

SCIENTIFIC REVIEW

THE PROBLEM OF CURRENCY-INDEXED LOANS - CASE OF "CHF"

Ana Opacic³⁰, Vladan Perisic³¹, Jelena Gluscevic³²

ABSTRACT

Currency indexation entered the legal system of Serbia by changes of the Law of Contract and Torts in 1993 due to great economic movements and inflationary pressures. Law permitted contracting of loans in which the obligation can be tied to a foreign currency, so that the payment is done on the day according to the parity of that currency with the national currency. This form of currency indexation has a protective character, it should maintain the real value and equality of mutual giving between the contracting parties, but today, in case of "CHF" it has become usurious and it seriously compromises the equivalent of mutual giving in the contract. In this paper the authors provide the analysis of creation and basic characteristics of problems of loans in CHF and based on the conducted research, suggest actual measures for overcoming the problems of more than 20 000 citizens of Serbia.

KEY WORDS: Currency indexation, CHF, Serbia, Overindebtedness, Contract, Loan

JEL: H81

UDC: 336.781(497.11)

336.747.6

COBISS.SR-ID 227956748

³⁰ Corresponding Author ,Faculty of Business Economics and Entrepreneurship, Belgrade,Serbia,
e-mail:ana.galjak@gmail.com

³¹ Faculty of Business Studies and Law, Union "Nikola Tesla", Belgrade, Serbia

³² Faculty of Business Economics and Entrepreneurship, Belgrade, Serbia

INTRODUCTION

Loan indexed in CHF was not created at the area of Eastern Europe, as it could wrongly be concluded, but it was created in practice in Australia in 1980 (Jonnes, 2005). Australian banks offered to farmers loans indexed in foreign currencies such as CHF and Japanese yen. Interest rates of such loans were three times lower than the loans in Australian dollar, so it is clear that the demand was great for this new loan product. Situation seemed ideal up to 1986, when the Australian dollar entered the phase of depreciation, so the difference in the interest rates of the Swiss franc rapidly grew and became very unfavorable. Farmers who took loans in Swiss francs, faced with inability to pay the enormous interest rates, tried to agree with the banks on rescheduling of debt, however up until 1991, banks successfully collected the payments of the enormous interest rates for the loans indexed in CHF (Jonnes, 2005). Farmers, as the users of these loans in Australia, initiated court proceedings against banks, but without greater success, because the banks justified their unfair business operations by the responsibility of farmers for choosing between the loans in domestic currency and the ones indexed in foreign currency. As we can notice neither the scenario nor the rhetoric are not much different now than they were then. Banks, as well as the regulatory body of NBS, are defending themselves by using that basic argument that the user of the loan knew the risks and that he/she by signing the contract on the loan with the creditor accepted such risk. Average citizen is not able to estimate the certainty of the realization of the currency risk, especially of the currency whose stability depends only on one country. For such estimate of risk, it is necessary to have extraordinary knowledge of economic flows and it demands a continuous monitoring in order to be able to react at the right time, as well as exceptional knowledge of the matter of currency risks (Brkić, 2005). All of this is usually not the case with natural persons as loan users, such form of knowledge in economics is not possessed even by bank employees who, as loan advisors, inform users on all possible risks, so the justification of such argumentation for not acting, in case of Serbia, is questioned.

In Australia the case of CHF is solved through court proceedings, when the information, owned by the banks, was revealed. Former employee of the Westcap bank, John McLennan revealed the details of the bank's correspondence, from which it is obvious that neither the bank nor the user of the loan were able to control the risk which could happen (Jones, 2005). The investigation followed, which determined that the bank was committing fraud on purpose, because it even hired a law office with the goal of covering the intention of acquiring the extra profit. The condemnation of the political public followed as well as direct involvement of the state in respect of providing compensation (Jones, 2005). Australian scenario spread, in the later years, to other countries as well like Austria, Croatia, Montenegro, Bosnia and Herzegovina, Romania, Poland, Hungary etc. All cases follow the similar pattern, exceptionally favorable loan, then the realized risk and enormous payments by the users, great number of bankruptcies, court proceedings and at the end the reaction of the state. However, from the realization of the horrible scenario until the reaction of the state and the protection of the loan users who were deceived, many tragedies happen such as divorces, lost homes, suicides and bankruptcies which no court epilogue can compensate for (Opačić et al., 2016).

