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Hungarian Credit Institutions before the European Court of Human Rights: Overcoming the FX Loan Crisis from a Human Rights Law Perspective**

Abstract

In the 2000s, retail financing products – including loan agreements registered in a foreign currency – became immensely popular in Hungary. Under these loan agreements, the loan was disbursed in Hungarian Forint at the offer foreign exchange rate of the financial institution and had to be repaid in Hungarian Forint at the then current bid foreign exchange rate applied by the financial institution. The growing demand for these financing products created a housing bubble that eventually burst in 2008, leading to a major social crisis. The crisis management of the Hungarian state was intensely discussed from numerous perspectives, yet the human rights aspect of the legal issues remained in the background. This article explains the history of the Hungarian foreign exchange loans by focusing on the fundamental rights of those involved. The article begins by presenting the economic causes leading to the crisis and the loan products in question, then it explores the legal difficulties surrounding the crisis management and the domestic lawsuits. This section is followed by analysing how the European Court of Human Rights dealt with this issue. The article ends with examining the deficiencies detected in the relevant decisions of the Strasbourg court, and how this decision fits in the general approach that is applied by the court when it comes to economic crises.

Keywords: human rights in economic crises, foreign currency loan agreements, fundamental rights of legal persons, ECHR, protection of property, direct effect of directives, inadmissibility

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I. Introduction

The era of the Hungarian foreign currency *(FX)* loan crisis has been discussed multiple times and in multiple forms in the Hungarian legal, economics and political science literature. Parallel to the slow recovery and the decrease in litigation, more comprehensive books of studies,[1] personal memoirs[2] and critical analyses of the management of the crisis have been published. The lawsuits precipitated by the crisis passed every instance of the Hungarian regular court system, ultimately reaching the Curia.[3] Moreover, at the international level, both the European Court of Justice and the European Court of Human Rights (the *ECtHR* or the *Court*) had the opportunity to examine various legal aspects of the FX loan crisis. This article reviews an aspect of this storm of litigation that is less discussed both in the legal literature and in the press: the fundamental rights of the creditors, including credit institutions.

The wider context of the topic is the management of economic crises, more specifically the human rights safeguards under crisis management. It goes without saying that extraordinary situations require extraordinary legislative measures. The concept of public emergency is well embedded in the human rights law regime and is contained by the European Convention on Human Rights (the *ECHR* or the *Convention*), too. However, the Convention does not include any derogation clause for economic crises or, more generally, situations where the existence of a nation that is not at stake, therefore, the general rules for derogation apply. Consequently, if the legislator introduces measures that potentially violate human rights, the wording of the relevant provisions – and the inherent limitations – apply along with the jurisprudence of the Court. How does the fact of an economic crisis appear in the argumentation of the Court? In what stage of the evaluation does the ECtHR consider the demand for the state to ease the social tension caused by recession, and how can this demand justify any restrictive measures adopted as part of a recovery package?

To illustrate the responses of the ECtHR to the above questions, this article takes the Hungarian FX loan crisis as an example that revolves around the collapse of the residential FX mortgage portfolio. First, the article presents the events that contributed to the appearance of loans denominated in foreign currencies on the Hungarian retail market, and the impact of the global financial crisis. The article then explains the legal construction of the affected loan products, the measures by the Hungarian state aiming to mitigate the crisis, and the related domestic litigation initiated by the banks. Following the exhaustion of domestic remedies, the banks turned to the European

[1] See Bodzási B. (ed.), *Devizahitelezés Magyarországon. A devizahitelezés jogi és közgazdasági elemzése,* (Budapesti Corvinus Egyetem, Budapest, 2019).

[2] Király J., *A tornádó oldalszele,* (Park, Budapest, 2018). The author, Júlia Király, was the vice president of the Hungarian National Bank between 2007 and 2013.

[3] The high court in Hungary.

Court of Human Rights, that declared their complaints inadmissible. The article reviews this inadmissibility decision and argues that the ECtHR based this decision on an incomplete reading of the underlying facts and the law for two main reasons. First, the decision did not take crucial factual elements into consideration, such as the passivity of the state and the competent public institutions to prevent the escalation of the crisis, and second, the decision misinterpreted the effect of EU law on individuals. The article concludes that the ECtHR did not deviate from its general approach to interference with fundamental rights in times of economic crises. Unfortunately, this time, the basis of this legal assessment was at best deficient.

II. The era of consumer FX loans in Hungary

1. Housing schemes after the regime change

The development of residential mortgage products was the result of collision of two chains of events.

The first chain of events was the transformation of the Hungarian market for the construction of residential premises. Following the political, social and economic change in 1989, the market for the construction of houses showed a strong decline. The number of newly built premises dropped by almost 50% between 1989 and 1994 (from 51 thousand per year to approx. 21 thousand apartments per year), and it lagged behind the ideal 40 thousand new apartments per year for more than ten years (until 2004).[4] In addition to the shrinking supply side of the market, the low level of the Hungarian salaries compared to the European average, paired with a high rate of inflation made it very difficult for a person in Hungary to buy their own apartment. The solution to such cases would be retail financing; however, this was underdeveloped due to the characteristics of the previous regime. The strong depreciation of the Hungarian Forint (HUF) and high central bank rates kept the interest rates of the HUF loan products high and so these loans did not become popular.

The second chain of events revolved around the general market liberalisation following the regime change. Hungary submitted its application for EU membership in 1994, and joined the OECD in 1996, which resulted in the gradual abolition of all barriers concerning credit operations denominated in a foreign currency (i.e. currency

[4] Kovács L., A devizahitelek háttere, (2013) 12 (3) *Hitelintézeti Szemle,* 183–193., http://epa.oszk.hu/02700/02722/00066/pdf/EPA02722_hitelintezeti_szemle_2013_3_183-193.pdf (Last accessed: 31 December 2020); Hungarian Central Statistical Office: *Housebuilding and camping house building (1960–),* https://www.ksh.hu/docs/hun/xstadat/xstadat_hosszu/h_zrs001.html (Last accessed: 31 December 2020).

other than HUF). As a long-term consequence of future EU accession, the introduction of the euro became an increasingly clear vision for the country.

These two processes crossed shortly after 2000. In 2001, the Hungarian government announced a housing scheme that encompassed a retail housing loan (denominated in HUF) that was favourable to both the banks and consumers.[5] Under this scheme, the state provided a 3% interest subsidy for mortgage products, and it covered 80–100% of non-performing loans under certain circumstances. This scheme made credit institutions, which previously concentrated on corporate financing, diversify their portfolio and focus more on the retail market.

The scheme shook up the Hungarian construction market and considerably raised creditor demand. While the 90s could have been described as an era of a weak loan market and low competition, the 2000s saw a boom in retail financing products. Demand grew even more sharply after the government raised the interest subsidy from 3% to 10% in 2002, which put more pressure on the banks to expand their retail portfolio. However, retail financing entails higher costs than corporate business, in terms of maintaining the infrastructure (setting up branches, recruiting personnel etc.), therefore the banks needed extra volume to achieve a fair return, which in turn generated fierce competition on the supply side.[6] The volume targets were incorporated in the compensation plans of the banks' executive officers, too.

In 2002, the new government withdrew the housing scheme for budget reasons (although it has to be noted that the scheme could not have been maintained after Hungary's accession to the European Union anyway, as it raised state aid concerns).[7] This measure made HUF loan products even more unpopular: around the time of the millennium, the central bank rate of the HUF was above 10%, which resulted in high interest rates on the financial market. The banks therefore offered a new option for consumers wishing to buy their own apartment: loan products denominated and registered in a foreign currency (most frequently in CHF). Under these loan agreements, the loan was disbursed in HUF at the offer FX rate of the financial institution and had to be repaid in HUF at the then current bid FX rate applied by the financial institution (the *FX Loan Agreements*). This loan product became popular in an instant. By 2010, FX Loan Agreements accounted for two-thirds of the total Hungarian household debt, i.e. HUF 7300 billion (approx. EUR 24,5 billion), equalling 28% of the GDP.

[5] Government Decree 12/2001. (I. 31.) on state subsidies for residential purposes.
[6] Bethlendi A., Egy rossz termékfejlesztésből rendszerszintű piaci kudarc, (2015) 14 (1) *Hitelintézeti Szemle,* (5–29) 7–8.
[7] See Judgment of 19 March 2015, *OTP Bank Nyrt.,* C-672/13, ECLI:EU:C:2015:185.

2. The impact of the global financial crisis on the housing bubble

The effects of the global financial crisis reached Hungary a few years after the crisis broke out in the United States. The reason for this delay was that the structured financial instruments – which contributed to the bubble on the American real estate market bursting – rarely appeared in the portfolio of the Hungarian financial institutions. Hungarian banks, even under difficult circumstances, were able to obtain the necessary amount of foreign currency on the interbank market.

The turning point came with the bankruptcy of Lehman Brothers Holdings, Inc., the fourth-largest investment bank of the United States, which filed for bankruptcy protection in 2008 and prompted panic among investors. The general fear induced investors to withdraw their accounts and hoard their cash and, as a result, the credit markets became frozen. In their credit agreements, the banks had trouble providing appropriate collateral, which caused a general liquidity crisis. This crisis had its impacts primarily on the bank system and the interbank credit market. Investors preferred investments that were traditionally considered to be safe (such as the Swiss government bonds), which was conducive to the gradual increase in the foreign exchange rate of the Swiss Franc.

The crisis found Hungary in a particularly sensitive state. The high sovereign debt (with the net external debt reaching approx. 50% of GDP at the end of 2007), the high interest rate of the central bank and the widespread FX Loan Agreements all added up to a high foreign debt. A significant portion of this debt (almost two third of the total net external debt) was attributed to the private sector.[8] Although the level of the foreign exchange reserves of the Hungarian Central Bank met the requirements at that time, it proved to be clearly insufficient when the banks attempted to obtain foreign currency from sources other than the interbank market. The foreign parent companies of the local subsidiaries initiated significant capital injections to facilitate the smooth operation of their Hungarian branches. However, expensive credit on the interbank market and the constant rise of the foreign exchange rates ultimately resulted in drastically increased repayment instalments under the relevant FX Loan Agreements. By July 2010, Hungarian household debt amounted to approx. HUF 10,600 billion (approx. EUR 40 billion) equalling 40% of the GDP. The collapse of household lending raised the threat of a social catastrophe. To escape the catastrophic consequences of this collapse, the debtors looked for legal ways to challenge the FX Loan Agreements. In order to explain the most frequently occurring legal issues in these litigations, the article continues by presenting the legal construction of FX Loan Agreements.

