# THE LEGAL CONSEQUENCES OF INVALIDITY OF A LOAN CONTRACT[1]

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**Abstract**

In recent years the courts have examined innumerable aspects of the invalidity of foreign currency loan contracts. However, to date there has been no examination of how the legal consequences of invalidity of a loan contract must be drawn in the event that the contract cannot be declared valid. A loan contract qualifies as a legal relationship aimed not at the transfer of the right of ownership of something, but at the use of another's money, so that restitutio in integrum – the restoration of the original state of affairs – is impossible due to the irreversibility of the contract's performance from the outset. As a consequence of the 2008 economic crisis, in the overwhelming majority of lawsuits – due to the nature of the legal relationship – the impossibility of restitutio in integrum due to retroactive irreversibility must be established, since the party seeking restitutio in integrum would not be capable of repaying the received loan. Ultimately, the impossibility of restitutio in integrum ensues anyway due to the (partial) lapse of claims deriving from the legal relationship. As a consequence of the impossibility of restitutio in integrum – if the court cannot retroactively remedy the harm caused by the invalidity of the agreement – the contract must be declared to be in force until a judgment has been reached. In such cases, the court determines the debtor's outstanding principal in its judgment, taking the money of account as a basis, and compels the debtor to pay this amount accordingly.

*JEL codes:* K120, K22

*Keywords:* contract law, economic law, invalidity

## 1. INTRODUCTION

In recent years the courts have examined innumerable aspects of the *invalidity of foreign currency loan contracts*. Besides judgments reached in individual lawsuits, Hungary's supreme court, the Curia, also handed down an opinion and uniform-

1 The present study is a revised version of the author's essay published in the Hungarian Legal Gazette (Péter Gárdos: The legal consequences of invalidity of a loan contract. *Jogtudományi Közlöny,* 2014/11, pp. 504–514).

ity decisions. Opinion No. 2/2012 (XII. 10) of the Civil Department of the Curia examined the unfairness of the unilateral right to amend contracts, as contained in the general terms and conditions applied by financial institutions in consumer loan contracts. Civil uniformity decision No. 6/2013 (hereinafter: Uniformity Decision) reviewed the validity of foreign currency loan constructions and the individual legal consequences of invalidity, while Civil uniformity decision No. 2/2014 once again examined the question of unfairness in the unilateral amendment of contracts and the application of the exchange rate margin. To date there has been no examination of how the legal consequences of invalidity of a loan contract must be drawn in the event that the contract cannot be declared valid. At the beginning of 2014, a *jurisprudence-analysing working group* was established at the Curia to investigate this issue. However, the investigation can be expected to have little impact on foreign currency-based consumer loans, given that Act XXXVIII of 2014 on the settlement of individual questions relating to the Curia's uniformity decision pertaining to consumer loan contracts of financial institutions, as well as Act XL of 2014 on the rules for liquidating debt and certain other provisions set down in the aforesaid Act XXXVIII of 2014, stipulate rules for these loans which differ significantly from the general rules of civil law. Beyond the scope of these, however, *the decision of the jurisprudence working group has considerable relevance.*[2]

## 2. GENERAL LEGAL CONSEQUENCES OF INVALIDITY OF A CONTRACT

Act IV of 1959 on the Civil Code (hereinafter: Old Civil Code) and Act V of 2013 on the Civil Code (hereinafter: New Civil Code) deal rather concisely with the legal consequences of invalidity, and for this reason significant uncertainty has arisen on numerous issues in this area. It was with the intention of reducing this uncertainty that Opinion No. 1/2010 (VI. 28) of the Civil Department of the Curia examining the legal consequences of invalidity (hereinafter: Opinion) was issued in 2010, aimed at anticipating the invalidity regulations of the New Civil Code.

By virtue of the law, invalidity has legal consequences that take effect either automatically or only in response to a petition.

2 After the present article had been submitted, the jurisprudence-analysing working group adopted its summary opinion. The jurisprudence working group also came to the conclusion that, with regard to Act XXXVIII of 2014 and Act XL of 2014, the significance of the examined questions would be negligible in actual lawsuits. In view of this, the jurisprudence working group merely made a decision on the publication of its report, while not deeming it necessary to adopt an official opinion.

The *automatic legal consequence* of invalidity is that it is not possible to establish a right based on an invalid contract and to demand performance of that contract.[3] This provision means that if the court finds during a lawsuit that the contract which is the subject of the suit is invalid, then it will not compel the party to perform based on an invalid contract. More than this, however, the judgment will only contain in the event that one of the parties asks the court to draw the legal consequences of invalidity.

Based on the Old Civil Code, there were three *legal consequences of invalidity that could take effect in response to a petition*: the contract is declared valid by the court, the original state of affairs is restored (restitutio in integrum), or the contract is declared in force until a judgment has been reached.[4] The New Civil Code changes this on a single point: instead of declaring the contract in force, it allows for restitution for unjust enrichment.[5] While the courts are ordinarily bound by the petitions of the parties, this only partly applies in the case of the legal consequences of invalidity. The court may deal with the legal consequences of invalidity in a way that departs from a party's petition; however, it may not apply any solution against which both parties protest.[6]

An item-by-item examination of these legal consequences would exceed the limits of the present study. For this reason, in what follows we will merely examine *whether restitutio in integrum can occur,* or whether – at the exclusion of any other legal consequence – the court *must declare the loan contract in force* until a judgment has been reached.

The Old Civil Code only partly determines *the order in which the legal consequences of invalidity* may be applied by the court. Based on the law, a declaration of validity and restitutio in integrum is the primary legal consequence which the court may choose. Declaring the contract in force and restitution for unjust enrichment based on the New Civil Code may occur if the contract cannot be declared valid retroactively, or if the state of affairs that existed prior to the signing of the contract cannot be restored in kind.[7] The Uniformity Decision further refined this sequence when it stipulated that the court must primarily strive to declare the contract valid, and may only apply the other legal consequences of invalidity if the contract cannot be declared valid (e.g. contracts against good morals or usurious contracts).[8]

3 Section 6:108 (1) of the New Civil Code. Although the Civil Code did not set down this item, point 2 of the Opinion stipulated the same.

