REQUEST FOR A PRELIMINARY RULING (C-212/20)

in the subject of consumer mortgage loans denominated and indexed to

Swiss franc (CHF) - POLAND

- SUMMARY OF POLISH BANK ASSOCIATION'S WRITTEN OBSERVATIONS

1. SUBJECT MATTER AND QUESTIONS REFERRED FOR A PRELIMINARY RULING

1. In May 2020 the District Court for Warsaw-Wola in Warsaw referred further questions concerning the interpretation of the provisions of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts (**"Directive 93/13"**). The case was filed in the Court of Justice of the European Union under the signature C-212/20.

2. The dispute before the referring court concerns a mortgage loan agreement indexed to Swiss franc for residential purposes, concluded in 2008. In the rationale of the request for a preliminary ruling it was indicated that the borrowers understood the contractual terms concerning the exchange rate ("**conversion clauses**"), which referred to the rate from bank's exchange rate table, as a reference to the current market rate. However, they did not have a precise position on what the market rate meant, for example, they pointed to the average rate published by the National Bank of Poland. The defendant bank also understood the conversion clauses contained in the loan agreement as authorizing it to determine the exchange rate only within the scope of the market rate. The defendant bank claimed in the proceedings that the rates were determined at the market level.

3. In the light of the abovementioned circumstances, the referring court has doubts:

   a) whether the so called conversion clause (i.e. a clause referring to exchange rates specified in bank's exchange rate table) must be formulated in an unequivocal manner, i.e. algorithmic in the view of the referring court? The national court asks whether the clause must enable the borrower to calculate on his own the rate applicable to each conversion operation, whether a provision that provides for a market rate to be applied is also admissible (**first question**)?

   b) whether it is possible to interpret the conversion clause as meaning that the bank's "arbitrariness" in determining the exchange rate table will be restricted by an (pro-consumer) interpretation by assuming that, instead of an "arbitrary" exchange rate, the bank is obliged to determine the exchange rate at a market level, especially where both parties had the same understanding of contractual provisions or where the consumer was not interested in the disputed provision, in particular where he did not familiarize himself with the content of the contract at all (**second question**)?

4. Regardless of whether to link this problem with the issue of unequivocality (as the referring court does) or not, the question of whether a non-referential reference to the exchange rate contained in a foreign currency loan agreement is contrary to the requirements of good faith and creates a significant imbalance in the rights and obligations of the parties resulting from the agreement to the detriment of the consumer is a significant and important question for resolving thousands of the so-called Swiss franc cases in Poland, especially if the elimination of the reference to bank's exchange rate table would result in a far-reaching sanction such as the collapse of the entire contract or the transformation of the loan into a non-market loan.

5. The case in which questions were referred for a preliminary ruling is one of over 30.000 cases on foreign currency loans currently pending before Polish courts. By invoking the abusiveness of conversion clauses, borrowers demand the invalidation of agreements in their entirety or the invalidation of provisions relating to indexation. The number of loan agreements in Swiss franc in banks' portfolios (and consequently the scale of the problem) is estimated at over 400 thousand.

6. The demands of borrowers undoubtedly endanger the stability of the financial sector. The authorities supervising the financial sector in Poland stated that the invalidity of agreements concluded in the years 2007-2008 will generate a sector's loss of about **40 billion zlotys (10 billion euros)**. This loss would be at least twice as high if all the agreements concluded in the years 2002-2012 were challenged. If, in addition - according to the consumer community's arguments - banks' restitution claims (including the repayment of the principal made available on the basis of the agreement) were to become time-barred, the loss would amount to **60 billion zlotys**, taking into account only the agreements concluded in the years 2007-2008. It would be more than twice as high for the entire foreign currency loan portfolio.

7. Polish courts' jurisprudence on foreign currency loan agreements formulates a quite unequivocal thesis (the jurisprudence is not entirely uniform, however, the discussed views definitely dominate), that **any arbitrariness of the bank in fixing the exchange rate applied within the framework of conversion clauses is unacceptable and is a source of abusiveness of these clauses**. Thus the jurisprudence, although not explicitly, **requires the conversion clause to have a referential character**, that is to say, it must refer to external criteria which are known to the consumer at the time of the conclusion of the contract and, moreover, are completely independent of the bank's discretion. Only if these two conditions are met would it be possible for the borrower to calculate the exchange rate for individual conversions himself and to check the "correctness" of the rate determination made by the bank for each subsequent currency transaction.

8. It should be underlined that the requirement of the referential character of a conversion clause was formulated neither by the Polish banking market regulator nor by the Polish legislator in the course of legal regulation of foreign currency loans.