[8] For a comprehensive summary of the history of the financial crisis in Hungary please see Király, *A tornádó oldalszele*.

III. The residential FX loan as a legal construction

The innovative nature of residential FX loans may be illustrated by the fact that, when these products became widespread, they did not even have a comprehensive legal definition. There was no act providing for a unified and comprehensive definition of FX loans and FX based loans; only the general APR Decree contained a method for calculating the annual percentage rate of loans associated with foreign currency.[9] When the crisis broke, the measures aiming at mitigating the recession were focused only on certain aspects of the crisis and, accordingly, the different laws and regulations came up with different definitions for FX loan agreements. The overlap between these definitions was not complete. Therefore, it was left for the Curia to face this regulatory hiatus.

1. The general structure of FX loan agreements as established by the Curia

In its civil law uniformity decision 6/2013.[10] (the *6/2013. Uniformity Decision*), the Curia made the following main assumptions: (i) under the foreign-currency loan agreements, the debtors were entitled to use a certain amount of money, and (ii) there was no restriction in the Hungarian Civil Code[11] preventing the parties from freely agreeing upon the currency of the disbursement and the currency of the repayment. On this basis, the Curia held that an FX loan agreement was an agreement where the loan was disbursed in a currency other than HUF. A subcategory of FX loan agreements is the category of FX *based* agreements, under which the amount of the loan is registered in a foreign currency, but the creditor disburses the loan in HUF, and the debtor repays it in HUF, too. For the sake of simplicity, this article will use the term 'FX loan agreement' in a sense that it includes both FX loan agreements and FX based loan and financial lease agreements.

The most frequent choice of currency for registering the loan was the Swiss franc, followed by the Euro and the Japanese Yen. By September 2008, 95% of the total amount of FX loan agreements were denominated in CHF. The interest rate presented to consumers mainly depended on the interest rate that the banks faced on the interbank market when they acquired the necessary capital in the given currency (contrary to the common belief, financial institutions were required to provide the corresponding amount of foreign currency for each loan). After 2000, the average interest rate on the interbank market was between 1 and 5%, which allowed the banks

9 See Art. 11/B and 13 of Government Decree 41/1997. (III. 5.) on the calculation and publishing of the interest rate, the income of securities and the annual percentage rate.

10 Available at: https://kuria-birosag.hu/hu/joghat/62013-szamu-pje-hatarozat (Last accessed: 31 December 2020).

11 Act IV of 1959 on the Civil Code (the *Old Civil Code*).

to offer favourable interest rates to the consumer, too. In comparison, the interest rate of the HUF on the interbank market was between 8 and 10% (due to the high central bank rate), that necessarily resulted in a higher interest rate offered to the consumer. In addition, the Hungarian branches of several international banks (such as Erste, and Intesa Sanpaolo) were eager to acquire higher market share, and they were able to get cheap FX loans from their parent company. The retail financing gained momentum, and the FX bubble grew bigger and bigger.

In most cases, the loan was actually disbursed in HUF. To calculate the amount of the disbursement, the banks generally applied their then applicable offer FX rate (instead of the exchange rate of the central bank). Then again, the amount of the repayment instalments was calculated on the basis of the then applicable bid FX rate of the credit institution (the *FX Gap Provision*). The constant fluctuation of foreign exchange rates entailed a higher risk, entirely placed on the consumer side.

However, the unstable nature of the exchange rates was not the only uncertain element of the FX loan agreements. In the majority of loan agreements in general (even in those denominated in HUF), the credit institutions set out the right to increase interest, costs and fees unilaterally (the *Unilateral Increase Provisions*). The conditions for such increase were rather vague: the agreements merely contained a list of factors that could have an impact on the level of costs or interest. These factors included the yield-rate of Hungarian government bonds, the creditor's cost of funds and any change in the creditworthiness of the consumer, but also the operational costs of the relevant bank; their office lease fees as well as marketing costs. As illustrated by this list, some of these factors were only indirectly connected to the underlying loan, and some of them were hardly comprehensible in themselves.[12] Moreover, none of these factors was directly linked to the interest rate, therefore, it was not possible to predict that a certain increase of the operational cost of the bank would result in an equal increase in the interest rate of the loan agreement. To address this uncertainty and to achieve a transparent system of cost elements, the banks adopted a Code of Conduct in 2009, however, that code was not mandatory and did not apply to the FX loan agreements concluded earlier.

The 6/2013. Uniformity Decision also stated that the vast majority of the debtors in FX loan agreements were consumers. To comprehend the significance of this conclusion, the article will briefly present the general level of financial consumer protection in Hungary after 2000.

[12] Berlinger E., A változtatható és a változó kamatok veszélyei, in Bodzási B. (ed.), *Devizahitelezés Magyarországon. A devizahitelezés jogi és közgazdasági elemzése,* (Budapesti Corvinus Egyetem, Budapest, 2019) 38.

2. Financial consumer protection and the sectoral regulation of the credit market

As the cliché goes, the financial literacy and culture of Hungarian consumers have generally been at a low level. Nevertheless, neither the legislator, nor other public institutions or financial institutions made any particular effort to protect the growing number of consumers entering into loan agreements. Against this lack of interest in financial consumer protection, it is not surprising that the relevant legal acts did not even apply a uniform definition of 'consumer'.

At the time when FX loan agreements were heavily promoted and taken up, between 2004 and 2010, the Old Civil Code set out that a consumer is a person who concludes an agreement for a purpose outside the scope of his economic or professional activity. The specific sectoral act, the Old Banking Act[13] applied a narrower definition: a consumer was any natural person acting for a purpose outside the scope of his economic or professional activity. These concise definitions coupled with the conceptual slippage were unable to answer a number of questions that emerged in day-to-day life, such as should a person qualify as a consumer if they are providing security in order to enable their company to enter into a credit agreement?[14] And even if a person qualified as a consumer, judiciary practice set a certain standard of care. According to the recommendation of the president of the Hungarian Financial Supervisory Authority (the *PSZÁF*), the consumer 'acts in a reasonably informed manner, with due diligence and care that is expected in the particular situation'.[15] Further, the 6/2013. Uniformity Decision stipulated that 'it is at least expected from a borrower to study the contract thoroughly and, if necessary, to ask for clarifications about the provisions he does not comprehend. Failing to do so shall be interpreted to the detriment of the borrower pursuant to Art. 4(4) of the Hungarian Civil Code'.[16] As apparent, the then applicable Hungarian legal acts did not provide strong prerogatives for consumers. Moreover, no act resolved payment services provided to natural persons before 2009.[17]

This article argues that the legislator and the regulator expected an attitude from the consumer that matched the scope of the loan agreement, in the sense that consumers should have behaved in an extremely cautious manner. When a debtor offers his home as collateral, one would expect the debtor to learn about the agreement with the utmost accuracy. However, this idea behind the regulation did not take into account

[13] Act CXII of 1996 on credit institutions (the *Old Banking Act*).
[14] Court decision EBH 2005, 1321.
[15] 14/2012. (XII. 13.) Recommendation of the President of the PSZÁF, 2.
[16] 6/2013. Uniformity Decision, III.3.
[17] As most consumer protection laws, the acts on payment services provided to natural persons were adopted under the pressure of the European Union to harmonise legislation. For more details see Németh Cs., A pénzügyi fogyasztóvédelmi jog fejlődése Magyarországon 2008–2014 között (I. rész), (2015) (1) *Gazdaság és Jog,* (3–11.) 4.

the financial literacy of an average consumer, not to mention the fact that the FX loan agreement was a new and innovative product on the market.

To summarise the above, the agile business strategy of the banks to raise their market share, the shifted focus on retail financing and the oversupply of loan products hit both consumers and consumer protection regulation hard and found them unprepared. To illustrate the situation with a colloquial analogy, it was as if consumers were getting into a car for a long journey but did not check the brakes and did not care about the lack of airbags either.

IV. Crisis management and domestic litigation

1. Measures by the National Assembly and the government to mitigate the crisis

Given that the crisis affected horizontal relations (in the sense that the state was not part of the underlying FX loan agreements), the National Assembly referred to the basic principles of contract law, most notably to the respect for the contractual autonomy of the parties, and refrained from interfering with the existing relations. Therefore, the debtors started to challenge the FX loan agreements before the court. The civil lawsuits – mainly due to Hungarian procedural characteristics – showed little progress over time, and the number of cases was increasing. By 2010, it became clear that the growing number of non-performing loans might have long-term consequences, such as the negative influence on Hungary's sovereign Credit Default Swaps (CDS).[18]

In response to growing public indignation, the Hungarian legislator adopted several amendments to the Hungarian financial laws, most importantly to the Old Banking Act.[19] In 2010, the legislator introduced additional conditions for raising interest rates, fees and costs.[20] Credit institutions had to put their pricing principles in writing, based on which they could make any unilateral increase. The PSZÁF, the financial watchdog of Hungary, continuously assessed the validity of, and monitored compliance with, such pricing principles, but rarely found any failure. In addition, the so-called Early Repayment Act21 provided for the early repayment of FX loans secured by mortgages on residential real estate, resulting in a 23.3% decrease in such loans.

[18] The sovereign CDS indicates how much risk it entails for a bank to invest in a certain country. For a comprehensive summary see Király, *A tornádó oldalszele,* 309–312.

[19] Notably, the amendment applicable as of 27 November 2010 required the credit institutions to apply either a median FX rate set by the credit institution or the official FX rate of the Hungarian Central Bank.

[20] Government Decree 275/2010. (XII. 15.) on the conditions of the unilateral amendments to the interest rate set out in contracts.

[21] Act CXXI of 2011.

Nevertheless, as the HUF/FX exchange rates continued to increase, the remaining debtors still faced grave difficulties. As the economic crisis deepened, a tidal wave of borrowers challenged the validity of the FX Loan Agreements on several grounds.

2. Civil lawsuits in Hungary

The invalidity of FX loan agreements was claimed on two levels: (i) the debtors put forward that the structure of the FX loan agreements as such was in violation of Hungarian law, but even so, (ii) the debtors were insufficiently informed before concluding the individual contracts.