4 Civil Code, Section 237.

5 New Civil Code, Section 6:133; other legal consequences: Sections 6:110–6:112.

6 Opinion, point 7; New Civil Code, Section 6:108 (3).

7 Opinion, point 5; New Civil Code, Section 6:113 (1).

8 Uniformity Decision, point 4.

Based on the Uniformity Decision, therefore, it seems that in the case of invalidity of a loan contract, when making its decision on the legal consequences of invalidity, the court must *(a)* initially attempt to declare the contract valid; *(b)* if it cannot do so, then examine whether restitutio in integrum can occur; and *(c)* if there is no possibility of restitutio in integrum – for example, because a party is unable to return the service received – then allow for the contract to be declared in force until a judgment has been reached.

## 3. SUBJECT OF THE EXAMINATION

In what follows, we will show that the above-presented sequence of legal consequences of invalidity does not prevail: if, after all, the loan contract cannot be declared valid, then restitutio in integrum cannot occur. The reason for this is that restitutio in integrum is only possible for contracts aimed at the transfer of ownership,[9] and consequently the question of what legal consequences of invalidity of a loan contract apply in the event that the contract cannot be declared valid can be answered based on the characteristic performance of the loan contract; namely, on whether the contract is aimed at transfer of ownership. In the present study, we argue that *the characteristic performance of the loan contract consists of ensuring the right for temporary use of money, and not the transfer of the right of ownership of the money, and for this reason restitutio in integrum is impossible.*

In order to answer the question, we will examine below: *(a)* what qualifies as the characteristic performance in the case of a loan contract; *(b)* with respect to the legal consequences of invalidity, what happens if, in the case of a foreign currency loan, the money of account differs from the money of payment; *(c)* how prescription applies in relation to the legal consequences of invalidity; and *(d)* how liquidation of debt occurs if the calculation of interest is annuity-based.

In examining the question, foreign currency loan-related lawsuits do not provide any foothold. This is because Section 239/A of the Old Civil Code enables the plaintiff to request only that the invalidity of the contract be determined, without also having to ask for any legal consequences of the invalidity to be drawn. Plaintiffs take advantage of this opportunity almost without exception, and consequently the question of which legal consequence of invalidity is to be applied has arisen only occasionally in judicial practice.

The New Civil Code entered into force on 15 March 2014. Its provisions relating to contracts must be applied as a principle rule to contracts concluded after this date.[10] Nevertheless, the Old Civil Code remains applicable for a long time as well.

9 Opinion, point 3.

10 Section 50 (1) of Act CLXXVII of 2013 governing interim and authorizing provisions related to the entry into force of Act V of 2013 on the Civil Code.

For this reason, in what follows we examine questions of the legal consequences of invalidity primarily based on the regulations of the Old Civil Code, while discussing separately any instance where the New Civil Code brings a relevant change.

## 4. CHARACTERISTIC PERFORMANCE IN THE CASE OF A LOAN CONTRACT

### 4.1 Relevance of the characteristic performance

If the contract cannot be declared valid, or if the court finds that the declaration of validity is not an appropriate legal remedy, then the court will stipulate restitutio in integrum or declare the contract in force until the date of the judgment. In the Opinion, however, restitutio in integrum is not possible in every case: a condition for this is that the performance should be *originally reversible*, and restitutio in integrum *should not subsequently become impossible either.* If the performance is irreversible, then restitutio in integrum is impossible and the court declares the contract in force until a judgment is reached. For this reason, we primarily examine below whether the loan contract is aimed at providing a reversible performance.

### 4.2 Is the performance originally irreversible in the case of a loan contract?

The contract is *originally reversible* if it is aimed at the transfer of ownership, while performance that consists of carrying out an activity, abstaining from the activity, ensuring the right of utilisation, etc. is *irreversible*. The reason for the above distinction is clear: in the case of a sale and purchase, the thing sold and the purchase price are both returnable, thereby restoring the original state of affairs,[11] but in the case of a tenancy agreement usage that has occurred cannot be undone. This distinction explains why, in the case of services performed on the basis of supply contracts, service agreements and usage contracts (lease, leasehold, commodatum), as well as services performed on the basis of an insurance contract or suretyship that comprises the fulfilment of a commitment and undertaking of risk, the court – instead of restitutio in integrum – will declare the contract in force until a judgment has been reached, settling accounts between the parties in this way.

We will examine the method of declaring the contract in force in detail below, but here we also make mention of the significant theoretical and practical differences

11 Settlement of debt according to the duration of usage can be disregarded from the point of view of the present study; for this, see point 10 of the Opinion.

between the two legal consequences. *The goal of restitutio in integrum is to treat changes occurring on the basis of the contract as if they had not happened.* Given that this is not possible in the case of legal relationships not aimed at the transfer of ownership, since with a lease – for example – usage that has occurred cannot be undone, the declaration in force takes a different approach. *In declaring the contract in force, the court recognises that until the date of the judgment the parties are obligated to fulfil performance based on the invalid contract; however, with respect to the future, it confirms the invalidity of the contract.* Since – as we mentioned in the introduction – the parties are not burdened by an obligation to execute based on an invalid contract, the effect of declaring the contract in force is that in its judgment the court compels payment for services already rendered, but does not recognise any obligation with respect to performance of services not yet rendered. Taking the example of a lease agreement, therefore: if the contract has been concluded for two years, but after one year the court determines the invalidity of the contract, then it will merely examine whether any performance occurred without counter-performance (whether the tenant used the rented property without having paid any rent, or whether the tenant paid rent for a period during which they did not use the property), and if it did occur, then it will compel the concerned party to pay the counter-value. On other issues, however, the court will not intervene in the past.

