REQUEST FOR THE PRELIMINARY RULING (C-19/20)

on Mortgage Loans Denominated in/Indexed to Swiss Francs in Poland

- STANDPOINT OF THE POLISH BANK ASSOCIATION

I. INFORMATION ABOUT THE CASE

1. In December 2019, the Regional Court in Gdańsk, Poland, submitted a request for a preliminary ruling to the Court of Justice of the European Union (the "**CJEU**") concerning the application of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts (the "**Unfair Terms Directive**") to mortgage loans denominated in/indexed to Swiss Franc ("**FX loans**").

2. In the years 2004-2011, many Polish banks offered such FX loans, with typically lower interest rates and costs than loans taken out in PLN, to their customers. After the Swiss Franc materially appreciated in value against PLN in 2009-2015, many borrowers filed claims against banks. The claims are brought on a similar premise – borrowers argue that the mortgage loans contained unfair exchange rate clauses, because they refer to the relevant bank's own exchange rate, without disclosing how this rate is arrived at. Borrowers go so far as to argue that – as a result of the alleged unfairness - the entire loan should be invalidated (rescinded) and they should recover the instalments they have already paid, but without returning the principal amount of the loan, which results in the unjust enrichment of the borrower and basically transforms the loan agreement into a charitable donation.

3. The questions submitted by the Polish court refer to the case of Bank BPH (GE). The Polish court making the referral considers that the reference to the bank's exchange rate margin is indeed unfair, but is seeking confirmation that it can remove only this unfair element, leaving the remaining terms intact without invalidating the entire loan agreement.

4. **The case raises universal issues of major importance to other foreign banks operating in Poland, as well as to other cases** in which consumers argue that the existence of an unfair term should invalidate the entire agreement. In particular, three of the five questions posed by the Polish court are critical to the banking sector. The Polish Bank Association submits that in response to the questions posed by the Polish court, the CJEU should confirm that:

    a. the court should remove only the unfair term (in BPH's case, the term relating to the bank's exchange rate margin), leaving the remaining contractual provisions in place, rather than invalidating the entire loan agreement; the FX loans can continue to operate by reference to the exchange rate of the National Bank of Poland (**Question 2**);

    b. the court should refrain from invalidating the agreement in its entirety, if the parties concluded an annex in which they eliminated the unfair contractual term (**Question 1**);

    c. even if the court were to decide to invalidate the relevant loan agreement, the borrower

should not be allowed to refuse repayment of the principal under that loan agreement; both parties' restitution claims become due and payable only upon a final judgment (**Question 4**).

II. BACKGROUND ON POLISH FX LOANS AND THE CLAIMS OF BORROWERS

5. In 2002–2012 nearly 1 million Swiss franc loans were granted in Poland, including by foreign banks: Santander, mBank (Commerzbank), ING Bank, Bank Millenium (Banco Comercial Portugues), Raiffeisen, and Deutsche Bank.

6. These loan agreements typically stipulated that the disbursement of the loan, the indexation of the loan principal and each calculation of interest will be made on the basis of the buy or sell currency rates announced daily by the individual banks in their foreign exchange rates tables. At that time, such clauses were typical market standard and were not prohibited, and the banks were encouraged to grant FX loans.

7. In 2011, Poland amended its banking regulations, requiring banks to set out in the loan agreements detailed terms regarding the methods of the calculation of the exchange rate and enabling the borrowers to repay the loan directly in the relevant foreign currency.

8. When executing the loan agreements, the borrowers typically confirmed they were aware of the exchange rate risks. But the change in the economic conditions which occurred many years after the loan agreements were executed (following the Global Financial Crisis and the Swiss National Bank's decision to abandon the cap it had set for the Swiss franc), inspired borrowers to seek ways to avoid the foreign exchange risk by filing claims against banks.

9. Currently, nearly twenty thousand cases are pending before courts in Poland. The borrowers (associated in strong lobbying groups and represented by specialist law firms) are claiming that the loan agreements (even those entered into prior to 2011) lack precise and clear information as to how the foreign exchange rates are calculated by the banks, and such exchange rate clauses are unfair. Instead, borrowers are demanding the invalidation of their agreements or cancellation of the indexation (effectively converting the FX loan into a PLN loan). They are claiming that the banks should return the instalments paid to date to them, but the banks should not be able to claim back the principal, on the basis that such claims have already become time barred under Polish law (the borrowers argue that the three-year limitation period for the banks' claim for the return of the principal started running on the loan disbursement date and would have expired before anyone had started challenging these agreements).

10. The Polish Bank Association considers that **the borrowers are instrumentally relying on the EU unfair terms protection mechanisms as a way to be released from a credit obligation or to**

obtain extraordinary gains, believing that, as a result, not only will they no longer be obliged to repay the principal of the loan but also that the bank will return the instalments paid to date to them. **This would result in a solution that would be absurd both in legal and economic terms** and would pose a threat to the stability of the financial system in Poland.

