer from the people of Iceland was 'lol, no, not us'. The UK and the Netherlands ended up footing the bill, which they promptly sent back to Iceland (who eventually paid after much legal wrangling).

Now take a look at Deposit Solutions, a Berlin-based fintech company backed by Peter Thiel.

This week it raised another €15m from the Trump-supporting billionaire and other investors at a reported €110 million valuation. What's the idea behind the four-year-old startup? Making it easier for banks to sell their customers savings products from other financial institutions across the European Union.

The proposition is worth examining in detail, not only because it is not the only startup doing this sort of thing — Raisin is another notable example — but also because it gets to the heart of a crucial debate about banking in Europe.

On the surface, Deposit Solutions offers a white-label system that lets a bank include offers from other banks on its online banking portal. With a few clicks, a person could move money from their existing bank into a savings account at another bank, which paid a higher rate.

The benefit for the third-party bank is attracting deposits without building a branch network or spending heavily on marketing, says Max von Bismarck, Deposit Solutions' chief business officer. Meanwhile, he adds, the original bank is able to siphon off excess deposits that might otherwise be parked with the European Central Bank, for example, which currently applies a negative rate on such money.

The customer gets a higher interest rate; the third-party bank gets deposit money relatively easily; and the original bank gets rid of deposits it may not want on its own balance sheet. Both Deposit Solutions and the original bank share a fee paid by the third-party bank, which is proportional to the volume of deposits that move.

So far, so simple. But things get more interesting when you look at the mechanics, as explained to us by von Bismarck.

In order to transfer deposits to the third-party bank, the original bank will pool customer orders and then make one single transfer at a time. At first sight, this would appear to be a problem for a third-party bank that wants to attract retail deposits that count towards its liquidity coverage ratio.

The Basel III regulations say that “unsecured wholesale funding provided by other legal entity customers” is discounted entirely when calculating liquidity coverage ratios.

However, von Bismarck says two features of Deposit Solution’s product mean that the funds have the “regulatory quality” of retail client liabilities (i.e. ordinary deposits). First, he says, “it’s still individual people making individual pay in or pay out decisions. At no point does a bank or anyone else have discretion.” And, second, the system allows the individual claims on the pool of money to be tracked and identified.

So far, this offering has attracted 15 financial institutions, including Deutsche Bank, who want to either increase or reduce the amount of deposits they have.

Deposit Solutions also runs its own website, Zinspilot, where it offers savings products directly to consumers in Germany. Zinspilot translates to “interest rate navigator” and operates using two correspondent banks rather than using its own banking license. Currently, Zinspilot offers products from banks in Austria, Malta and from Close Brothers in the UK. Next year, Deposit Solutions plans to open a similar website in the UK and since 2011, says von Bismarck, the business as a whole has “mediated” over €1bn of deposits.

But then you get to the politics. This isn’t just a product for moving deposits around within a country, this is also a product for moving money around the European Union, for letting savers find higher rates in countries other than their own.

One question is whether or not savers will properly assess the risks of banks in other countries. On Zinspilot, Deposit Solutions only offers products from countries that are rated A or above by ratings agencies. “That means we’ve excluded banks from Greece, Cyprus and Croatia,” says von Bismarck.

Another is whether or not countries will be willing or able to compensate depositors from other countries in the event of a crisis

Von Bismarck notes “it is a general principle of the European deposit protection regime that economic beneficiaries are covered, regardless of legal account holder and citizenship of the beneficial owner.” Indeed, there have been moves to strengthen that principle. In 2013, the EU agreed to institute greater uniformity in deposit protection schemes from country to country, following the experiences in Iceland and then Cyprus.

However, the issue is by no means settled and, as von Bismarck puts it, “the ultimate counterparty risk for the individual saver is the deposit insurance scheme of the given country”.

Indeed, some argue that without a common, pan-EU deposit protection scheme problems will persist. See this speech by Már Guðmundsson, governor of the central bank of Iceland, given in February 2015, and wonder if history might not repeat itself one day:

In order to reverse the ongoing run on domestic deposits, a declaration was made that all deposits in Iceland were safe and all deposits in Icelandic-headquartered banks were given priority over other unsecured claims. This distinction made between domestic deposits and foreign currency deposits in the banks’ foreign branches added fuel to the fire of the so-called Icesave dispute about the settlement of deposit guarantees in the Dutch and British branches of one of the banks. But guaranteeing those deposits would never have been credible and might have bankrupted the Government had it been attempted. The deposits in question were in foreign currencies and amounted to 11½ billion euros – far in excess of Iceland’s FX reserves, which amounted to 2½ billion euros. And the sovereign was completely closed off from foreign capital markets at that point. Furthermore, in economic terms, given that these deposits were used to a significant degree to finance illiquid assets in outside Iceland, such a payment, if it had been possible, would have amounted to a net transfer of resources from Iceland to other countries – where the United Kingdom would have been prominent – at a time when Iceland was going through its deepest financial and economic crisis in the post-war period! That made no sense.