As to the question of what is *the characteristic performance in the case of a loan contract,* there are two approaches in attempting to find an answer. One possible interpretation is that the object of the loan contract is money or other fungible goods of which *the debtor obtains the right of ownership by way of transfer, thus making the possibility of restitutio in integrum evident,* since this circumstance in itself confirms that the contract is aimed at transfer of the right of ownership. The other interpretation takes as its basis that the loan contract ensures the right for temporary use of money, meaning that *the contract is aimed not at the transfer of ownership of something, but at the use of someone else's assets*. Here, the transfer of ownership which the transaction necessarily entails is merely an unavoidable consequence arising from the special nature of money, but not the true object of the contract between the parties and not the intention of the parties in concluding the transaction.

*The standpoint of the legal literature is unified with respect to the characteristic performance of a loan contract,* as quotes taken from the principal authors of legal studies relating to monetary obligations clearly confirm. According to *Cottely*: "We describe a loan contract as an agreement by which the lender cedes ownership of money to the other party (borrower) as credit for temporary use in return for a consideration. (…) Under the loan contract, the party providing the loan primarily commits itself to handing over the money to be lent into the other party's

possession, ceding ownership of the lent amount until a specified date."[12] According to *Bátor*, author of the chapter on monetary obligations in the *Szladits* commentary which essentially defines the legal literature following the Second World War, a loan is defined thus: "The lender is under obligation to leave the amount of the loan in the debtor's possession – and by extension in their use – until the date of repayment stipulated in the contract. This is the obligation of the lender for which the debtor provides a consideration through the payment of interest."[13] In his commentary on the Old Civil Code, *Zoltán* highlights the granting of credit and the element of trust as characteristic features of the loan contract,[14] while in his monograph on loan contracts, very aptly describing the legal relationship, he writes: "In the case of a loan contract, *strictly speaking the lender never really considers that the thing in their ownership is being passed into the 'ownership' of the borrower. Consciously, the borrower scarcely grasps the fact of obtaining ownership of the thing received as a loan. In the consciousness of both parties, the focus is on relinquishing and receiving a thing for temporary use.*"[15]

*The interpretation set forth here is in line with the interpretation of a loan that has evolved in foreign laws. Roy Goode*, for example, defines a loan in the broad sense (including, besides monetary loans, deferred payment of a purchase price and financial lease) as the provision of some form of benefit, for the use of which the debtor will pay a consideration at a later date.[16] A draft proposal for the regulation of European contract law defines a loan as an agreement based on which the lender cedes use of a thing for a temporary period to the debtor, who is obliged to return the object of the loan at a later date, with or without interest. The object of the loan may be money or some other thing.[17] The preamble attached to the draft proposal points out that *the bulk of European states regard a monetary loan as a contract aimed at temporary use*.[18]

*These authors therefore highlight temporary usage, and not acquisition of ownership, as the primary object or characteristic performance of a loan.* As Ödön *Zoltán* points out in his monograph: "The borrower's acquisition of ownership is therefore in reality a technical solution that necessarily follows from the specific nature of the object of the loan and the contractual obligation."[19]

*The contradiction between content and form,* i.e. between temporary use as the economic goal of the transaction and the transfer of ownership as the necessary

12 Cottely, p. 161.
13 Bátor (1942), pp. 158 and 177.
14 Eörsi, Gyula –Gellért, György (1981), p. 2426.
15 Zoltán, Ödön (1972), p. 78; the italics are ours.
16 Goode, Roy (2004), p. 578.
17 von Bar, Christian – Clive. Eric (2009), p. 2456.
18 von Bar, Christian – Clive, Eric (2009), p. 2461.
19 Zoltán (1972), p. 78.

means of this, is conspicuously highlighted by *István Gárdos* and *András Nagy*, as well as by *Zoltán* in the literature of the period before the change of political regime.

As *István Gárdos* and *András Nagy* argue in their study on foreign currency loan contracts: "The concept of a loan (…) conceals an interesting contradiction. While the economic content of the transaction can be described as the temporary use of someone else's asset, legally it appears as the transfer of ownership. This contradiction arises from the particular nature of the typical object of a loan, namely money. Money can be used primarily to effect payment, but payment entails a transfer of ownership, and for this reason the lease of money – i.e. the mere transfer of possession – is not possible. In the case of money, this same economic goal is achieved by a loan, which entails a transfer of ownership. This contradiction between the content and form of a transaction is resolved by the fact that the transfer of ownership is only temporary, with the debtor obliged to pay back the amount of the loan on expiry of the loan period (transferring to the lender ownership of an amount of money equivalent to that originally received). Despite the transfer of ownership, the essence of the service provided under the loan contract is that the debtor uses the lender's money, while the lender shoulders risks related to the debtor's creditworthiness, both present and future. In the case of a loan, transfer of the right of ownership of the money is not final – such as, for example, in the case of a sale and purchase – but only temporary; for this reason, from the point of view of the transaction's economic content, it can rightly be regarded as use of another's money, for which the consideration is the fee for this usage (the usual stipulated interest)."[20]

In his book on loan contracts, Ödön *Zoltán* – criticizing judicial practice – points out: "In determining the legal consequences of invalidity, judicial practice generally applies the provision contained in Section 237 (1) of the Civil Code. (…) Counter-arguments may, however, be raised against this position. Namely, in the event that the determination of invalidity occurs after the loan amount has been handed over, meaning at a time when the borrower has already made use of the loan amount, the situation preceding the signing of the contract cannot be restored in reality because the actual usage of the loan amount for a specified period cannot be undone. (…) A loan contract – notwithstanding its specific construction – is essentially a long-term legal relationship. From the aforementioned point of view, it scarcely makes any material difference what object is being used: whether it be a sum of money or some other thing. If, in case of a lease of a washing machine, the original condition cannot be restored because the lessee used the washing machine for a specified period (even though money can compensate