9. In the years 2004-2011, many Polish banks offered their clients foreign currency loans with typically lower interest rates and costs than loans taken in Polish zloty. Loan agreements usually stipulated that the loan disbursement, indexation of the principal and each calculation of interest would be made on the basis of currency purchase or sale rates announced daily by individual banks in their exchange rate tables. At that time, such clauses were a typical market standard and were neither prohibited nor considered abusive; moreover, banks were expected to grant such loans.

10. In 2008, i.e. at the time of granting the largest amount of foreign currency loans and in connection with the financial crisis, the Banking Supervision Commission issued Recommendation S II[1], under which each foreign currency loan agreement included provisions on: "methods and time limits of determination of the foreign exchange rate based on which, in particular, the amount of the disbursed credit, the amount of credit tranches and capital and interest rates are calculated, as well as the principles of conversion of disbursement and repayment of credit to the currency" (point 5.2.2 (C) of Recommendation S II). A very similar regulation was included in the Act of 29 July 2011 amending the Banking Law. Pursuant to the newly added Article 69 (2) (4a) of the

[1] The so-called recommendations are issued by the market regulator on the basis of the banking law, they do not have a character of generally binding provisions of law, but banks must adapt to them under the threat of regulatory sanctions.

Banking Law, an indexed or denominated foreign currency loan agreement should include detailed rules for determining the manners and dates of fixing the exchange rate on the basis of which, in particular, the amount of the loan, its tranches and principal and interest instalments are calculated, as well as rules for converting into the currency of loan disbursement or repayment. **As the referring court rightly points out, in the course of these regulations, bank's freedom to set the exchange rate tables was not questioned in any way. The legislator's aim was only to introduce greater transparency and thus to lead to a greater competition between banks in terms of currency spread.**

11. Later on, after the financial crisis, only information on "methods and time limits of determination of the foreign exchange rate" were considered significant, without, however, requiring the referential character of the conversion clause. It should be underlined that the **significance of a given information for the consumer is a fundamental circumstance for assessing the abusive nature of contractual terms which do not contain such information**[2].

12. Since the Polish legislator and the regulator of the banking market did not consider the indicated information as significant, it should be assumed that this is how he saw the proper balance of interests of lenders and borrowers with respect to foreign currency loans. If, according to the CJEU case law, *"it may legitimately be supposed that the national legislature struck a balance between all the rights and obligations of the parties to certain contracts"* [3], such an assumption should be made as regards Polish legislation **on the date of conclusion of the loan agreement**. This means that the balance of interests of parties to a loan agreement struck by the Polish legislator did not include the requirement of the referential character of the conversion clauses.

13. In the opinion of the Polish Bank Association, **the requirement of the referential character of exchange rate tables and conversion clauses is unjustified** and is a result of incorrect application of the provisions of Directive 93/13 and the relevant provisions of Polish law.

14. The bank's exchange rate table, similarly to any other exchange rate tables operating on the currency market, has a character of a price list and is therefore determined in a manner characteristic for price determination. The amount of prices is determined, on the one hand, by the policy of a given entrepreneur and, on the other hand, by objective market conditions. Entrepreneurs' freedom in determining prices is covered by the constitutionally guaranteed freedom of economic activity (Article 22 of the Constitution of the Republic of Poland). The use of it cannot be considered unlawful. This means that the very manner of determining currency prices cannot be unlawful. If this was the case, the legality of all entities operating on the currency market should be questioned.

15. This is all the more so as the Annex to Directive 93/13 provides for a substantial relaxation of the requirements in relation to (i) financial services and (ii) currency buying and selling transactions. Cases specified in the Annex take into account the specificity of services related to financial markets (including currency markets). They enable the supplier of such services to make changes to the charges for financial services if it is objectively justified, for example - by the situation on the financial market. In the Annex, restrictions on unilateral shaping of contract terms and price changes have been completely excluded in relation to contracts for the sale and purchase of currencies. These cases have many features in common with conversion clauses, which refer to bank exchange rate tables. These clauses are in fact a price list of currency exchange services which are related (servant) to loan agreements. These clauses give the service supplier the

[2] Judgment C-348/14, *Bucura*, paragraph 66.
[3] Judgment C-51/71, *OTP Bank v. Ilyés, Kiss*, paragraph 53.

necessary freedom to shape the terms and conditions of concluding currency transactions. Therefore, the assessment of conversion clauses must take into account the liberalization of requirements on the grounds of the Annex to Directive 93/13. **However, the Polish jurisprudence's position does not take this factor into account.**

16. In the opinion of the Polish Bank Association, it should not be the case that technical modifications to the manner in which exchange rate tables are established - which would be applicable to the service of long-term loan agreements - are in fact derived from good customs or the precept to protect consumer interests. **The manner of establishing exchange rate tables is a result of a certain market practice and is uniform for all cases of application**. The bank shapes the exchange rate tables, implementing a specific policy with respect to currency transactions. Restricting the bank in this freedom and imposing - for the purposes of foreign currency loan agreements - different rules in this respect would be unjustified and disproportionate.