Concerning the specific structure of FX loan agreements, a great number of t applicants claimed that they were in fact HUF-based agreements, since there was no foreign currency transaction behind the agreements.[22] The loan was disbursed in HUF, and similarly, the loan had to be repaid in HUF, too. Further, the applicants pointed out that all the risk associated with the depreciation of the foreign exchange rate was put solely on the debtor. This mechanism in itself raised concerns as to the validity of FX loan agreements. The legal reasoning behind this claim varied: the applicants claimed that the FX loan agreements were contrary to the principle of good faith; they were usurious; they were based on grave misrepresentations and were impossible to fulfil. In addition to the general risk posed by the FX rate, the FX Gap Provision was also challenged in many lawsuits. Finally, during the lawsuits, many references had been made to the allegation that the FX loan agreements did not come into existence as the parties had not been in agreement upon essential conditions. The biggest concern was that the actual amount to be repaid could not be specified in the FX loan agreements, as it was subject to constant change (following the fluctuation of FX rates).

Beyond the specific structure of the FX Loan Agreements, the debtors challenged the Unilateral Increase Provisions, too. According to the applicants, these provisions were not sufficiently clear and precise, since the contracts clearly circumscribed the specific mechanism through which any cost, fee or interest to be borne by the consumer was calculated.

The judgments delivered by the first and second instance courts were contradictory to each other in all of the above-mentioned features of the FX Loan Agreements,

[22] Vezekényi U., A fogyasztói deviza alapú hitelezéssel összefüggő perekben felmerült jogkérdésekről és az ezekből levonható tanulságokról, in Bodzási B. (ed.), *Devizahitelezés Magyarországon. A devizahitelezés jogi és közgazdasági elemzése,* (Budapesti Corvinus Egyetem, Budapest, 2019) 378–379.

and the number of lawsuits was steadily rising: from 600 proceedings initiated in November–December 2013 to 36,000 by the end of 2016.[23]

***a)* Proceedings before the Curia: establishing the Fairness Test**

Although not every lawsuit reached the Curia, the political pressure on the judicial body was increasing. To facilitate the work of the lower instance courts, the Curia first issued a number of general guidance.

The first of these was the 2/2012. (XII. 10.) PK Opinion (the *2/2012. Opinion*)[24] about the Unilateral Increase Provisions. The Curia introduced a test consisting of seven principles that the Unilateral Increase Provisions had to meet. This test comprised: (i) the principle of unambiguous and intelligible language, (ii) the principle of itemised determination, (iii) the principle of objectivity, (iv) the principle of actuality and proportionality, (v) the principle of transparency, (vi) the principle of the freedom to terminate and (vii) the principle of symmetry (together the *Fairness Test* or the *Seven Principles*). When elaborating on the Seven Principles, the Curia primarily referred to the requirement of 'plain intelligible language' as contained in section 209(5) of the Old Civil Code. This provision was included in the Old Civil Code by way of implementing the Unfair Terms Directive of the European Union,[25] and it was applicable from 22 May 2009. In addition, the Curia referred to the provisions of the Old Banking Act, applicable from 1 January 2010. Of course, all these provisions came into force years after the first FX loan agreements were concluded.

However, this general guidance was not sufficient to give unambiguous responses to the many other questions surrounding the FX loan agreements. As reiterated above, the lower instance courts judged crucial aspects of these contracts in different ways. For example, placing the entire risk for the depreciation of the foreign exchange rates on the consumer was considered by one tribunal as rendering the agreement null and void, while another affirmed its validity. In order to prevent the Curia from assessing the question case by case, the head of the Civil College of the Curia requested the lower instance tribunals to submit information on the number of the lawsuits concerning the FX loan agreements, as well as the main recurring legal questions.

The information received was processed within three weeks, and the Curia put its conclusions in the 6/2013. Uniformity Decision. This Uniformity Decision underlined,

[23] From November 2013, the court marked these lawsuits by writing 'DH' on the file, hence the exact statistical data. The statistical data of the National Office for the Judiciary is available at https://birosag.hu/nyomtatvanyok/deviza-es-forinthiteles-peres-eljarasok/devizahiteles-peres-ugyek-2013-november-1 (Last accessed: 31 December 2020).

[24] 2/2012. (XII. 10.) PK Opinion on the unfairness of the standard terms of contract allowing for unilateral modification of a consumer-loan contract employed by a financial institution.

[25] Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts, OJ L 95, 21.4.1993, p. 29–34. (the *Unfair Terms Directive*).

as a matter of principle, that the FX Loan Agreements do not violate national legislation, are not contrary to the principle of good faith, are not usurious, are not based on grave misrepresentation, nor are impossible to perform solely for the reason that it is the debtor that bears the risk of the fluctuation of the FX rate in exchange for a favourable interest rate.[26] The drastic depreciation of the HUF against other currencies following the conclusions of the FX Loan Agreements could not be assessed within the scope of validity, because any reason for invalidity must be present at the very moment of the conclusion of the underlying contract. Therefore, the concept of the FX loan agreements was affirmed by the court: the *possibility* of an event occurring that would result in a great disproportionality to the detriment of the consumer, and thus violating the principle of good faith, was not considered as a provision already contrary to good faith.

The debtors were greatly disappointed by the 6/2013. Uniformity Decision but they did not lose hope. There was an ongoing preliminary procedure before the European Court of Justice (the *ECJ*), in which the ECJ had to answer, *inter alia,* whether the FX Loan Agreements met the requirement of being written in a 'plain intelligible language', as interpreted according to the Unfair Terms Directive.[27]

***b)* The responses given by the *Kásler* case to the questions concerning the FX Gap Provisions and whether the provisions were written in plain intelligible language**

Árpád Kásler and his wife Hajnalka Káslerné Rábai concluded their FX Loan Agreements just months before the economic crisis broke out, on 29 May 2008. Due to the rapid depreciation of the HUF, their repayment instalments increased steadily. Like many of the debtors at that time, the couple turned to the court and initiated proceedings against OTP Bank, the largest retail bank in Hungary. The applicants argued that their FX loan agreement did not meet the criteria of Art. 4(2) of the Unfair Terms Directive. Pursuant to that provision, the potential unfair nature of a term cannot be assessed if that term relates either to the definition of the main subject matter of the contract or to the adequacy of the price and remuneration, on the one hand, as against the services or goods supplied in exchange, on the other, *insofar* as these terms are written in plain intelligible language.

The applicants specifically referred to the FX gap provision. It was argued that the different exchange rates confer an unjustified benefit on the bank. To assess this claim on the merits, the applicants had to substantiate two alternative lines of argumentation: (i) either the FX gap provision was a regular contractual provision, in the sense that it did not relate to the main subject matter of the contract; or (ii) the

[26] 6/2013. Uniformity Decision, point II.

[27] Judgment of 20 April 2014, *Kásler Árpád and Káslerné Rábai Hajnalka v OTP Jelzálogbank Zrt.,* C-26/13, ECLI:EU:C:2014:282 (the *Kásler*-judgment).

FX gap provision did relate to the main subject matter of the contract; however, it was not in plain intelligible language.

The case of the Káslers ultimately reached the Curia, that in turn initiated a preliminary procedure about the FX gap provision. In its judgment, the ECJ held that it was for the national court to determine whether the FX Gap Provision constituted part of the subject matter of the FX loan agreements. In any case, this provision could not be regarded as a remuneration that was exempt from an assessment of its fairness, provided that the provision was drafted in a clear and intelligible manner.[28] This requirement should go beyond grammatically correct and plain language. The ECJ requested an assessment of whether the consumer, when reviewing the information material before signing the FX Loan Agreement, was able to recognise the difference that is generally present between the offer and the bid rate of a foreign currency, and was able to assess the impact of the change of the FX rate on the instalments and on the entire amount of the loan.[29] Finally, even if such a contractual term was invalid, the national court may remedy the situation by replacing the invalid term with an applicable, dispositive provision of the national law.[30]

By its very nature, the judgment of the ECJ could not decide the outcome of the underlying case. However, the Curia relied heavily on the sections of the judgment that explained the requirement of 'clear and intelligible language'. On this basis, the Curia delivered its judgment 2/2014. Civil Law Uniformity Decision (the *2/2014. Uniformity Decision*) on 16 June 2014. This decision was a major turning point in the legal assessment of FX loan agreements.

c) Final decision on the FX Gap Provision and the Unilateral Increase Provisions

The 2/2014. Uniformity Decision held that the contractual term that conferred the entire risk of a change in the FX rate on the consumer – in exchange for a favourable interest rate – indeed constituted the subject matter of the FX loan agreements. That said, the invalidity of these terms cannot be assessed unless they are not drafted in a clear and intelligible manner. However, the 2/2014. Uniformity Decision claimed that the FX rate gap itself was unfair because there was no actual underlying service behind the application of a different FX rate when providing the loan and when receiving the instalments, respectively. Instead of applying different FX rates, the Curia held that the instalments must be calculated on the basis of the applicable rate of the Hungarian Central Bank.

Concerning the Unilateral Increase Provisions, the 2/2014. Uniformity Decision confirmed the Fairness Test as set out in the 2/2012. Opinion and held that these were

[28] *Kásler*-judgment, para. 59.
[29] *Kásler*-judgment, paras 74–75.
[30] *Kásler*-judgment, para. 85.

unfair unless they would completely satisfy the seven principles of the Fairness Test. The 2/2014. Uniformity Decision did not expect consumers to inquire about any provision they find unclear. The Curia held that it fell within the responsibility of the credit institution to present the surrounding circumstances of the FX Loan Agreement so that the consumer was able to evaluate the obligations they were about to undertake.[31] According to the Curia, meeting the Fairness Test was a necessary requirement for such a presentation.

Pursuant to the Fundamental Law, uniformity decisions have a binding legal effect on lower courts.[32] Consequently, the credit institutions expected that this reasoning would appear in the upcoming judgments. However, there was little time left for the legal representatives of the banks to change their litigation strategy. The legislator, based on the findings of the Curia, re-regulated the FX loan agreements.