20 Gárdos, István – Nagy, András (2013), p. 383.

for the value of this usage, so that the situation prior to the signing of the contract is economically restorable), then this same stance should also surely be taken if it is not a washing machine, but 2,000 forints which is being made available for use. Consequently, with respect to the invalidity of a loan contract already wholly or partly fulfilled, strictly speaking the parties' original legal relationship should always be liquidated by applying Section 237 (2) of the Civil Code."[21]

This interpretation is supported and supplemented by the concept of monetary loans contained in the Act on Credit Institutions and Financial Enterprises (Credit Institutions Act).[22] According to this, the object of a loan contract is not merely to make a sum of money available; in addition, "financial service activity aimed at providing credit or monetary loans also includes measures relating to the examination of creditworthiness, drawing up of credit or loan agreements, and recording, monitoring, review and recovery of disbursed loans." Irreversibility of the services listed by the Credit Institutions Act is undisputable due to the *facere* nature of these services. *It is not possible to break up the uniformity of the service of the creditor* in a way that disbursement of the loan qualifies as reversible, while other services listed under the concept of monetary loans by the Credit Institutions Act qualify as irreversible.

Based on all the above, I believe it is justified to say that *a loan contract does not qualify as a legal relationship aimed at the transfer of ownership, therefore restitutio in integrum is impossible due to the original irreversibility of the contract*, as based on point 3 of the Opinion. Consequently, the court has no choice with respect to the legal consequence of invalidity: *if the contract can be declared valid, then this must occur; if, however, this is impossible, then the legal relationship between the parties must be settled by declaring the contract in force until a judgment has been reached.*

### 4.3 Is the performance retroactively irreversible in the case of a loan contract?

The Opinion excludes restitutio in integrum even in cases of retroactive irreversibility, i.e. where the original state of affairs could have been restored originally, but it became impossible later.[23] Retroactive irreversibility may only arise in the case of an originally reversible performance, so that examination of this may only occur if the loan – despite the above – is not regarded as an originally irreversible performance. *In the case of foreign currency loan contracts, a change in the*

21 Zoltán (1972), pp. 377–378.

22 Old Credit Institutions Act, appendix no. 2, point I. 10.3; new Credit Institutions Act, Section 6 (1), point 40. c).

23 Opinion, point 6.

*debtor's economic situation may qualify as a circumstance resulting in retroactive irreversibility.*

According to point 4 of the Opinion, "a party may only successfully claim the performance due to them in return if it simultaneously undertakes, and is able, to return the service received from the other party." Based on the Opinion, therefore, when restitutio in integrum occurs it is always necessary to examine the solvency of the party requesting restitutio in integrum.

*The purpose of the loan is to be spent by the debtor* (e.g. on the purchase of real estate, vehicles or consumer goods, or the repayment of an earlier debt). It is precisely because of this that the peculiar feature of the loan arises whereby a period necessarily elapses, between the disbursement and the repayment of the loan, during which the amount of the loan is not in the possession of the debtor. It follows from this that *a specific feature typical of a loan contract is that the performance becomes irreversible.*

This fundamental characteristic of loans is enhanced by the particularities of today's situation. The problem with foreign currency loans essentially springs from the economic crisis that occurred at the end of 2008. A significant exchange rate depreciation took place as a consequence, added to which many people lost their jobs or suffered reduced income. As a result, a substantial number of debtors – parties contesting foreign currency loans almost without exception – became unable to fulfil their contractual payment obligations, are in default on their due repayment instalments, and *cannot realistically be expected to pay their debts in one sum.*

It consequently follows from point 4 of the Opinion that if a plaintiff were to fail to prove in their lawsuit that, in the event of a favourable judgment, they are able to repay the loan, then the court would not be able to choose restitutio in integrum even if the performance is otherwise reversible. *In this case, declaring the contract in force would be the only remedy.*

### 4.4 Impossibility of restitutio in integrum

One might suggest that the viewpoint put forward in the Opinion, which holds that restitutio in integrum is only possible in the case of a contract aimed at transfer of ownership, must be treated "more flexibly" given that the *special nature of a payment obligation demands a different approach.*

*Emilia Weiss* points out in her monograph on invalidity that "neither physical impossibility nor economic inexpediency will generally count against, for example, application of the classic invalidity sanction of restitutio in integrum in the case of the sales contracts that make up a significant portion of economic turnover,

the far less important barter agreements, and particularly the loan contracts that comprise a significant number of invalid contracts."[24]

This interpretation is presumably based on the obvious contention, hard to contradict at first glance, that *the money received (or more precisely, a sum of money equivalent to this) can be returned, so that there can be no question of the impossibility of restitutio in integrum.* If the debtor pays the received amount back to the creditor, while the creditor returns the interest received to the debtor, then the original state of affairs is restored. *In our opinion, this stance is mistaken since the outcome thus achieved does not truly represent restitutio in integrum.* When examining this, it is necessary to begin by looking at what is meant by restitutio in integrum, and by comparison to see whether, in the case of a loan, repayment of the principal and any interest due for the usage period leads to an identical outcome.

The conceptual starting point for restitutio in integrum is as follows: "Restoring the situation that existed prior to the signing of the contract represents a complete liquidation of contractual obligations, thereby necessitating creation of the situation that would have existed if the parties had never signed the contract."[25] In essence, implementing restitutio in integrum entails the mutual reimbursement in kind of the performance provided by each party.[26] A requirement also applies in the event of restitutio in integrum that "the court, in drawing the legal conclusions of invalidity, must take care to maintain the balance of value between performances of originally equal value, and to prevent the unjust enrichment of either party."[27] "It follows from this that restitutio in integrum does not mean reimbursement of each delivered performance 'one for one,' but rather that, in restoring the original state of affairs, the prevailing principle must be to maintain the original balance of value."[28]

Based on the above principles, *restitutio in integrum in the case of a sale and purchase means the return of the thing sold and the repayment of the purchase price.* In the case of a loan, this would seemingly correspond to the debtor paying back the loan and the creditor refunding the interest received. This, however, is not an appropriate solution.