17. On the other hand, assessment from the point of view of good customs or the protection of consumer's interests can be applied to the **manner in which exchange rate tables are used in the framework of multiannual loan agreements (unlike the manner in which they are constructed). However, this is a different legal problem than the problem of the freedom to determine the tables.** In this context it is justified to refer to the so-called **"currency exchange office coercion"** test, that is, whether the use of exchange rate tables was a consumer's obligation or merely an entitlement[4].

18. Many foreign currency loan agreements provided – from the very beginning - for the possibility of disbursing and repaying the loan directly in the foreign currency, thus eliminating the currency exchange office coercion. **Since July 2009** Recommendation S II was in force, which required banks to enable the repayment of foreign currency loans in their currency (paragraph 5.2.4. of Recommendation S II). Thus, as early as July 2009, banks enabled their customers to repay loans in a foreign currency which they could purchase on the free market (e.g. in stationary or online currency exchange offices), **which means that in this regard the currency exchange office coercion was eliminated. Since August 2011**, on the basis of the Act of 29 July 2011 amending the Banking Law and certain other acts (Journal of Laws No. 165, item 984), the possibility of repaying the loan directly in a foreign currency was introduced, resulting directly from the provisions of law (Article 69(3) of the Banking Law). Therefore, since August 2011 customers could repay foreign currency loans in their currency on the basis of a statutory authorization.

19. Regardless of the above, Polish Bank Association has significant doubts about – common in Polish jurisprudence - **deriving the abusiveness of conversion clauses only from the hypothetical arbitrariness in their application.** The literal approach to the principle that in order to assess the abusiveness it is only the formulation of the contractual clause that is significant, not the manner of its execution (which seems to be criticized also by the referring court), makes the **very possibility** of arbitrary shaping of the table considered as the cause of abusiveness. **It is not examined whether the interests of any consumer have in fact been affected by the arbitrary shaping of the exchange rate (i.e. deviating significantly from the market rate).**

[4] Judgment of 10 September 2020, C – 738/19.

2. POLISH BANK ASSOCIATION'S ANSWER PROPOSAL

20. In the opinion of the Polish Bank Association, pursuant to Art. 1(2) of Directive 93/13, the conversion clause should not be included in the scope of Directive 93/13, because at the date of conclusion of the disputed agreement, Polish law required banks only to publish the applicable exchange rates.

21. If, however, conversion clause is considered to be subject to assessment from the perspective of abusiveness, it must be assumed that the content of this clause does not have to provide the consumer with the possibility to determine the amount of the exchange rate for a given conversion himself and to check the correctness of the exchange rate's determination made by the bank, but may limit itself to indicating that the market rate will apply.

22. Also in the absence of a reference to the market rate, it is possible under Directive 93/13 to interpret a contract, such as the one that is the subject of the reference, in such a way that the conversion clause referring to the rate in the bank's exchange rate table should be understood as a reference to the market rate.

23. In the opinion of the Polish Bank Association, the questions referred for a preliminary ruling should be answered as follows:

    1) ***The requirement that the conversion clause be unequivocal cannot be understood as meaning that a conversion clause must be of a referential character and must provide the consumer with the possibility to determine the amount of the exchange rate for a given conversion himself and to check the correctness of the exchange rate's determination made by the bank, while eliminating any discretion of the bank in determining the level of the exchange rate.***

    2) ***Directive 93/13 does not preclude an interpretation of a conversion clause in such a way that it will be established that - on the basis of such a clause - the bank is entitled to determine the exchange rate only at a market level, provided that such an interpretation is favourable to the consumer and is supported by the circumstances of the case, such as a common understanding of the clause by the parties, and national law does not preclude such an interpretation.***

3. RATIONALE FOR POLISH BANK ASSOCIATION'S POSITION

3.1 FIRST QUESTION

24. The conversion clause contained in the disputed agreement **should not** fall within the scope of Directive 93/13, since it reflected the then applicable statutory model for determining the exchange rate – it referred to the exchange rate fixed by the bank, which the bank was obliged to publish in a generally accessible manner.

25. According to Article 1(2) of Directive 93/13, the contractual terms which reflect mandatory statutory or regulatory provisions and the provisions or principles of international conventions to which the Member States or the Community are party, particularly in the transport area, shall not be subject to the provisions of this Directive.

