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Loans in foreign currency

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Commercial analysis: Could the recent case of Hajnalka Káslerné Rábai v OTP Jelzálogbank Zrt before the EU Court of Justice lead to borrowers challenging foreign currency loans? Christophoros Christophi, managing partner of Christophi & Associates LLC, based in Cyprus, comments on the case.

Original news

Árpád Kásler, Hajnalka Káslerné Rábai v OTP Jelzálogbank Zrt: Case C-26/13

In May 2008, Mr Kásler and Mrs Káslerné Rábai took out a mortgage loan from a Hungarian bank in Hungarian forints. The equivalent value in Swiss francs was fixed at CHF 94,240.84. According to the terms of the contract, the loan, the related interest, the administration fees and default interest and other charges would be determined in CHF.

The contract further stipulated that the amount of the loan in CHF would be set at the buying rate for that currency, applied by the bank on the date that funds were advanced.

The couple challenged the terms which allowed the bank to calculate on the basis of the selling rate for CHF. They said that this clause is unfair as the loan is repaid using a different exchange rate from that used when it was set.

What was the outcome of this case?

The decision delimits the scope of art 4(2) of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts (the Directive). Article 4(2) of the Directive exempts terms defining the contract's main subject matter and the 'remuneration' for the good or service exchanged.

The case is interesting because it involves a claim against a commercial bank in Hungary by two borrowers that made a loan on foreign currency (Swiss francs). Therefore it is related to consumer rights and consumer protection and matters that are of interest across the European Union.

The outcome of the case was to clarify some aspects of the Directive, especially the meaning of 'plain and intelligible' language in core contract terms and to open the way for national courts to substitute contract terms, under certain circumstances, if they find that a term violates national law.

What issues did this case raise?

The case related to foreign currency loans which are fairly common practice in European countries. In these type of loan agreements the amount of the total sum to be returned as well as that of each individual installment are calculated in a foreign currency, in this case the Swiss Franc.

These loan agreements include standard terms according to which the bank has the right to charge consumers lower interest rates than would be the case if the contract were in local currency. However due to

the nature of the transaction there are many issues involved which are not always clear in the mind of the consumer.

In this particular case two different rates were applied--while the total outstanding amount was calculated on the basis of the rate the bank applied when buying Swiss Francs, the installments were based on the sale rate. The two rates can be considerably different, the sale 'price' being as a rule higher. So the main issue was whether the specific term was exempt following art 4(2) of the Directive.

The court held that the term in question was not autonomous 'remuneration', since the bank did not provide any additional service in relation to the credit agreement (in particular, it did not provide the lenders currency exchange services). So, in this sense, it could be the subject of examination.

However the court held that the said term could still be perceived as a core term, falling under the exemption of art 4(2), if the national court found, all the relevant elements taken into account, that the term 'constitutes an essential element of the debtor's obligation' (para [51]). Thus the term is not exempted as 'remuneration'--it could, however, be exempted as 'essential element of the obligation', which is for the national court to decide.

The second issue was this. If the said term was a core term falling under the exemption of art 4(2), can a transparency test be applied--although the applicable law did not contemplate this possibility? The transparency test in essence means that a contractual term must be drafted in plain intelligible language. The Court of Justice did not really answer this question leaving it with the national court to decide taking into account national law. In this context Advocate General Wahl's Opinion was different on this point. He was of the view that even in the absence of a clear provision in national law, the Directive should be read as if imposing such an obligation on national law.

Further the Court of Justice held that art 4(2) of the Directive must be interpreted as meaning that, the requirement for 'plain intelligible language' is to be understood as requiring:

- not only that the relevant term should be grammatically intelligible to the consumer, but
- also that the contract should set out transparently the specific functioning of the mechanism of conversion for the foreign currency to which the relevant term refers and the relationship between that mechanism and that provided for by other contractual terms relating to the advance of the loan

so that consumer is in a position to evaluate, on the basis of clear, intelligible criteria, the economic consequences for him which derive from it.

Finally with reference to art 6(1) of the Directive, the Court of Justice held that it must be interpreted as meaning that, in a situation such as that at issue in the main proceedings, in which a contract concluded between a seller or supplier and a consumer cannot continue in existence after an unfair term has been deleted, that provision does not preclude a rule of national law enabling the national court to cure the invalidity of that term by substituting for it a supplementary provision of national law.

To what extent is the judgment helpful in clarifying the law in this area?

The judgment is very helpful because it gives additional powers to national courts to delimit the applicability of national legislation so that it is line with the scope of the Directive.

Firstly national courts can ascertain having regard to the nature, general scheme and stipulations of the contract and its legal and factual context, if a term lays down an essential obligation of that agreement which, as such characterises it.

Secondly such terms, in so far as they contain a pecuniary obligation for the consumer to pay, in repayment of instalments of the loan, can be the subject of examination by the courts and do not escape scrutiny.

Thirdly, the term 'plain and intelligible' language of contractual terms was amplified. The Court of Justice in essence widened the rights of the consumer by deciding that the term 'plain and intelligible' is to be understood as requiring not only that the relevant term should be grammatically intelligible to the consumer, but also that the contract should set out transparently the specific functioning of the mechanism of

conversion for the foreign currency to which the relevant term refers and the relationship between that mechanism and that provided for by other contractual terms relating to the advance of the loan, so that consumer is in a position to evaluate, on the basis of clear, intelligible criteria, the economic consequences for him which derive from it.

Finally with reference to art 6(1) of the Directive the Court of Justice gave the power to national courts to cure the invalidity of an unfair term by substituting for it a supplementary provision of national law if national law permits this.

What are the implications for practitioners?

The key practical consequence of the judgment is that under certain circumstances it would be possible for national courts to replace an unfair term in a loan agreement with a supplementary national law provision.

So the first question would be to examine whether it is possible under national law for a national court to replace an existing contractual term with another one. If that is possible then it will open for borrowers to sue banks and claim as a remedy the substitution of an unfair term in a loan agreement with another one which is more fair.

If national law does not permit intervention into existing contractual agreements, which is the case in most common law countries, then the judgment may not have so many hands-on practical advantages.

Do you envisage any practical or technical difficulties or unintended consequences arising from the decision?

The judgment did not leave any grey areas therefore I would not say that there might be any practical or technical difficulties or unintended consequences arising from the decision.

The judgment is certainly very interesting as it may signal a way towards widening and strengthening consumer rights.

Are there any patterns or trends emerging in the law in this area? What are your predictions for future developments?

It is clear that the judgment is a positive development in the field of consumer rights vis-à-vis the banks. The Court of Justice elevated the importance of the Directive by interpreting its provisions widely and for the benefit of weakest party--ie the consumer. The philosophy of the Directive itself was to grant certain rights to consumers by declaring certain contractual terms as unfair. However it is not always clear when and under what circumstances a term may be unfair and which terms enjoy a sort of immunity.

This judgment gives a new perspective and understanding of the principal aim of the Directive which in turn is expected to have an impact on the applicability of domestic law provisions by national courts. I believe that there will be further jurisprudence in the future in the same direction--ie strengthening consumer protection.

Are there still any unresolved issues lawyers will need to watch out for?

This question cannot be answered since each case raises different issues and depends on its own facts. The Directive has many aspects and provisions and case law so far has touched on a handful of them.

There are certainly many unresolved issues. Consumer protection lawyers should watch out for any future decisions of the Court of Justice that touch upon the interpretation of the exemption provisions of the Directive since they are those that add or subtract from consumer protection rights.

Interviewed by Anne Bruce.

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