As we indicated above, although a transfer of ownership occurs, the debtor receives the amount of a loan not permanently but temporarily, and must repay this amount even in the event of validity of the contract. *The repayment of the loan amount is not, therefore, a specific consequence of restitutio in integrum, but a fundamental obligation burdening the debtor on the basis of the loan contract.*

24 Weiss, Emilia (1969), p. 417.
25 Opinion 3/2010 (XII. 6), point 2.
26 Opinion, point 3.
27 Opinion, point 8.
28 Opinion, point 8.

Consequently, while in the case of a sale and purchase as featured in the above example, the return of the thing sold results in a change compared to the contract between the parties, given that the contract was aimed at the permanent transfer of ownership of the thing sold (meaning that the buyer was not obliged to re-transfer ownership of the thing based on the contract), the *repayment of the loan amount essentially leads to an outcome identical to the goal specified in the contract.* The situation is the same in the case of a lease agreement, for example, where restitutio in integrum is indisputably impossible because of the original irreversibility of the performance. In the event of invalidity of a lease agreement, the court does not order the return of the object of the lease, especially not in the context of restitutio in integrum. The tenant is not compelled to return the object of the lease because the original state of affairs must be restored, but because the legal title to use has been terminated, meaning that the tenant would be retaining the leased object without valid legal title. *The repayment of the loan amount, or the return of the leased object, does not liquidate the legal relationship between the parties retroactively to the time of signing of the contract, but merely with respect to the future.*

The obligation to repay money received as a loan itself indicates that the essence of the service performed under the loan contract *is not the transfer of ownership, but what remains true of the loan even after repayment: that the debtor was able to use the given amount for a specified period.* The fact that the debtor was able to use the amount received as a loan, as with any other contract for use of something, renders the performance originally irreversible.

The problem of restitutio in integrum is demonstrated well by the question of settling the interest paid by the debtor. In the case of a sale and purchase, the buyer is obligated to return the object acquired, and the seller to repay the purchase price for that object. In the case of a loan, this solution apparently leads to the same outcome if the court compels the creditor to repay the interest already paid by the debtor, since this results in the situation which existed prior to the signing of the contract, where the loan amount belonged to the creditor and the interest amount to the debtor. However, the analogy is not applicable. *The interest is not a consideration paid for the transfer of ownership (not a purchase price), but a fee to be paid for usage (pro rata over the period of use).* This is well expressed in the legal literature, which uniformly regards interest as the consideration for use of another's money (clearly conveying that the legal "vernacular" also regards a loan as granting the use – and not the acquisition of ownership – of another's money). The repayment of interest is not, therefore, the counterpart of repayment of a loan. *Interest is the fee for usage that cannot be undone, which is still due to the creditor even if the principal has been repaid.* Repayment of interest would signify that the debtor had used the loan amount free of charge. This also follows from

the Opinion, which states that "the party unilaterally making use of the service of the other party (…) is obligated to pay the interest or fee for usage."[29] Consequently, in the context of restitutio in integrum, the creditor would not be compelled to repay the interest, since this is the consideration for having provided money for the debtor's use. This would lead to a situation, irreconcilable with the logic of the Opinion, whereby restitutio in integrum in the case of a loan contract would occur with the debtor returning the received amount while the creditor would not be obligated to provide reimbursement for any performance. (We will examine additional problems relating to interest below.)

All this likewise supports the conclusion that there is no possibility of restitutio in integrum in the case of a loan contract, since *the performance of the loan contract is by nature irreversible; in the context of restitutio in integrum, therefore, it would not be possible to provide for reimbursement for performance according to the principles set forth in the Opinion.*

The Curia's jurisprudence-analysing working group was divided on this question. "According to what can be regarded – with a narrow difference in votes – as a majority stance, if the court has not declared the contract valid, then restitutio in integrum is conceptually impossible in the case of total invalidity of either a consumer or a non-consumer loan contract, and settlement may only occur with declaration of the contract in force until a decision is reached."[30]
For this reason, in what follows we will examine what obligations burden which party in the event of a loan contract being declared in force.

### 4.5 Declaring a loan contract in force

#### *4.5.1 Declaration in force in general*

"If the state of affairs that existed before the signing of the contract – owing to either original or retroactive irreversibility – cannot be restored or is not expedient, and the contract cannot be declared valid, the court declares the contract in force for the period until a decision has been reached and orders monetary reimbursement of the consideration for any performance that may have remained without counter-performance."[31]

In its judgment BH2013. 241, the Curia indicates that *"in the context of declaring a contract in force, the court must ensure that in the meantime no performance should remain without a counter-performance.* The balance in value of the per

29 Opinion, point 10.
30 Jurisprudence-analysing working group: Applicability of the legal consequences of invalidity for loan contracts (summary opinion), p. 17.
31 Opinion, point 6.

formances should only be examined if the reason for invalidity is attributable to an imbalance in the value of the performances." The reasoning for the judgment points out that: "According to Section 237 (2) of the Civil Code, if the state of af fairs that existed before the signing of the contract cannot be restored, the court declares the contract in force for the period until a decision has been reached and orders monetary reimbursement for any performance that may have remained without counter-performance. As a main rule, therefore, the court *must examine not the balance in value of the performances, but only whether there is a performance for which no counter-performance has occurred.* In the context of invalidity, an examination of the balance in value of the performances can only take place if the contract is a usurious contract, or if the invalidity of the contract is established due to contestation on the grounds of a conspicuous disproportion in the value of the performances. (…) The stance of the Curia, however, is that when declaring a contract in force it is generally not a requirement that the court should retroactively examine or bring about a balance in value of the parties' performances. *It must only take steps to ensure that, in the event that one party has already delivered its performance while the other party has not yet fulfilled its own performance, this should then occur."* In the lawsuit in question, the Curia took this reasoning as its basis for drawing the legal consequence of invalidity of a lease agreement in such a way that it declared the contract in force, but – given that the reason for invalidity did not lie in the proportional relationship between the performance and counter-performance – did not change the amount of the lease fee specified in the invalid contract. Similar reasoning is apparent in judgment BDT2010. 2351.[32]