26. In the CJEU judgment of 9 July 2020[5] it was indicated that Article 1(2) of Directive 93/13 must be interpreted as meaning that: *"a contractual term which has not been individually negotiated but which reflects a rule that, under national law, applies between contracting parties provided*

[5] Case C-81/19.

that no other arrangements have been established in that respect falls outside the scope of that directive".

27. On the date of conclusion of the disputed loan agreement, Polish law did not impose an obligation on banks to specify in the indexed or denominated loan agreement how the exchange rate applicable to settlements under the agreement will be determined. Only a general provision was in force, which obliged banks to publish the applied exchange rates (Article 111 of the Banking Law). The obligation to specify in the contract how the exchange rate will be determined was introduced by the national legislator only in 2011 under the Act of 29 July 2011 amending the Banking Law and certain other acts, also called the Anti-spread Act.

28. However, even if it is assumed that the conversion clauses are covered by Directive 93/13, **there is no basis for assuming that Directive 93/13 requires this rate to be fixed in the loan agreement in a <u>referential manner</u>.**

29. Provision of a referential character is not the only provision that can be regarded as **unequivocal** within the meaning of Directive 93/13. The unequivocality or intelligibility of the clause is a different issue than the possibility for the client to determine the rate himself or to check on his own the "correctness" of the rate determination made by the bank.

30. The CJEU case law on unequivocality (intelligibility) of contractual provisions does not equate it with the precept of the referential character of the conversion clause[6]. This case law underlines the possibility of evaluating economic consequences (and even more specifically - costs of loan), which should not be equated with the requirement to enable the consumer to determine the rate by himself or to check the correctness of the rate determination made by the bank according to the previously indicated algorithm.

31. Even without getting to know the data (methodology) of establishing the exchange rate table, the consumer was able to understand the potential economic consequences on the basis of: **(i)** the loan agreement itself, **(ii)** information provided by the bank on the foreign exchange risk - including in the format required at that time by the Polish supervisory authorities (Recommendation S), **(iii)** published historical data showing the volatility of exchange rates and their amount. Therefore, the consumer was able to understand that each time a loan instalment was repaid, a certain amount expressed in CHF (which the amount in CHF was constant) should be paid in its PLN equivalent (the amount of which was variable) **based on the daily changing exchange rates**, which had the attribute of market rates.

3.2 SECOND QUESTION

32. The essence of this question is the possibility of applying a pro-consumer interpretation of the model form of a contract in order to avoid the declaration of its abusiveness.

33. In the circumstances of the case heard by the referring court, it is possible to interpret the conversion clause in a way which, on the one hand, corresponds to its common understanding by the parties and, on the other hand, is a result of a pro-consumer interpretation, according to which the conversion clause enables the bank to determine in the exchange rate table only the exchange rate corresponding to the market exchange rate.

34. In accordance with Article 5 of Directive 93/13, the principle of pro-consumer interpretation is not applicable in cases referred to in Article 7(2) of Directive 93/13. However, as explained by the CJEU in judgment C-70/03, this exception should be understood as relating solely to the

[6] Judgment C-186/16 *Andriciuc*, judgment C-26/13 *Kasler*.

abstract control of abusiveness. Thus, the pro-consumer interpretation can be applied in the framework of the so-called incidental control of abusiveness, such as the control performed by the referring court.

35. The interpretation of contract terms is a necessary step before assessing their abusive nature.

36. In Polish law, the basic principles of interpretation of legal acts are contained in Article 65 § 1 and 2 of the Civil Code. According to the provision of § 1, a declaration of intent should be interpreted in view of the circumstances in which it is made as required by principles of community life and established custom. In accordance with § 2, in contracts, the common intention of the parties and the aim of the contract should be examined rather than its literal meaning.

37. Taking into account that the subject of interpretation is a model form of a contract rather than a contract, the basis for interpretation should be Article 65 § 1 rather than § 2 of the Civil Code. Nevertheless, if in a particular case the parties had a common understanding as to the meaning of the model form of a contract, the application of Article 65 § 2 of the Civil Code cannot be excluded. As the referring court established, this was the case in the case pending before it. As it results from the evidence proceedings, the borrower was convinced that the contract term refers to the market exchange rate. Similarly, the bank was convinced that the term authorized it only to determine the exchange rate at a market level. **As a result, since the parties understood the term in the same way, there is no obstacle to it being given this content.**

38. The requirement to apply a pro-consumer interpretation also leads to similar conclusions. This interpretation requires to choose, from among possible meanings of a contract term, those that are more beneficial to the consumer. Out of the possible meanings of the conversion clause, the more beneficial to the consumer is the meaning which limits bank's freedom in determining the exchange rate table by referring it to market values. Applying a pro-consumer interpretation therefore leads to the same effects as taking into account the common will of the parties.