11. According to initial estimates made by the Polish Bank Association, the total loss suffered by Polish banks involved in such loans, assuming that a universal PLN conversion would be introduced, would amount to **PLN 60 billion, i.e. approximately 3% of Poland's GDP.** Of course, the losses suffered by the banks would in fact be much higher if the borrowers' invalidation claims are accepted.

III. UNIVERSAL ISSUES FOR DETERMINATION

12. [**Question 2 – blue-pencil doctrine**] The Polish court is seeking confirmation that it can remove the unfair element of the BPH exchange rate clauses (unspecified bank's exchange rate margin), but keep the rest of the contract valid and operable.[1]

13. Removing part of a contractual term is referred to as the blue-pencil doctrine – which is widely accepted, for example, in German case law. Such an approach is consistent with the underlying objective of the Unfair Terms Directive, which provides in Article 6 (1) that unfair terms should not be binding, but the rest of the contract should continue to be binding without the unfair terms, if this is possible. The loan agreement can continue to operate without the bank's exchange rate margin. In such case the exchange rates should be calculated on the basis of the rate of exchange of the National Bank of Poland. The rate of the National Bank of Poland is expressly referred to in the exchange rate clause at issue in BPH's case, but it is also the default rate under Polish law, per Section X of the Polish Civil Code.

14. **It is crucial that the CJEU approves the application of the blue-pencil doctrine in BPH's case, to confirm its wider applicability**. The national courts should be allowed to remove from a contract only those provisions which are truly unfair (provided that the contract can operate without such terms), without resorting to more severe measures such as invalidation of the contract. If the above-mentioned doctrine is not approved in BPH's case (which naturally lends itself to the blue-pencil doctrine), this would undermine the role and applicability thereof in future cases, prompting borrowers in consumer contracts to rely on a single, unfair element in the contract to argue that the entire contract should be invalidated, where this is not necessary.

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[1] In the case at hand, the exchange rate after this deletion would read: "*2. The buy rates are defined as the average PLN exchange rates against the relevant currencies, published in the table of average exchange rates of the National Bank of Poland, ~~minus the buy margin~~*."

15. For the above reasons, the blue-pencil doctrine is of critical importance to banks operating in Poland (and elsewhere in the EU) – both in connection with FX loans, and other consumer contracts.

16. [**Question 1 – amending unfair terms**] After the relevant loan agreement was executed, the parties amended the unfair contractual term in 2011 by specifying how the bank's margin will be calculated and allowing the borrower to repay the loan directly in Swiss Franc. The Polish court is seeking confirmation that it should not invalidate the entire loan agreement, given that the unfair contractual term has been amended and is now fair.

17. This poses a universal question as to whether the parties can subsequently rectify unfair contractual terms, and what effect this should have on the validity of the contract. The Polish Bank Association's position is that the assessment as to whether the agreement may continue to be binding must be made as at the date of the ruling (or as at the date when the dispute in the case arose), taking into account any such contractual amendments.

18. **The Polish Bank Association further argues that, if the parties amend the contract, so that it may continue to operate without the unfair terms, such contract should be upheld and kept valid.** There is no reason to invalidate an entire contract merely because of the fact that for a certain period of time it contained an unfair term. Otherwise, entrepreneurs will have no incentive to take steps to rectify their contracts and amend any unfair terms. Upholding the validity of the contract is also in line with the above-mentioned principle of the Unfair Terms Directive that the contract should continue to be binding without the unfair terms, if this is possible.

19. [**Question 4 – invalidating the loan**] Finally, the Polish court seeks confirmation that even if the loan is invalidated, then both parties' restitution claims should become payable only upon a final judgment being rendered. This question arises because, as noted above, Swiss Franc borrowers argue that the limitation period applicable to the claims of banks for the return of the principal starts running on the loan disbursement date, even if the loan was invalidated by the court on account of unfair contractual terms years later. The relevant limitation period applicable to banks is 3 years, while the relevant limitation period for consumers is up to 10 years. Most of the FX loans were granted in 2006-2008 and were long-term (in the case at hand – for 30 years), whilst the consumers started challenging those loans after 2015. If the borrowers' argument is accepted, banks would be time-barred from seeking to recover the principal loan issued, despite the invalidation of the loan and the borrowers' recovery of all instalments paid under the loan agreement. This is an absurd result.

20. Although the nature of the sanctions relating to the use of unfair terms in contracts with consumers is a matter reserved for national law, **this issue is highly relevant for other foreign banks operating in Poland, but also those operating within the EU.**

21. EU law does not allow the use of disproportionate sanctions. **Under no circumstances should it be allowed that in the case a court invalidates a loan, the customer will not be obliged to repay the principal under that loan.** Such understanding of the invalidation sanction would, in practice, lead to an actual transformation of a loan agreement into a unjust windfall for the borrower. This is an extreme sanction for banks, incompatible with the fundamental principles of EU and Polish law. It would also undermine the stability of the financial system in Poland, for the reasons described above.