In a decision in the context of settlement, the court considered at what price the parties should be obligated to settle in the event of a performance remaining without counter-performance: settlement occurred at the price set in the invalid contract.[33] The same idea appeared in another decision in the context of settlement, in which the court pronounced that "for as long as the contract remained in force, proper use of the thing constituting the object of the contract was due to the plaintiff, while the paid fee was due to the defendant based on the contract concluded between the parties in their own right; and for this reason, when the contract ceased to be in force, the court had to take this into account when ordering reimbursement of the consideration for any performance that may have remained without counter-performance."[34]

Declaring a contract in force until a judgment has been reached means that the

32 It is worth noting that in the lawsuits in question there was no instance of a performance remaining without counter-performance, so that the judgments contain no direction as to how the settlement of accounts must proceed.

33 BDT2014. 3111.

34 BDT2010. 2352.

court accepts the performance that has occurred on the basis of the contract so far, while settling the legal relationship with regard to the future. When declaring a contract in force in this way, the court in making its judgment *draws a strict line: what has happened until then under the title of performance of the contract is unaffected; at the same time, given that the contract is invalid with respect to the future, neither performance nor counter-performance can be demanded in the future on this basis, while the consideration for any performance already delivered without corresponding counter-performance must be reimbursed.* The consideration must be identical in value; otherwise one or other of the parties would gain a financial advantage.

As interpreted here, the declaration of a contract in force *may appear to raise concerns on two points:* on the one hand, if the parties have already delivered the performance pursuant to the contract, then in the final analysis declaring the contract in force leads to the same result as declaring the contract valid, which would appear to contradict the goal of the legal institution. And on the other hand, if the reason for invalidity does not lie in the proportional relationship between the performance and counter-performance, then by declaring the contract in force the court allows the party offering the performance to gain the profit set down in the contract. A possible response to the first concern is that *the legal consequences of invalidity do not provide a solution for every legal relationship.* In the case of already fulfilled, irreversible legal relationships, if the contract cannot be declared valid then the infringement must be sanctioned in some other way. One typical method for this is restitution. With regard to the second concern, we must begin from the assumption that *if the court intervenes in the contract and, during settlement, compels the party to pay for the counter-performance minus the profit, then the party making use of the performance would be enriched* because it would gain access to the performance at a price which is unattainable on the market. This solution would be likewise unjustified, and for this reason it is reasonable for settlement between the parties to take place on the basis of the contract.

*4.5.2 Declaration in force in the case of loan contracts*

As a consequence of declaring a loan contract in force, *the performance of each party thus far does not lose its legal basis, and so neither party is obliged to return it.* This means that the debtor was entitled to use the loan, while the creditor was entitled to the interest and credit fee received. *With regard to the future, however, the debtor cannot use the loan, which it is obligated to repay* (failure to repay the loan amount held would result in unjust enrichment), *while the creditor is not entitled to any more interest.* When declaring a contract in force, therefore, the court must determine the extent of the debtor's outstanding principal, and order the payment of this amount via a constitutive judgment.

The court's judgment cannot interfere with performance delivered up until the time the judgment is handed down, except if the performances delivered by the parties were not equal in value, whether because the creditor collected more than they were entitled to, or because the debtor is in arrears with their interest payments. In this event, the party in arrears must be compelled to fulfil its obligations due up to the date of declaring the contract in force, in accordance with the conditions of the contract that has been declared in force.

## 5. CURRENCY OF THE DEBT

### 5.1 Introduction

Below we examine *which currency the court employs in ordering the debtor to pay off their debt when declaring a contract in force.* In doing this, we take as our starting point the Curia's declaration that foreign currency-based loan contracts are foreign currency contracts. "The parties determined the monetary debts of both the creditor and debtor arising from the loan contract in foreign currency (the money of account), which both parties were obligated to pay in Hungarian forints (money of payment)."[35] In order to determine the currency in which the court orders payment, a more detailed examination of the concept and significance of *the money of account and the money of payment* is necessary.

### 5.2 The concept of a monetary debt

Although monetary debt or payment obligation is one of the most fundamental concepts of civil legal relations, its definition is not set down in the Civil Code. The uniform standpoint of the legal literature is that in the absence of a definition, we may regard a thing as money which fulfils the economic function of money. "When, however, the question is not of interpreting some specific provision of law, but concerns money and monetary debts in general, then without doubt we must regard those things (currencies) as money which at a given place and time fulfil money's roles of an economic and legal nature."[36]

The concept of monetary debt can be derived from Section 231 of the Old Civil Code, and from Section 6:45 (1) of the New Civil Code. According to this section, a

35 Uniformity Decision, point 1.

36 Bátor, Viktor (1941), p. 226. It follows from this definition of money that the Civil Code only views debts that correspond to the above definition of money as monetary debts. Not qualifying as a monetary debt, therefore, is a monetary unit debt, whereby a party undertakes an obligation to hand over a specific piece of money, and likewise not belonging here is a currency debt, where a party undertakes an obligation to pay a specific currency (e.g. exclusively euro).

monetary debt – in the absence of any stipulation to the contrary – must be paid in the currency valid in the place of performance. A debt determined in another currency or in gold must be converted taking the exchange rate valid at the place and time of payment as the basis.[37]

It follows from this definition, in the case of a monetary debt, that *the parties determine the monetary debt not directly, but always by means of a value equation*. As *Grosschmid*, *Bátor* and *Meznerics*, among others, pointed out: in the case of a monetary debt, the debtor undertakes that when the debt falls due he will pay an amount in the currency of the money of payment that equals the debt imposed in the contract in the currency of the money of account. The difference between the money of account and the money of payment, therefore, is relevant in the case of every monetary debt. Even in the case of a debt imposed in forints in Hungary, to be paid in Hungary according to the date of signing of the contract, one must remember that *the money of payment can only be determined at the time of payment*. It follows from the difference between the concept of money of account and money of payment that a change in the Hungarian legal tender and the place of performance automatically determines, without amendment of the contract, the currency in which the debtor will be obligated to pay. If the euro becomes Hungary's legal tender, then every previously imposed debt – in the absence of an agreement between the parties to the contrary – will be liable to be redeemed in euros. If, on the other hand, the place of performance changes following the signing of the contract, this new place of performance will determine the currency in which the debt is redeemed.[38] In view of all this, it is necessary to examine the concepts of the money of account and the money of payment.