CURRENCY INDEXATION AND THE PROBLEM OF "CHF" IN SERBIA

Loans indexed in CHF entered the banking sector of Serbia in 2005, with the offer of HVB bank, which offered housing loans with the extremely favorable interest rate of 4.75% (Brkić, 2005). It is important to mention that at that time taking loans in dinars was not possible, but only in euros. Users, guided by low interest rates on one hand, opted for this loan product, but the attention must be paid to the fact that in many cases the user was not creditworthy for taking the loan in euros, so he/she was offered, by the bank employees, as the only way of concluding a contract on housing loan, to take a loan indexed in CHF. It is especially questionable that the banks, after the approved funds were tied to euro, actively offered the same clients to convert their loans in CHF due to better conditions, with ensuring them that if there are any currency turbulences, they can at any time convert their loan again and index it in euros. From today's perspective, this must be interpreted as responsibility of the bank, and the inability of the client to really understand the risk which can happen, so we cannot say, in any case, that the client by signing the contract understood and accepted the risk. On the contrary, we can say that there was an intentional fraudulent behavior of the management of the bank, which as the dominant party of the adhesion contract was very aware of all risks of this loan taking, and on which it did not inform the client. We can pose a question based on which information the clients made their decisions on whether to take the risk and conclude a contract on loans indexed in CHF. First of all based on the fact that they are creditworthy, that the CHF is extremely stable currency and that the NBS actually pointed that greater offer of these loans is strengthening the security of citizens. Is it not malicious to, nowadays, determine in the court that the clients were well aware of the risk they are entering during concluding such a loan relation (Opačić, 2016).

In our law, contracting the currency clause in the internal relations is allowed by changes of the Law of Contract and Torts from 1993, so in accordance with the article 395 of Law of Contract and Torts 1993, if the money obligation is tied to payment in certain foreign currency or gold, its fulfillment can be demanded in the domestic currency according to the exchange rate valid at the moment of the payment. Currency clause represents an instrument of protection from the risk of changes in the exchange rates, where the amount of the obligation, i.e. claims are contracted in foreign currency, and the payments are done in dinars (Opačić, 2015). Currency clause is most often contracted in order to protect the creditor, with the goal of preventing the decrease of real value of claims or their devaluation due to the change in values of money due to time passing (Law on Foreign Exchange Operations, 2014). The reason for which the currency clause is included in the loan contract is the need to maintain the real value of principal debt which is approved in dinars to the consumer. Such acting of banks was in accordance with the law and it is a consequence of general negative experience with the unstable domestic currency (Revt 249/14-2). However the base for the criticism of banks' actions, especially with the currency clauses related to the Swiss franc, is in the previously said, keeping the real value of the principal part of the loaned amount, and not earning the extra profit and unfounded gaining of wealth of the banking sector. With contracts with currency clause the obtained amount of money is evaluated according to the amount of the currency which serves as the meter of value i.e. the obligation is established to return the real value of the obtained money and pay to the bank an appropriate compensation for using the obtained money (Opačić et al., 2016). So, the question of whether the client knew or had to know, at the time of concluding the questionable contracts, is pointless because according to everything aforementioned it is clear that these high risk loans are placed to the weaker party, a regular citizen without the previous warning regarding the severity of the risks and referral of

insurance against them. An easy test for this claim would be the research regarding the knowledge of bank employees on the currency risks. This argumentation of banks in court proceedings, which are ongoing, based on the attempt of annulment of the currency clause as well as the loan contract as a whole, also the more frequent court proceedings for termination of the contract due to the changed circumstances, has led us try and conduct the questionnaire among the bank employees on basic issues by putting them in the role of loan users. The questionnaire included 84 participants in Banca Intesa, Telenor bank, Raiffeisen bank, Unicredit bank, EFG bank and ProCredit bank. In chart one, we can see the overview of the participants according to their age. By considering the age range for determining the capability of advising on the currency risks, we can see that even 36% of the participants is within the age range from 25 to 35, and that the majority of bank employees are actually employees of age from 36 to 45, which is around 50% of participants.

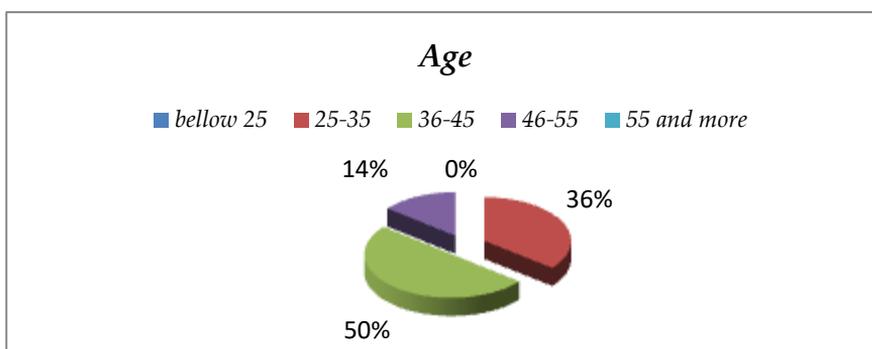


Chart 1: The overview of the participants according to their age

We should connect this criterion to the field of education of those bank employees who are in position to advise the natural persons on the currency risks.