3. From judicial decision to the legislation – the FX Loan Act

Weeks after the delivery of 2/2014. Uniformity Decision, on 4 July 2014, the Parliament adopted Act XXXVIII of 2014 on the resolution of questions relating to the Uniformity Decision concerning the settlement of certain issues relating to loan agreements between consumers and financial institutions (the *FX Loan Act*).

In essence, the FX Loan Act repeated the main conclusions of the 2/2014. Uniformity Decision. The FX Loan Act provided that the FX Gap Provision is considered to be null and void, thus preventing what would have been a massive wave of litigation. Instead of the application of different FX rates, the FX Loan Act rendered the rate of the Hungarian Central Bank as the mandatory FX rate to be applicable during the performance of the FX loan agreements.

Concerning the Unilateral Increase Provisions, the legislator took the Fairness Test and reformulated it as a rebuttable presumption. The FX Loan Act set out that the Unilateral Increase Provisions, as applied from 1 May 2004 – on which date Hungary joined the EU – in the FX loan agreements, are null and void because they do not meet the Fairness Test.[33] To rebut this presumption, the credit institutions could have initiated proceedings in which they could only claim that their standard FX Loan Agreements complied with all of the principles of the Fairness Test.[34] This meant that, in practice, that the credit institutions could not challenge the legitimacy of these principles. The credit institutions had 30 days from the date of effect of the FX Loan Act to lodge this claim before the domestic court. The rules of this court procedure

[31] 2/2014. Uniformity Decision, III. 2.
[32] Fundamental Law, Art. 25(3).
[33] FX Loan Act, Section 4.
[34] FX Loan Act, Section 8(4).

significantly deviated from that of the ordinary civil proceedings. The rebuttal of the unfairness presumption was considered in an expedited procedure. After the court received an application, it must set the date of a public hearing within 8 days from the receipt.[35] No intervention, counterclaims, modifications of the statement of claims or requests for missing information were allowed.[36] In sum, the credit institutions entered into a procedure with tight rules that gave the judge any hardly possibility to delve into the individual agreements. At the same time, all the other ongoing suits – 13,268 civil proceedings – relating to the validity of the FX Loan Agreements were suspended by virtue of the FX Loan Act.

4. The litigation attempting to rebut the unfairness presumption

Altogether 73 credit institutions challenged the unfairness presumption as provided by the FX Loan Act. The general terms and conditions (the *GTCs*) submitted by each credit institution, were more than ten thousand pages long and, in addition to these, robust legal arguments concerning the legality of the FX Loan Act were presented in each application.

Part of these arguments addressed Hungary's failure to fully transpose the Unfair Terms Directive. Hungary should have implemented this directive by 1 May 2004; however, the transposition remained incomplete: the requirement of the 'plain intelligible language' as provided by Art. 4(2) of the Unfair Terms Directive[37] was not incorporated in the Hungarian law. Due to this failure, an infringement procedure was initiated by the European Commission. As a result, Hungary transposed this requirement by amending the Civil Code in 2009, and the infringement procedure was closed the same year. Nevertheless, this amendment of the Civil Code, incorporating Art. 4(2) of the Unfair Terms Directive, did not have retroactive effect. Therefore, the credit institutions argued that the FX Loan Agreements concluded between 2004 and 2009 were in full compliance with the law.

The other main line of argumentation was that the FX Loan Act violated the provisions of the Fundamental Law of Hungary on prescribing the protection of property and the requirement of a fair trial. Moreover, the FX Loan Act allegedly violated the equivalent provisions of the European Convention of Human Rights. The rationale behind invoking the ECHR was that the ECtHR, when assessing the

[35] FX Loan Act, Section 10(2).
[36] FX Loan Act, Section 7(7)a)–d), h).
[37] Art. 4(2) of the Unfair Terms Directive: 'Assessment of the unfair nature of the terms shall relate neither to the definition of the main subject matter of the contract nor to the adequacy of the price and remuneration, on the one hand, as against the services or goods supplies in exchange, on the other, *in so far as these terms are in plain intelligible language.*' (Highlighted by the author.)

fulfilment of the admissibility criteria, pays special attention to whether the applicant referred to a violation of the ECHR when exhausting the domestic legal remedies, and the national courts could assess such allegations. In the majority of Hungarian cases, the courts did not share the view of the credit institutions on the potential violation of the ECHR.

5. The resolution of the Constitutional Court

During the litigation challenging the FX Loan Act, numerous applicants submitted a motion in which they requested the court to turn to the Constitutional Court and initiate a procedure to assess whether the FX Loan Act complies with the Fundamental Law. As a result, the Constitutional Court delivered several resolutions in which it assessed certain provisions of the FX Loan Act.[38] In addition, three concerned credit institutions, as well as one debtor (a natural person) submitted individual complaints pursuant to Section 26(2) of the Constitutional Court Act.[39]

The credit institutions referred to the violation of Article B(1) of the Fundamental Law. According to their motion, the FX Loan Act ignored the statutory limitation period and allowed for the enforcement of obligations stemming from long-term contracts that had expired and, hence, were unenforceable. This is contrary to the respect of acquired rights that are, as per the motions, 'intangible assets that were acquired in exchange for material investment, while trusting in the applicable legal environment'.[40]

The credit institutions also claimed that declaring the FX loan gap provisions *ipso iure* null and void violated the general restriction on retroactive legislation, and not even the ECJ set out any such requirement. Moreover, there is an actual FX operation underlying FX-based loans, which inevitably results in a difference between the FX rates, and this cost must be borne by one party or the other.

The credit institutions also maintained that the settlement mechanism behind the FX loan agreements was well known at the time of the conclusion of the agreements in question and therefore each party was aware of the inherent risks in this mechanism.[41] Further down the line of this argumentation, their motion referred to the violation of their property rights. As claimed by the credit institutions, the income stemming from

[38] See Resolution 34/2014. (XI. 14.), Resolution 2/2015. (II. 2.), Resolution 7/2015. (III. 19.), Resolution 3121/2015. (VII. 9.).

[39] Act CLI of 2011 on the Constitutional Court.

[40] Cited by Resolution 7/2015. (III. 19.), para. 6.

[41] This is further supported by Gárdos I., Gondolatok a devizahiteles törvények kapcsán, (2015) (3) *MTA Law Working Papers,* https://jog.tk.hu/mtalwp/jog-jogertelmezes-gondolatok-a-devizahiteles-torvenyek-kapcsan (Last accessed: 31 December 2020).

the FX Gap Provisions constituted a material asset that was withdrawn by the FX Loan Act without any kind of compensation and redistributed to the debtors.

The complainants in their motion also challenged the FX Gap Provisions, more precisely the mandatory application of the Central Bank FX rates. According to the motion, should the FX Gap Provisions be null and void, the debt must be registered as a loan denominated in HUF, and the settlement should be adjusted accordingly.

The Constitutional Court held that all the above motions were unfounded. Concerning the unfairness of the FX Gap Provisions, the Constitutional Court referred to the 6/2013. Uniformity Decision, stating that the performance of the FX loan agreements did not require any conversion. Instead, there was a recalculation of the debt. This recalculation resulted in an additional payment obligation that lacked any underlying service; therefore, the FX Gap Provision qualified as *ipso jure* unfair. In this respect, the Constitutional Court deemed the arguments relating to the retroactive legislation irrelevant because such a referral cannot result in a situation in which numerous unfair – thus, void – provisions remain untouchable and the debtor continues to have a payment obligation.[42]

In relation to the arguments on the general restriction on retroactive legislation, the Constitutional Court again referred to the 6/2013. Uniformity Decision that deemed the Unilateral Increase Provisions to be unfair. The Constitutional Court took the view that the FX Loan Act merely elevated the interpretation of the Curia on the impugned provisions to the level of a statute.[43] Since the legal interpretative activity of the law enforcement bodies and the legislation are not directly related to the prohibition on retroactive legislation, the Constitutional Court rejected the related arguments without delivering any decision on the merits.[44]

As regards the potential violation of the right to property, the Constitutional Court highlighted that the payment obligation of the credit institutions was a direct consequence of the null and void nature of the impugned provisions. The unfair provisions – that were not analysed by the Constitutional Court on the merits – did not create any legitimate expectations, therefore they could not be subject to the protection of property rights.[45]

[42] Resolution 7/2015. (III. 19.), para. 36.
[43] Resolution 7/2015. (III. 19.), paras 38–41.
[44] Resolution 7/2015. (III. 19.), para. 43.
[45] Resolution 7/2015. (III. 19.), para. 48.

V. The credit institutions in Strasbourg: the decision delivered in the case of *Merkantil Zrt. and others*

The lawsuits initiated by the credit institutions before the Hungarian courts were dismissed without exception. Some of the former plaintiffs – including the members of the biggest Hungarian retail bank, the OTP Group – lodged an application to the ECtHR in the spring of 2015. This step appeared to be reasonable, yet unusual. The Hungarian applicants before the ECtHR are mostly natural persons for a number of reasons.

First, the Hungarian courts deliver significantly fewer decisions concerning the fundamental rights of legal entities. Since the Fundamental Law took effect in 2012, the Constitutional Court had delivered altogether 22 decisions regarding the fundamental rights of a legal person until 31 May 2020. As the exhaustion of domestic legal remedies is one of the main admissibility criteria of the ECHR, the small number of decisions inevitably resulted in fewer applications to the ECtHR. In 2015, nearly half of the cases before the Court concerned the excessive length of court proceedings,[46] while the Hungarian press mostly dealt with cases about the poor detention conditions in Hungarian prisons. Therefore, there was limited awareness among companies of this potential way of litigation. Moreover, in the case of major companies, any lawsuit to be initiated against the state is subject to careful consideration. To give some flavour to this conversation, the memory of the sectorial taxes imposed on the banks in Hungary was still vivid, and numerous other examples of the Hungarian government adopting legislation in fast-track proceedings, without any prior civil consultation, were widely known. Finally, the business planning of the banks also experienced some challenges. The reason for the confusion was that, in the event of a judgment finding a violation, the ECtHR may grant the applicant just satisfaction (instead of an indemnity). The Court had not yet published any clear formula or tool to calculate the amount of such satisfaction. The first comprehensive study on the issue was published in 2015.[47] As such, there was no guarantee that the credit institutions would receive a fair value of their lost property even with a favourable judgment.