### 5.3 Money of account; the principle of free calculation

The pre-war and post-war literature on civil law treated the difference between the money of account and the money of payment as evident, and even during the period of foreign currency restrictions, Hungarian law largely recognised the right of the parties to choose the money of account (the so-called principle of free calculation).

*Béni Grosschmid* sets down the principle of free calculation within the heading of Money of Account, under the subheading Basic Principles. "The debt can be

37 Essentially the Commercial Code of 1875 contained an identical provision. Section 326 of this law specified that: "If the contract deals with a calculation value or currency which is not in circulation in the place of performance, then payment takes place at the place of performance on the date of maturity in the national currency according to the quoted exchange rate."

38 Section 279 of the Old Civil Code; Section 6:44 (3) of the New Civil Code.

imposed in any currency which is at all suitable for this, in domestic or foreign."[39] *Grosschmid* already uses the phrase that the money of account represents the "backbone" of the debt: "other designations that present themselves (in place of money of account): calculation, backbone, basic amount, etc."[40]

*Grosschmid* uses an apt analogy to present the difference between the money of account and the money of payment. He likens the difference between the two currencies to a situation where the contract would specify: "You provide 10 hundredweight of wheat in grain. Meaning: as much grain (whatever it be: wheat, rye, a mixture of the two, etc.) which at the prevailing value = 10 hundredweight of wheat. (...) The 10 hundredweight of wheat (...) is the money of account."[41]

*Grosschmid* also examines the question of in what currency the court can order payment: "In which currency should payment be ordered? In the money of account. As also with an order or execution of distraint."[42] "So that there is therefore no question that the foreign-currency debt, either at maturity or as a consequence of default, would be transformed into the domestic currency (valuta fori)."[43]

Like *Grosschmid*, *Szladits* made a distinction between the money of account and the money of payment as above. "Accordingly, in a monetary debt in the narrower sense, there is a conceptual difference between the mode of imposing and the mode of paying a monetary debt. Conceptually a distinction must be made with every monetary debt between the money of account and the money of payment: one determines the content of the obligation, while the other the actual means of payment."[44]

The same approach was taken by *Viktor Bátor*, who stated that the content of the debt is essentially defined by the money of account, the "backbone of the debt"; this is what determines how much of the money of payment must be provided to perform the obligation, meaning that the content of the debt is defined by the money of account, not by the money of payment. The debtor (including in this context the creditor who is obliged to make the loan available) always performs the original obligation, whatever the money of payment actually provided. *Bátor* points out as self-explanatory that: "Whatever currency the payment of the debt was made in, the creditor did not loan the amount of money in which that payment was made, but the amount of money of which it carried out the payment in order to write off the debt."[45]

39 Grosschmid, Béni (1932), p. 237.
40 Grosschmid, Béni (1932), p. 237; and in the same way, see: Viktor Bátor (1941), p. 269.
41 Grosschmid, Béni (1932), p. 238.
42 Grosschmid, Béni (1932), p. 501.
43 Grosschmid, Béni (1932), p. 519.
44 Szladits, Károly (1933), p. 49.
45 Bátor, Viktor (1941), p. 177.

The monograph by *Iván Meznerics*, published in 1944, contained the following main conclusions. "Monetary debts may be imposed in any kind of asset (free calculation)."[46] "Our national legal system and most European legal systems also recognise the key principal of the imposition of monetary debts, namely that the debt may be imposed in any kind of asset (free calculation system)."[47] Moreover, with regard to the restrictions due to the war, the author expressly emphasises that "the contracting parties are free to choose the asset of account even during the period of currency restrictions."[48]

*Meznerics* examines whether the debt may be imposed in a currency other than the legal tender of the place of performance in transactions between domestic and foreign residents, as well as between domestic residents. His answer to both questions is in the affirmative. "Currency regulations do not limit the parties' freedom to transact (...) in determining the money of account of the debt. In other words, the parties may determine the amount of monetary services in any kind of asset, including a foreign currency, even during a period of foreign currency restrictions."[49] To corroborate the above, *Meznerics* quotes the judgment of the Curia, which states that: "no law prohibits the assumption of an obligation in a foreign currency or unit of calculation; provided that it is not aimed at, or does not result in, the disruption or endangerment of ordinary economic activities, this does not violate the order of the state's existence."[50]

As regards the currency in which the court orders payment, *Meznerics* concurs with the aforementioned stance of *Grosschmid*: "In theory, therefore, the judgment of the court may not convert a debt imposed in a foreign currency to the domestic currency."[51]

*This confirms the accuracy of the statement set out in Point 1 of the Uniformity Decision; namely, that in civil law a foreign currency-denominated loan (i.e. when payment is made in ) cannot be differentiated from a foreign currency loan (i.e. when payment is also made in foreign currency).* The reason for this is that the parties are entitled to the right of free calculation, i.e. they may choose any currency as the money of account in the absence of a legal prohibition.