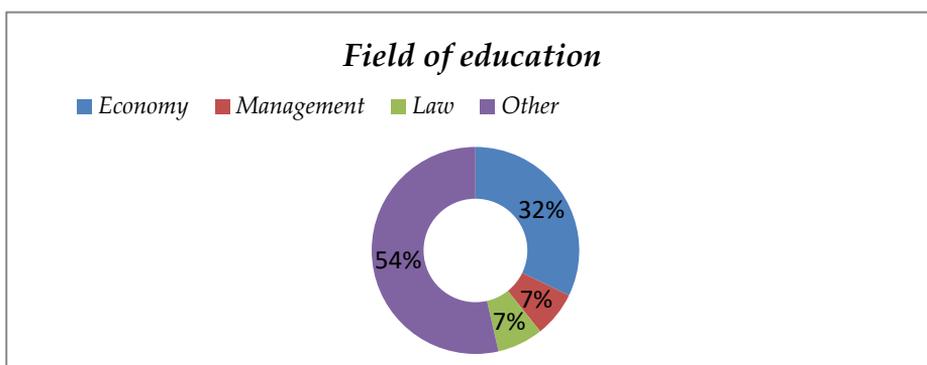


Chart 2: Field of education

Chart 2. shows that 54% participants are educated in the field of economics and 14% in the similar scientific fields, law and management, so we can conclude that employing of staff is done in a correct way, and that we can trust that these persons have enough economic knowledge for conducting the function of loan advising. However, the degree of education masks this statistics. If we look more carefully at the chart 2, it is obvious that even 32% of loan advisors come from the unrelated scientific fields, and if we look at the

part of questionnaire which examines the degree of education we can see that even 20.16% has a secondary education degree. At the end, chart 3. shows the preferences of loan users, so which is the deciding criterion which creates the new loan user.

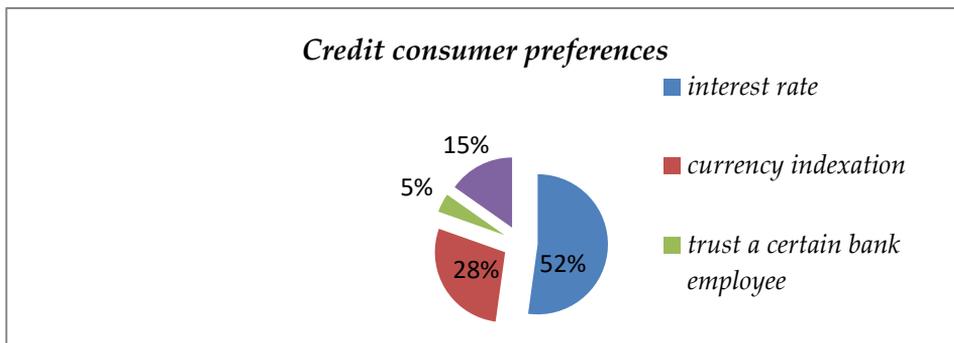


Chart 3: Credit consumer preferences

The following question was posed to the participants: "What is crucial during choosing the loan product?" As chart 3 shows even 52% of participants responded that it is the height of the interest rate, and what is especially interesting is that even 15% of the participants trust a certain bank, so that is why just by bank's placing a certain loan it is considered to be safe. The conducted questionnaire confirmed our assumptions, that the loan advisors, besides being, in most cases, inexperienced and young, they usually do not possess education in the field in economics or similar fields like law and management, and especially worrying is the fact that the large number of bank advisors graduated only from secondary schools. Is the answer to the previously posed question now a bit easier? Australian study (Jones, 2005) showed that the loan users were completely inexperienced regarding the questions of currency risks and that they even showed weak understanding of the documents and explanations which they obtained from the creditors, which had as a consequence them relying on the advice of the bank employees, who are not involved, to an appropriate extent, and they themselves do not understand the risks and dangers which come with currency risks in the long run. How can we then talk about the awareness of the risk and the responsibility of the other weaker party in the loan contract?