Against this background, the application of the banks meant an exciting development for domestic legal human rights practice; besides, it was of great economic

[46] https://www.echr.coe.int/Documents/Facts_Figures_2015_ENG.pdf (Last accessed: 31 December 2020) 11.

[47] S. Altwicker-Hamori, T. Altwicker and A. Peters, Measuring Violations of Human Rights: An Empirical Analysis of Awards in Respect of Non-Pecuniary Damage Under the European Convention on Human Rights, (2016) 76 *Zeitschrift für ausländisches öffentliches Recht und Völkerrecht (ZaöRV)/ Heidelberg Journal of International Law (HJIL),* 1–51. https://doi.org/10.2139/ssrn.2631404

significance. In their application, the credit institutions referred to damage amounting to more than one hundred million EUR that was claimed to be the result of the FX Loan Act. Even though there was no assurance that the applicants would be compensated with the same amount, even a fraction of this sum could have meant a heavy burden on the state budget of Hungary.

1. The main elements of the complaints of the credit institutions

The credit institutions mainly referred to the breach of two articles of the ECHR, Article 6 on the right to fair trial, and Article 1 of Protocol 1 on the entitlement to the peaceful enjoyment of property. Since neither of the invoked rights is absolute, the applications focused on the alleged lack of legal basis and the disproportionate nature of the interference, namely the FX Loan Act and the Settlement Act.

Concerning the lawsuits initiated by the banks to rebut the unfairness presumption, and hence the alleged violation of Art. 6, the applications claimed that the Hungarian courts were restricted in terms of their power of decision. The courts could only assess whether the GTCs of the banks passed the Fairness Test, and they were not allowed to take into account other circumstances surrounding the conclusion of the FX loan agreements. As a consequence, the FX Loan Act considerably restricted the banks' right to submit evidence and their right to have a reasonable opportunity to present their case, which in turn violated the principle of equality of arms.[48] Moreover, the applications referred to the extreme deadlines that significantly undermined the chance to carry out a thorough collection and presentation of evidence.

Concerning the alleged violation of the right to property, the applicants claimed that the amounts collected from the consumers, as well as the future contractual claims under the Unilateral Increase Provisions were deemed to be a 'possession' for the purposes of Art. 1 of Protocol no. 1. This allegation itself raised numerous concerns, as it could not be assessed independently from the assessment of the lawfulness of the interference of this possession. The reason for that is this allegation required the applicants to prove that, despite the presumption introduced by the FX Loan Act, the GTCs were lawful and valid provisions. Should the GTCs have failed the Fairness Test, no possession could have been established, as invalid provisions may not give rise to contractual claims, and hence future possession. Since the ECtHR does not have the competence to assess the validity of contractual claims, the credit institutions focused on the argument that the FX Loan Act as a legal instrument is an unlawful interference, and that, before the enactment of this legislation, they had a valid contractual claim. Consequently, both the claim for having a possession and the

48 *Merkantil Zrt. v Hungary,* ECtHR 20 December 2018, 22853/15, para. 64. (the Merkantil Decision).

claim addressing the violation of the right to property depended on the lawfulness of the FX Loan Act.

Having that in mind, the credit institutions pointed out that, before 1 January 2010, the applicable Hungarian legislation did not include any provision that rendered the unilateral raise of interest rates unfair or set out conditions for raising them. On the contrary, some measures of the government, and the first judgments of the Hungarian courts delivered in FX loan cases, appeared to be tacit confirmation of the validity of the Unilateral Increase Provisions. The Old Banking Act and the relevant government decrees set out conditions that were fulfilled by the banks, and up until the 2/2012. Opinion (that introduced the Seven Principles) being issued, no legal instrument was in effect that made the interest rate-raising practice of the banks dubious. Moreover, the 2/2012. Opinion precluded the unfairness of those contractual terms that complied with the Government Decree.[49]

In addition to the above, the banks claimed that the state violated the restriction on retroactive legislation, because the FX Loan Act was applicable to GTCs in force from 1 May 2004 while, under Hungarian law, the general statute of limitation is five years. Therefore, the scope of the FX Loan Act (adopted in 2014) extended for more than ten years, reopening claims concerning instalments that were already paid by the debtors.[50] Finally, the banks reiterated that the FX Loan Act violated their procedural rights and thus infringed Art. 6 of the ECHR.[51]

To present the big picture behind the legislation, the credit institutions also submitted that the actual reason behind the financial crisis in Hungary at that time was that, since 2008, the HUF had drastically depreciated against other currencies (in particular against the CHF and the EUR) and this could not have been foreseen. Moreover, before the financial crisis, the debtors of the FX loan agreements were in a more favourable position than those of HUF-based loan agreements, and some measures adopted during the crisis also provided significant assistance to the consumers (such as the early repayment scheme). In sum, the existence of Unilateral Increase Provisions was not the root cause of the crisis. Nevertheless, it was the applicants that were obliged to pay back more than a hundred billion forint to consumers.[52]

2. The *Bárdi and Vidovics* case as a precedent

Shortly before receiving the applications of the credit institutions, the ECtHR had already faced the problem of the Hungarian FX Loan Agreements – and the special features of

[49] Merkantil Decision, para. 87.
[50] Merkantil Decision, para. 88.
[51] Merkantil Decision, para. 89.
[52] Merkantil Decision, para. 90.

the FX Loan Act – from the debtors' perspective. The applicants in the *Bárdi and Vidovics* case[53] were two natural persons who concluded their FX Loan Agreements in 2006. When the crisis broke out, the applicants turned to the Hungarian courts and requested them to establish the invalidity of their FX Loan Agreements. While the litigation before the domestic court was in progress, the National Assembly adopted the FX Loan Act, the provisions of which were applicable to the litigation by the applicants, too.

The applicants found that this procedure violated their right to a fair trial as protected by Art. 6 of the ECHR, because it was the National Assembly that enacted legislation determining how their disputes were to be resolved. It, by definition, lacks several guarantees of a civil procedure, i.e. it is not independent of the legislative and executive authorities, several procedural safeguards are not guaranteed in its proceedings, and legislative actions are not amenable to appeal. Therefore, the National Assembly could not qualify as a tribunal, so it was in no position to decide on the dispute.[54]

In its decision, the ECtHR confirmed that the FX Loan Act was able to influence the outcome of the disputes before the Hungarian courts. However, the Court pointed out that the state was not party to these disputes. The sole purpose behind the FX Loan Act was to ensure that all claims relating to the same subject matter could be resolved in a prompt and comprehensive manner, avoiding any inconsistency in case-law and also overburdening the judicial system.[55] Moreover, the FX Loan Act did not apply to one specific legal procedure; instead, its scope was of a general nature, including all relevant FX loan agreements (whether challenged before a court or not). The Court found that the FX Loan Act merely implemented the Uniformity Decision of the Curia that gave guidance on resolving the issues of the FX loan agreements. For this reason, the applicants could have foreseen a reaction by the National Assembly. There was no reason for the ECtHR to assume that such guidance would not have had to be followed by the domestic courts in any case, even without the enactment of the FX Loan Act. Consequently, the decision concluded that the interference with the right to fair trial was of a much less drastic nature and held the applications manifestly ill-founded.[56]

This decision contained numerous bad signals for the credit institutions. First, the strict procedural rules set out by the FX Loan Act seemed to be in conformity with Art. 6 of the ECHR. Second, it appeared that, when it came to the assessment of the interference (and the potential arbitrary nature of the FX Loan Act), the Court would attach great significance to the fact that the state did not seem to benefit from the FX Loan Act; it was not a party to the FX loan litigation.

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[53] *Bárdi and Vidovics v Hungary,* ECtHR 19 December 2017, 27514/15 and 13876/16 (the Bárdi-Vidovics Decision).

[54] Bárdi-Vidovics Decision, para. 23.

[55] Bárdi-Vidovics Decision, paras 28 and 31.

[56] Bárdi-Vidovics Decision, paras 31–32.

3. The main elements of the decision in the *Merkantil* case

Although the ECtHR had already assessed the details of the FX Loan Act in the *Bárdi and Vidovics* case, it did not decide on the applications of the banks until one year later. The Court did not unify the proceedings initiated by the different banks, so the decisions were published on separate dates at the end of 2018 and in the beginning of 2019. The first decision was delivered in the case of *Merkantil Zrt and others v Hungary* on 20 December 2018 (the Merkantil Decision).

The panel consisted of seven judges who held, unanimously, that the complaint was inadmissible. Even so, the panel analysed in great length the articles in question, namely the right to fair trial (Art. 6) and the right to the peaceful enjoyment of property (Art. 1 of Protocol No. 1), concluding as follows.

Concerning the principle of equality of arms, the ECtHR highlighted thatthe tight time limits and the strict procedural rules were applicable to all parties to the litigation, and did not result in any imbalance.[57] Having said that, the Court concluded that these arguments related to access to court (instead of the equality of arms) and continued its assessment in this context.

As regards this specific remedy, the FX loan litigation, the ECtHR held that these procedures were of a *sui generis* nature, designed to address a pressing social problem. As numerous FX loan proceedings were suspended at that time, and many others were anticipated, the Court became convinced that the FX Loan Act aimed at preventing a backlog of cases and pursued the legitimate aims of consumer protection and efficient administration of justice. Although the time limits were indeed tight and required extensive efforts from the banks, they were not impossible to meet. And since it was the banks that launched the proceedings, they must have had prepared themselves for the strict rules and arranged heir resources accordingly.

Concerning the interference by the legislature in the administration of justice and the presumption of unfairness, the Court pointed out that there was no general prohibition on retroactive legislation. The 2/2014. Uniformity Decision of the Curia contained an unambiguous guidance for the courts on the FX loan litigation, and the ECtHR saw no reason to assume that such guidance would not have had to be followed by the domestic courts in any case, even without the enactment of new legislation. The purpose of the FX Loan Act was not to determine the outcome of the proceedings in favour of the state, but to ensure consumer protection and public interest in general.[58] Moreover, the credit institutions must have been aware of the potentially unfair nature of the GTCs in question, because the relevant piece of EU legislation, the Unfair Terms Directive, became applicable to Hungary on 1 May 2004.[59]

[57] Merkantil Decision, para. 70.
[58] Merkantil Decision, paras 77–78.
[59] On this day Hungary joined the European Union.

Concerning the presumption of the unfairness of the GTCs, the ECtHR reiterated that presumptions of fact or of law operated in every legal system. Since the credit institutions had the opportunity to attempt to rebut the presumption, it was eventually for the domestic courts to determine whether the GTCs complied with the Fairness Test. The applicants had the opportunity to submit evidence and arguments, and the standard of proof was not set excessively high. As the ECtHR put it, nothing in the file suggested that the Hungarian courts had assessed the arguments submitted to them arbitrarily.

As a conclusion, the Court found that the FX Loan Act and its effects did not appear to violate Art. 6 of the Convention. In this regard, the ECtHR deemed the applications manifestly ill-founded and rejected the complaints.[60]

Concerning the complaints relating to Art. 1 of Protocol No. 1 of the Convention, the ECtHR put forward two assumptions. First, the instalments and the future instalments paid by the consumers in line with the GTCs qualified as the 'property' of the banks, therefore they fell within the scope of Art. 1 of Protocol No. 1 of the Convention. Second, the application of the FX Loan Act resulted in an interference with the applicants' right to property.[61]

On the above basis, the ECtHR applied its ordinary framework of assessment, and it carried out the so-called three rules analysis.[62] In this framework, the Court considered whether the interference was lawful, whether it served a legitimate aim and whether it was proportionate. The ECtHR responded to the first two questions with ease. The decision found the interference lawful because it was realised through a legal act, the FX Loan Act. Furthermore, the FX Loan Act appeared to have a legitimate aim. With reference to the explanatory memorandum to the FX Loan Act and the Constitutional Court's decision, the ECtHR concluded that the impugned measures were aimed at preventing a backlog in the domestic courts and at protecting customers. The decision also highlighted that states enjoy a wide margin of appreciation when legislating on the implementation of social and economic policies. The ECtHR found that the FX Loan Act had a reasonable foundation; therefore, it would respect the Hungarian legislature's judgment as to what was 'in the public interest'.

The remaining question was whether Hungary struck a fair balance between the general interest of the community and the need to protect the individual's fundamental rights.

After presenting the general economic background, the Court addressed the arguments of the complainants. As to the validity of the GTCs, the ECtHR accepted

[60] Based on Art. 35(4) read in conjunction with Art. 35(3)a) of the Convention.

[61] Merkantil Decision, paras 96–97.

[62] M. Carss-Frisk, *The right to property – A guide to the implementation of Article 1 of Protocol No. 1 to the European Convention on Human Rights,* (Human Rights Handbooks 4) (Council of Europe, 2001), https://rm.coe.int/168007ff4a (last accessed: 31.12.2020.) 21–26.

the state's submission that the FX Loan Act did not create new grounds of invalidity but merely codified the uniform judicial practice concerning section 209(1) of the old Civil Code. Although the decision confirmed that the Seven Principles appeared for the first time in the 2/2012. Opinion, delivered in 2012, the Court noted that these principles concerned those GTCs that would have qualified as invalid pursuant to the Unfair Terms Directive. Therefore, the complainants could not have any reasonable expectation on their part that the GTCs in the FX Loan Agreements concluded since 1 May 2004 and not complying with the Seven Principles would be considered fair. The decision noted the arguments that referred to the fact that the GTCs qualified as fair pursuant to both the old Banking Act and the Government Decree, and the 2/2012. Opinion itself precluded the invalidity of those terms that complied with the applicable legislation. The ECtHR pointed back to the domestic courts, highlighting that it is in the first place for the domestic authorities, notably for the courts, to interpret and apply the domestic law. Moreover, the ECtHR held that the old Banking Act did not provide for an unconditional right to unilateral amendments, and the banks should have taken into account the principles of good faith and fairness.

The Court also repeated that the FX Loan Act allowed for the potential rebuttal of the unfairness presumption. Furthermore, at the time of the adoption of the FX Loan Act, numerous cases of litigation were suspended that were likely to have led to the same result as contained in the FX Loan Act, i.e. the domestic courts would have found the GTCs unfair. The credit institutions merely had to reimburse or set off excess consumer payments arising from the unfair unilateral amendments. Therefore, the ECtHR concluded that the FX Loan Act did not upset the balance which must be struck between the protection of the applicant companies' rights and the public interest. As a consequence, the Court found this part of the application manifestly ill-founded, too, and rejected the complaints.

VI. Critical analysis of the decision of the ECtHR

Needless to say, the founding fathers of the ECHR hardly dreamed of drafting a text that would provide a last resort for financial institutions suffering an extra burden during an economic crisis. Even so, the scope of certain rights, notably the right to property, has always included legal persons, too; see in this regard Art. 1 of Protocol No. 1 and Art. 34 of the Convention. This notion is in harmony with the preamble of the ECHR, stating that fundamental freedoms strengthen the foundation of justice and peace in the world, and they are best maintained by, among others, an effective political democracy. This formulation suggests that the preamble puts a great emphasis on the rule of law in comparison to the ideals of humanity and the value of human beings and humankind.[63]

However, the decision of the ECtHR contains several elements that appear to undermine the objectives of the notion of the rule of law. This article argues that, notwithstanding the fact that the FX loan agreements contributed to the escalation of a grave financial crisis in Hungary, the measures aiming at economic recovery must comply with the standards of fundamental rights.[64] On this basis, the article continues to consider that certain allegations or lines of arguments in the decision of the ECtHR do not reflect a proper understanding of the underlying Hungarian legislation, or may be questioned from a European Union law perspective.

1. The missed opportunities of the Merkantil Decision

Decisions of the ECtHR that find an application manifestly ill-founded have often been criticized for lacking a proper reasoning (or a reasoning at all).[65] This practice is not only at odds with the ECtHR's own standards, but also makes it very difficult to grasp what standards of the 'manifestly ill-founded nature' had been missed in a specific case.

By contrast, the Merkantil Decision stands out due to the excessive length of the reasoning. The ECtHR, by way of a panel consisting of seven judges,[66] after considering the observations of both the government and the applicants and after three and a half years from the submission of the complaints,[67] delivered a 37-page decision that held the application manifestly ill-founded. The lengthy legal analysis makes it already questionable whether the case could have been *manifestly* ill-founded. Further, it what additional assessment criteria should have been included to make a judgment is also uncertain (the decision does not refer to any other factor that should have been considered). Consequently, the Merkantil Decision hardly gives any response to why the ECtHR decided in favour of inadmissibility instead of delivering a judgment.

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63 P.H. van Kempen, The Recognition of Legal Persons in International Human Rights Instruments: Protection Against and Through Criminal Justice?, in M. Pieth and R. Ivory (eds), *Corporate Criminal Liability,* (Springer, The Netherlands, 2011) 360. https://doi.org/10.1007/978-94-007-0674-3_14

64 This principle is frequently echoed on various international fora that discuss the recovery from the COVID-19 crisis: see for example the report of the UN Secretary General (2020): https://www.un.org/sites/un2.un.org/files/un_comprehensive_response_to_covid-19_june_2020.pdf (Last accessed: 31 December 2020).

65 J. Gerards, Inadmissibility Decisions of the European Court of Human Rights, (2014) 14 (1) *Human Rights Law Review,* 148–158. https://doi.org/10.1093/hrlr/ngt044

66 Inadmissibility decisions are most frequently decided by a single judge or a three-judge panel.

67 The application of Merkantil Zrt. is dated 4 May 2015, and the decision was published on 20 December 2018.

The Merkantil Decision also leaves some other pertinent legal questions unanswered. First, the ECtHR took as a starting point that the sums paid back by the credit institutions to the consumers were the 'property' of the credit institutions and did not evaluate the arguments of the parties in detail. The lack of analysis may cause some dismay.

The ECtHR has a solid practice under which property claims that have a sufficient basis in national law qualify as 'asset' falling within the scope of Art. 1 of Protocol No. 1.[68] The concept of 'legitimate expectation' applies with regard to these claims, as this notion also relates to the way in which the claim qualifying as an 'asset' would be treated under domestic law and in particular to reliance on the likelihood that the established case-law of the national courts would continue to be applied in the same way. When it comes to property claims that are based on contract, the Court appears to take a more cautious approach. Although in its decision on S. v. the United Kingdom, the ECtHR recognised that property may include rights having an exclusively contractual origin, it remained unclear whether the contract itself could be a sufficient basis for the claim. In the case of the claims of certain building societies concerning the interest paid to their investors, the ECtHR could not express any conclusive view on the existence of 'possessions', because the applicants had not secured a final and enforceable judgment in their favour.[69] It also remained unclear whether such a precondition would prevent the enforcement of future claims or not. The Court held in many cases that not only the person's existing possessions should be viewed as property, but it also includes claims which the petitioner lawfully expects to be fulfilled in the future.[70] The justification behind the protection of legitimate expectations is that 'the law should protect the trust that has been reposed in a statutory undertaking made by legislation'. Nevertheless, the cases concerning future claims related to those that had a legislative basis (instead of a contractual one).

In the present case, the Court had to assess claims that had an exclusively contractual origin; however, the exact amount of these claims could not have been quantified at the time of the conclusion of the FX Loan Agreements and the credit institutions did not have any final and enforceable judgment in their favour either. To add one more layer to the problem, these claims were based on contractual provisions that were deemed invalid under the FX Loan Act. To challenge this presumption, the credit institutions could not carry out comprehensive litigation that took account of every relevant circumstance; the national courts could only apply the Fairness Test. If the ECtHR concluded that the claims of the credit institutions qualified as property,

[68] See for example *Kopecký v. Slovakia,* ECtHR 28 September 2004, 44912/98, *Plechanow V. Poland,* ECtHR 7 July 2009, 22279/04, *N.K.M. v. Hungary,* ECtHR 14 May 2013, 66529/11.

[69] *National & Provincial Building Society, Leeds Permanent Building Society and Yorkshire Building Society v The United Kingdom,* ECtHR 23 October 1997, 21319/93, 21449/93 and 21675/93.

[70] *S v United Kingdom,* ECtHR 13 December 1984, 10741/84.

would that have meant that the Unilateral Increase Provisions were indeed valid provisions, and thus the FX Loan Act would have qualified as unlawful? Could the ECtHR set out any extra requirements for future claims having contractual origins in order to qualify as possessions? Replying to these questions could have significantly contributed to the improvement of the practice of the Court.