CONCLUSION

Users of loans indexed in CHF should have been warned during concluding a contract, that the selection of this currency indexation bears the risk of, in the long period during which a housing loan is payed, shifting of equivalency of mutual giving of the contract parties, due to the change in the exchange rate of the currency which is not only subject to the conditions in the money market, but also to the speculative behaviors, so that the value which has to be returned based on the taken loan becomes greater than the amount obtained (Opačić et al., 2016). Considering that we are talking about, as we already mentioned, the usual contract, it is the rule that vague clauses are to be interpreted in favor of the weaker party, i.e. loan user. In the previously prepared text the bank did not protect the rights of loan users to return only the amount which was taken, which disturbs the principle of equality of mutual benefits for which the responsibility must be placed to the bank, as well as the National Bank of Serbia which was obliged to conduct the control over the work of the banking sector (Zipovski et al., 2013) and disable this poor business practice of banks.

Considering the fact that the franc strengthened up to 250% from the moment of loan approval for certain users, there was great damage and serious breaches of mutual benefits of contract parties. Due to the time flow, since the loan contract is concluded, the enormous leap of value of the Swiss franc transformed the loan contract into the typical usurious contract. Law of Contract and Torts in article 141 foresees that the contract becomes null and void when someone, using the emergency state or difficult financial condition of the other party, due to his/her insufficient experience, nonchalance or addiction, contracts for themselves or for a third party the benefit which is obviously misbalanced with what he gave or done for the other party, or he is obliged to give or do. If we analyze this provision we shall see that both conditions are fulfilled, loan which solves the issue of housing can be interpreted as the condition of emergency or as difficult financial condition, and in relation to the banks each loan user does not possess enough experience to understand the loan contracts so he/she can be interpreted as nonchalant and not enough experienced. The disproportion of obligation which is asked for the application of the provision on the usurious contracts is more than obvious in the situation when after five or eight years of payment of the loans the user did not even commence the payment of the principal debt, which has enlarged in the meantime. The contract, at the moment of conclusion, was not, but during the payment time it has become a usurious contract. Since this contract is opposed to the principle of awareness and honesty and of equal value of mutual giving, as well as the principle that the participants are in obligational relations and are obliged to act in accordance with the good business relations and morale, sanction for these contracts is nullity. In the following period it is certain that there will be more and more court epilogues, an organized unique pressure to the banks and courts must be attained by the organizations which deal with protection of users of CHF indexed loans, in order to, with joint organized action really realize the rights for over 20 000 citizens of Serbia. However, one should always have in mind that no court epilogue can compensate for personal tragedies which are happening all around us.

REFERENCES

- [1] Brkić, M. (2005). Igra valuta i kamata, *Time*, 22. September 2005, available at: <http://www.vreme.com/cms/view.php?id=428372>
- [2] Jones, E. (2005). The Foreign Currency Loan Experience in 1980s Australia with particular reference to the Commonwealth Bank of Australia: bank documents, bank culture, and foreign currency loan litigation, *Discipline of Political Economy*, Sidney
- [3] Law of Contract and Torts, Official Gazette of SFRY, no.29/78, 39/78, 39/85, 45/89 and 57/89 and Official Gazette of SRY, no.31/93.
- [4] Law on Foreign Exchange Operations, Official Gazette of RS, no. 62/2006, 31/2011, 119/2012 and 139/2014, article. 2 and 34.
- [5] Opačić, A., Pilčević, A. (2016). Currency clause CHF as regional phenomenon in the context of euro integrations, *Services and user protection: [proceedings from and International scientific gathering held on 8th May 2016. At the Faculty of Law in Kragujevac]*. ISBN 978-86-7623-065-5, COBISS.SR-ID 223100684, Editor Miodrag Mićović, p.303-324.
- [6] Opačić, A. (2015). Protection of users of financial services in the context of harmonization with EU law, *Proceedings from and International scientific gathering XI May counselling, Kragujevac*, 2015, p. 317-333.
- [7] Opačić, A. (2016). The situation of users of financial services and currency clause that protects the interest of banks, *Selection of court practice: professional and informative magazine ISSN: 0354-3226.- 24*, no. 3 (2016), UDK 336.717.061(497.11)347.455, COBISS.SR-ID 221571596, p.5-10.
- [8] The Verdict and the Ruling of the Supreme Court of the Republic of Croatia in case Franc dated 14.05.2015, Revt 249/14-2.
- [9] Zipovski, Lj., Kvirgić, G., Vujadin N. (2013). Credit activities of commercial banks in Serbia: causes and consequences, *International Review (No.3-4)*.

Article history:

- **Received 17 October 2016**
- **Accepted 7 December 2016**