2. Assessment of the requirement of fair trial

Regarding the reference to the requirement of fair trial, the ECtHR reiterated that Art. 6 was not an absolute right, since adopting a procedural nature, *ab ovo,* called for regulation by the state, which enjoys a certain margin of appreciation in this regard.[71] However, neither the impugned provisions nor their application should prevent litigants from making use of an available remedy.[72]

Nevertheless, after sketching this background, the Court appears to have refused to consider whether a procedure with a specifically limited scope could be suitable for the applicants to make use of an available remedy. In an ordinary civil procedure on the validity of a contractual provision, the court takes into account all relevant circumstances surrounding the conclusion of the contract. In this case, however, the national courts could assess only whether the GTCs of the credit institutions met the Fairness Test. In defence of this procedure, one could argue that a failure to fulfil even one criterion of the Fairness Test would result in such a grave defect that the contract could no longer qualify as valid, and thus the assessment of any other circumstance is unnecessary. However, this argument is contradicted by the fact that the FX Loan Act applies only to FX Loan Agreements; therefore, no other type of loan agreements is subject to the Fairness Test (although Unilateral Increase Provisions frequently appeared in other civil contracts).

Based on the above, it could have been worth having a longer analysis of how the FX Loan Act did not prevent the applicants from asserting their civil rights[73] and to have a clear, practical and effective opportunity to challenge the FX Loan Act.[74]

With reference to the judgment in the *Bárdi and Vidovics* case, the Court highlighted that the purpose of the FX Loan Act was clearly not to determine the outcome of the proceedings in favour of the state,[75] but to ensure consumer protection and public interest in general. The Merkantil Decision did not consider the potential issue that the outcome, in itself, is determined, and the FX Loan Act restricts the

71 Merkantil Decision, para. 70.
72 *Tence v. Slovenia,* ECtHR 31 May 2016, 37242/14 and the case law referred to therein.
73 See in this regard *Beles and others v. the Czech Republic,* ECtHR 12 November 2002, 47273/99, para. 49.
74 *Geouffre de la Pradelle v. France,* ECtHR 16 December 1992, 12964/87, para. 34.
75 See by contrast *Maggio and Others v. Italy,* ECtHR 31 May 2011, 46286/09.

discretion of the Hungarian courts. The predetermined nature of the proceedings is illustrated by the fact that all 73 procedures aiming at rebutting the Unfairness Presumption were dismissed by the courts.

The Court also highlighted that, given the interconnections with EU law, the applicants were aware of the potentially unfair nature of the impugned provisions, because the GTCs were already to be regarded as unfair under the Unfair Terms Directive. The relevant part of the decision appears to suggest a certain duty of care, but the ECtHR did not elaborate upon such a duty, but merely underlined the role of EU law. This approach raises significant concerns, as detailed below.

3. Reference to EU law in the decision of the ECtHR

The Merkantil Decision makes an interesting statement, claiming that the Unfair Terms Directive became applicable to Hungary as of 1 May 2004. To say the least, this statement is not in harmony with the concept of directives under EU law.

Directives of the European Union are not directly applicable in the Member States, and their direct effect is restricted, too. Directives are addressed to the Member States, and it is up to the Member State to choose the most appropriate form and method of implementation.[76] It was precisely this discretion, left to the Member States, that was why the enforceability of unimplemented directives was surrounded by many questions.

As the documents of the infringement procedure 20 072 499 suggest, the Hungarian legislator failed to implement the Unfair Terms Directive in its entirety up until 22 May 2009. It does not mean that this directive lacked any effect in the Hungarian legal order. The European Court of Justice, in its practice, developed a number of reasons that would underpin the vertical direct effect of the directives.[77] The first argument is that, as set out by the TFEU, a directive shall be binding as to the result to be achieved (which does not mean that natural persons may refer to them during ordinary litigation). However, under Art. 267 of the TFEU, the Court of Justice of the European Union shall have jurisdiction to give preliminary rulings concerning the validity and interpretation of acts of the institutions, bodies, offices or agencies of the Union, which includes the directives, too. This argument is further corroborated by the conclusion of the ECJ that goes as follows: where the EU authorities have, by directive, imposed on Member States the obligation to pursue a particular course of conduct, the useful effect of such an act would be weakened if individuals were prevented from relying on it before their national courts and if the latter were

[76] Treaty on the Functioning of the European Union (the TFEU), Art. 288.

[77] P. Craig and G. de Búrca, *EU Law: Text, Cases and Materials,* (7th ed., OUP, Oxford, 2020) 237–238. https://doi.org/10.1093/he/9780198856641.001.0001

prevented from taking it into consideration as an element of EU law. Consequently, the ECJ deemed it necessary to examine, in every case, whether the nature, general scheme and wording of the provision in question can have direct effects on the relations between Member States and individuals.[78] The third reason for establishing the direct effect of directives highlights the omission of the Member State for failing to implement a certain directive. On this basis, a Member State which has not adopted the implementing measures required by the directive in the prescribed periods may not rely, as against individuals, on its own failure to perform the obligations which the directive entails.[79]

By contrast, the concept of the horizontal direct effect was explicitly rejected by the ECJ. As set out in the judgment in the *Marshall* case,[80] the founding treaties make it clear that the binding force of directives shall exist only in relation to each Member State to which it is addressed. Further arguments can also be made on the basis of legal certainty. As Advocate General Jacobs puts it in his opinion in the *Unilever* case, it would be disproportionately severe if a national court was obliged to find a breach of contract on the basis of disregarding a directive (in that case, a directive prescribing to notify a technical regulation).[81] As per the opinion, the horizontal direct effect of the directive would bring numerous uncertainties including the appropriate remedies for the breach of contract or the applicable legal regime that replaces the disapplied national measures.[82]

Against this backdrop, to strengthen the horizontal effect of directives, the ECJ developed the requirement of harmonious interpretation.[83] According to this concept, in domestic litigation involving an EU directive, national courts should interpret national law in the light of the wording and the purpose of that directive. However, this requirement applies to the interpretation of the existing national law, hence it does not replace the proper implementation of a directive.

Therefore, this article concludes that the expectation of the Court, which required economic operators to take into account an unimplemented directive, is based on a gross misinterpretation of the underlying EU law. The omission by the state may under no circumstances be imputed to the credit institutions.

[78] Judgment of 4 December 1974, *Van Duyn v. Home Office,* 41-74, ECLI:EU:C:1974:133, para. 12.
[79] Judgment of 5 April 1979, *Pubblico Ministero v. Tullio Ratti,* 148/78, ECLI:EU:C:1979:110, para. 22.
[80] Judgment of 26 February 1986, *Marshall v. Southhampton and South-West Hampshire Area Health Authority (Teaching),* 152/84, ECLI:EU:C:1986:84, para. 48.
[81] AG Opinion of 27 January 2000, *Unilever,* C-443/98, ECLI:EU:C:2000:57, para. 112.
[82] P. Craig, The Legal Effect of Directives: Policy, Rules and Exceptions, (2009) 34 (3) *European Law Review,* 349–369.
[83] Judgment of 10 April 1984, *Von Colson and Kamann,* C-14/83, ECLI:EU:C:1984:153, para. 26.; Judgment of 13 November 1990, *Marleasing SA,* C-106/89, ECLI:EU:C:1990:395, paras 7–8.

4. Violation of the right to property

As outlined above, the ECtHR did not assess in detail whether the payments already made and to be made under the Unilateral Increase Provisions and the FX gap provisions constitute 'property'. Instead, it presumed that the credit institutions were deprived of their property and carried on with the following steps of the legal analysis.

***a)* The lawfulness of the interference**
Concerning the lawfulness of the interference, the ECtHR correctly recognised that the assessment of the retroactive application of the FX Loan Act was strongly linked to the validity of the impugned provisions (i.e. the Unilateral Increase Provisions and the FX Gap Provision). When carrying out the analysis, the Court applied a dual approach.

First, the ECtHR refers to the decision of the Hungarian Constitutional Court, according to which the FX Loan Act had merely codified the interpretation of fairness, developed and made mandatorily applicable in the practice of the European and domestic courts.[84] Second, after this conclusion, the ECtHR carried out its own assessment, and correctly confirmed that the Fairness Test first appeared in the 2/2012. Opinion. This – relatively late – appearance did not prove to be decisive for the Court: the ECtHR again reiterated that those GTCs which, contrary to the requirement of good faith, caused a significant imbalance in the parties' rights and obligations to the detriment of the consumer were already to be regarded as unfair under the Unfair Terms Directive. The precise content of the principle of good faith was to be interpreted by the domestic authorities and could go beyond the Unfair Terms Directive; it could thus naturally involve a consideration of circumstances that later became the Seven Principles.[85] The applicants failed to prove that the GTCs in the FX Loan Agreements concluded since 1 May 2004 and not complying with the Fairness Test would be considered fair by the domestic courts. In this respect, the ECtHR specifically referred to the requirement of plain and intelligible language that is explicitly contained in the Unfair Terms Directive.

The Merkantil Decision again applied a somewhat unique approach to EU law as it expected the credit institutions to comply with a directive to which they are not addressees. Moreover, the Merkantil Decision appears to be based on a selective reading of the Unfair Terms Directive, as it did not take into consideration the other relevant provisions of that directive. In this regard, the Court overlooked the fact that, when it comes to the assessment of the validity (and fairness) of a contractual

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[84] Merkantil Decision, para. 102.
[85] Merkantil Decision, para. 103.

provision, the Unfair Terms Directive prescribes that every relevant circumstance shall be considered.[86] The FX Loan Act clearly disregarded this provision.

It is not disputed here that the concept of contractual invalidity and unfairness cannot be regulated extensively in a legal act, and the courts must be prepared to apply the principles indicating unfairness in light of the changing circumstances of economic life. Even so, it is telling that in the six-eight years preceding the FX loan crisis, neither the regulatory authorities nor the domestic courts held the impugned provisions unfair.[87] As the retail lending sector was already heavily regulated segment, the credit institutions could have reasonably expected the financial watchdogs to speak up in the event of any contractual provisions that would allow severe financial abuse. In sum, the Merkantil Decision expected the credit institutions to prove a negative claim (i.e. that the Unilateral Increase Provisions and the FX Gap Provisions were not unfair), it however disregarded the absence of any corresponding court judgments or resolutions by the financial regulatory authorities.

***b)* The legitimate aim of the FX Loan Act**

Concerning the legitimate aim of the FX Loan Act, the Merkantil Decision did not result in any novelties. The applicants argued that the FX Loan Act in fact aimed at favouring the debtors of the FX loan agreements without taking into account the fact that the increase in repayment instalments had mostly been attributable to the changes in FX rates resulting from the crisis, rather than to unilateral increases in interest rates and fees applied by the banks.[88]

It goes without saying that the FX Loan Act helped consumers to receive a substantial amount from the banks without the need to go to the courts. Furthermore, even in the absence of the FX Loan Act, the Curia's guidance (i.e. the 2/2012. Opinion and the 2/2014. Uniformity Decision) would have resulted in judgments favourable to consumers. It is disappointing however that, unlike in other cases,[89] the ECtHR did not take into account the role of the state in the escalation of the crisis. If the general interest is at stake, it is incumbent on the public authorities to act in good time and in an appropriate and consistent manner. However, as it is apparent from the growing popularity of the FX loan products during the 2000s, the Hungarian state even facilitated the spread of these products instead of introducing more specific regulation. In addition, the ECtHR failed to assess whether it was legitimate to deprive the banks of amounts that were paid on a basis of a fair interest rate. It is self-evident that the

[86] Unfair Terms Directive, Art. 4(1).

[87] Although the fact that all litigation claiming the rebuttal of the unfairness presumption was dismissed suggests that the matter is relatively simple.

[88] Merkantil Decision, para. 90.

[89] *Fener Rum Erkek Lisesi Vakfi v. Turkey,* ECtHR 9 January 2007, 34478/97.

global financial crisis affected financial institutions, too, and induced the banks to raise their interest rates.

The above submissions proved to be in vain. When a state measure appears to serve multiple purposes, the ECtHR tends to focus on the aim that it finds legitimate and disregards any additional results.[90] As summarised in the *Merabishvili* case: 'Even when it excludes some of the cited aims, if it accepts that an interference pursues at least one, it does not delve further into the question and goes on to assess whether it was necessary in a democratic society to attain that aim'.[91]

Traditionally, the ECtHR leaves the states with a wide margin of appreciation when it comes to balancing the interest of the national economy and that of private persons.[92] On this basis, the Court set out that it respected the legislature's judgment as to what constituted 'public interest' unless that judgement was manifestly without reasonable foundation.[93] This test means a lower standard for the state.[94] Applying this test to the actual circumstances, the Court decided that it could not substitute its own assessment for that of the domestic courts, and it would only assess the case further if the aim pursued by the FX Loan Act had proved to be manifestly unreasonable. Therefore, only the assessment of the proportionality remained from the three-rule analysis.

***c)* The assessment of the proportionality of the FX Loan Act**

Based on the jurisprudence of the Court, the wide margin of appreciation left to the state entailed that the ECtHR would apply a lower standard when assessing the proportionality of a state measure.[95] This lower standard means that the ECtHR aims at striking a 'fair balance' between the general interest of the community and the need to protect the individual's fundamental rights, and the requisite balance will not be found if the person concerned has had to bear an 'individual and excessive burden'.[96] In the case of claims relating to the deprivation of property, the assessment often boils down to looking at the compensation that the victim received.[97]

The ECtHR delivered numerous judgments that established a violation of Article 1 of Protocol 1 because the interference with that right caused an individual and excessive burden, even if the state measure in question was introduced amidst a

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90 J. Gerards, *General Principles of the European Convention on Human Rights,* (CUP, Cambridge, 2013) 226.
91 *Merabishvili v. Georgia,* ECtHR 28 November 2017, 72508/13.
92 *James and Others v. United Kingdom,* ECtHR 21 February 1986, 8793/79; *Animal Defenders International v. United Kingdom,* ECtHR 22 April 2013, 48876/08.
93 Merkantil Decision, para. 99.
94 See for example *Pressos Compania Naviera S.A. and Others v. Belgium,* ECtHR 20 November 1995, 17849/91. or *James and Others v. United Kingdom,* ECtHR 21 February 1986, 8793/79.
95 Gerards, *General Principles of the European Convention on Human Rights,* 243.
96 Merkantil Decision, para. 98.
97 W. A. Schabas, *The European Convention on Human Rights – A commentary,* (OUP, Oxford, 2015) 976.

severe economic situation.[98] The Merkantil Decision however did not include a lengthy analysis assessing the proportionality, either. The ECtHR referred to three main circumstances: the high number of the FX loan cases in the courts, the fact that the banks did have the opportunity to challenge the Unfairness Presumption and the fact that the banks only had to repay the amounts incurred under the invalid contractual provisions.[99] The ECtHR failed to address the fact that, with regard to a substantial part of the repaid amounts, the statutory limitation period had already expired. Furthermore, the decision did not mention the compensation of those consumers that had already repaid the entire amount of their debt. In sum, the ECtHR broadly measured the burden on the banks and the interference against the social pressure and did not consider several circumstances that had led to this pressure.

VII. Conclusions

The factual background behind the Merkantil Decision is composed of economic, social and legal measures and processes. It is a rather complex process to trace the origins of the Hungarian FX loan crisis.

Following the change in 1989, and during the preparation for joining the European Union, Hungary had gradually removed the barriers relating to financial operations in foreign currencies. The Hungarian credit institutions decided to increase their retail portfolio and launched more and more new products in order to compete effectively for the consumers. Loan products denominated in a foreign currency (most notably in CHF) were by far the most popular offers, since their interest rates were significantly lower than those of HUF-denominated loans. In parallel, the construction of new apartments increased, and consumers' apartments often served as a collateral to these FX loan agreements.

In comparison to this rapid development of innovative financial products, the level of financial consumer protection remained low. Neither the financial watchdog, nor the legislature seemed to expect a bubble to grow, and consumers concluded their FX loan agreements without any specific guarantees nor under dedicated regulation. The global financial crisis and the drastic depreciation of the HUF against foreign currencies resulted in the bankruptcy of a great number of people.

From a legal perspective, retail financing is a regulated area and, in addition to compliance with the sectoral regulations, loan agreements must comply with the general Hungarian contractual provisions, including those regulating fairness and

[98] *Scollo v. Italy,* ECtHR 28 September 1995, 19133/91.; *Hutten-Czapska v. Poland,* ECtHR 19 June 2006, 35014/97; *Béláné Nagy v. Hungary,* ECtHR 13 December 2016, 53080/13.

[99] Merkantil Decision, paras 109–110.

validity. These general contractual provisions partly serve the implementation of the corresponding EU law: the Hungarian Civil Code has fully contained the provisions of the Unfair Terms Directive since 22 May 2009.

However, the 2/2012. Opinion, the Uniformity Decision and the FX Loan Act set out specific principles that became the Farness Test and were applicable retroactively, from 1 May 2004. In addition to this, while the banks were allowed to attempt to rebut the Unfairness Presumption introduced by the FX Loan Act, none of the litigation brought by them proved to be successful. As a result, credit institutions repaid more than one hundred billion forint to consumers. The FX Loan Act thus resulted in a great financial loss to the banks, and the cost of litigation to rebut the Unfairness Presumption was added to that.

This article concludes that the FX Loan Act attempted to address an actual social crisis and, while doing so, it applied a highly technocratic perspective, and focused on the contractual voidness of certain provisions. The state kept the legal dispute in a horizontal relation (i.e. between the banks and the consumers) and, instead of providing aid to consumers, it made the credit institutions compensate the debtors. After the exhaustion of domestic remedies, the banks turned to the ECtHR to assess the lawfulness of a state measure that did not expropriate any property; instead, the measure put a significant payment obligation on the banks *vis-à-vis* consumers.

This type of measure is part of a subcategory within the main category of crisis management measures in general. The relevant jurisprudence of the ECtHR[100] is consistent when setting up the framework of the analysis: states enjoy a wide margin of appreciation in cases concerning the national economy, and the domestic authorities are better placed to assess such measures, assuming the measures in question are not manifestly unreasonable.

In the present case, the FX Loan Act set out how the banks should have behaved in their long-term contractual relationships since 1 May 2004. Given the retroactive effect of this law, the ECtHR was expected to pay close attention to the lawfulness of the measure, and to the foreseeability of this legislation. A measure interfering with a fundamental right must meet quality requirements, such as complying with the rule of law and preventing arbitrariness.

This article finds that the Merkantil Decision failed to include this meticulous assessment. In most parts of the decision, the ECtHR referred back to the national authorities, and where not, it made statements that are not accurate from an EU law perspective (see the parts on the direct horizontal effect of the Unfair Terms Directive). Moreover, the 'fair balance test' applied by the ECtHR when assessing the

[100] *James and Others v. United Kingdom,* ECtHR 21 February 1986, 8793/79, or specifically concerning the financial crisis in 2008: *Da Conceição Mateus and Santos Januário v. Portugal,* ECtHR 8 October 2013 62235/12 and 57725/12.

proportionality of the FX Loan Act lacked crucial factual elements and circumstances. Although the 'fair balance test' does not entail reweighing the interests in cases where the state enjoys a wide margin of appreciation,[101] the Court usually pays attention to any deficiencies of a state measure in question, including the potentially arbitrary nature thereof. In this case, the inaction of the financial authorities and the legislator during the climax of the conclusion of the FX Loan Agreements, as well as the repayment of instalments that were based on fair interest rates are factual elements that question the foreseeability of the FX Loan Act and must have been taken into account when assessing the proportionality of the FX Loan Act.

The history of the Hungarian FX loan crisis has not come to an end yet. There are several cases pending both before the Hungarian courts and the European Court of Justice even today. Given the significance of the crisis, one could have expected the ECtHR to deliver a judgment in which it responded to the fundamental right aspects of the management of this crisis. However, while the ECtHR did deliver a lengthy decision, it did not carry out an in-depth review. This article aimed at outlining both the missing opportunities for the ECtHR, as well as the flaws of the decision. Since none of the applicants turned to the Great Chamber, this line of litigation ended at the admissibility phase. In any case, one could hope that this fiasco does not discourage economic players from turning to Strasbourg in the event of any potential violation of fundamental rights. The doors of the European Court of Human Rights are open to every legal subject, including corporations, too.

101 Gerards, *General Principles of the European Convention on Human Rights,* 244.