This option does not only exist in the case of foreign currency loans: in the office rental market, for example, there are hardly any contracts where the money of account is not the euro. As far as these transactions are concerned, no one has ever claimed that the principle of free calculation is only applicable to the parties

46 Meznerics, Iván (1944), p. 35.
47 Meznerics, Iván (1944), p. 36.
48 Meznerics, Iván (1944), p. 37.
49 Meznerics, Iván (1944), p. 43.
50 P VII. 586/1935.
51 Meznerics, Iván (1944), p. 38.

if the activities of at least one of the parties are linked to the given currency (e.g. in the case of the money of account for rental being the euro, where the lessee earns income or the lessor incurs payment obligations in euros). Moreover, as we have already pointed out above, according to Section 231 (1) of the Old Civil Code and Section 6:45 (1) of the New Civil Code, the general rule in the case of monetary debt imposed in a foreign currency and payable in Hungary is that debts should be paid in Hungarian forints irrespective of the money of account. As supported by the quotations above, the content of monetary debt is determined by the money of account, while the importance of the money of payment lies only in the settlement of the debt. The same conclusion follows from the foregoing as was concisely reflected in the Uniformity Decision: namely, that *a foreign currency-denominated loan contains a foreign currency debt and, therefore, qualifies as a foreign currency loan from the point of view of civil law.* In other words, the designation "foreign currency-denominated loan" only serves the purpose of differentiation from a foreign currency loan with an "effectivity" clause (commonly referred to as a "genuine foreign currency loan").

### 5.4 Money of payment

*In the specialist literature, the settlement of monetary debt is referred to as payment ("lerovás" in Hungarian) and the currency in which monetary debt is to be settled is referred to as the money of payment ("lerovó pénznem").* The rules of the money of payment are clearly provided for in Section 231 (1)-(2) of the Old Civil Code and Section 6:45 of the New Civil Code: A monetary debt shall be settled *in the legal tender at the place and time of settlement*, converted at the exchange rate in effect at the place and time of settlement. This rule has remained applicable in Hungarian law in essentially unchanged form. According to *Grosschmid's* definition: "In the absence of a provision to the contrary, the debt shall be paid (...) in the currency that is the legal tender (and also the common currency) at the place and time where and when the payment is made."[52] *Grosschmid* takes the clear stance that this amount is only relevant in respect of the settlement and not the debt itself; this is why he refers to the money of payment as the amount "to be accounted, calculated, provided."[53] "The money of account is looked upon as the finite substance itself, and not only the measure of some other substance."[54]

*It follows from the non-mandatory nature of the provisions of the Civil Code pertaining to contracts that the parties are also free to determine the money of payment.* The parties may agree to add a clause to the contract whereby monetary

52 Grosschmid, Béni (1932), p. 384.
53 Grosschmid, Béni p. 384.
54 Grosschmid, Béni p. 385.

debt is to be settled in a currency other than the legal tender of the place of settlement, usually in the money of account. The money of payment determines the legal tender that may be used to settle the given debt (however, it is not a determinant factor as far as the qualification of the monetary debt is concerned). Payment in the money of payment shall settle the debt expressed in the money of account.

To demonstrate this through an example: A debt of EUR 1,000 can be settled in Hungary by payment of 300,000 (assuming an exchange rate of 300/EUR). In the case of a loan contract, payment of 300,000 corresponds to the performance of a disbursement or repayment obligation of EUR 1,000. In other words, the lender grants a loan of EUR 1,000 and the debtor thus incurs a repayment obligation of EUR 1,000 that will in all likelihood have to be settled in Hungarian forints. However, should the circumstances of the transaction change (e.g. Hungary joins the eurozone; or the lender assigns the receivable to an Austrian national and consequently the debt needs to be settled in Austria; or the debtor relocates to Canada and becomes subject to enforcement proceedings in that country), then the money of payment may change – without prejudice, however, to the amount of the debt.

### 5.5 Summary: currency of the debt and currency in which the court orders payment

It follows from the foregoing that *the debtor's debt exists in the money of account, while the money of payment of the outstanding debt depends on the provisions of the contract. In the absence of contractual provisions to the contrary, the debt must be paid in the legal tender at the place and time of settlement.*

Accordingly, in the case of a foreign currency loan, the debtor's debt exists in a foreign currency (typically in Swiss francs or euros, or in exceptional cases in Japanese yen). As is clear from the quotes above, *the court will order the debtor to pay in the money of account in case of the debtor's default or the invalidity of the contract.* This position is fully aligned with the Circular of 29 October 2012 from the head of the Civil Department of the Curia, which concluded in relation to ordering the enforcement of claims expressed in a foreign currency that: "If the money of account is the euro and the money of payment is the forint, then the accurate wording would be 'the value corresponding to EUR 500,000 at the time of payment' or 'the equivalent of EUR 500,000 at the time of payment'; if, however, the money of account is the forint and the money of payment is the euro, then the accurate wording would be 'the EUR value corresponding to 15,000,000 at the time of payment' or 'the EUR equivalent of 15,000,000 at the time of payment'." In this regard, the Circular rightly points out that if the enforcement order did not set out the outstanding debt in the money of account, it would interfere with

the agreement between the parties and would allocate the risk of an exchange rate variation occurring between the issue and the implementation of the enforcement order differently from the contract.[55]

*It follows from the foregoing that the court must determine the principal of the debt in the money of account, while the debtor must pay the debt in Hungarian forints, in the absence of an agreement to the contrary in the contract.*

## 6. THE LIMITATION PERIOD OF THE CLAIM

### 6.1 The connection between limitation and invalidity in the case of loan contracts

In view of the long duration of loan contracts, *it should also be considered whether or not the claim to be enforced in the lawsuit has lapsed*, as the settlement by the court of the legal relationship between the contracting parties as the legal consequence of invalidity may only take place within the term of limitation or adverse possession. (Various claims may arise from invalid contracts. We only consider the issue of limitation here as far as it relates to the secondary legal consequences of invalidity. In addition, one should also bear in mind that in the case of nullity of a contract, the primary legal consequences of invalidity shall apply without time limitation,[56] while in the case of avoidance, the time limitation for the enforcement of claims is one year pursuant to the Old Civil Code[57]; however, a party may invoke the invalidity of the contract as an objection without time limitation.[58])

The starting point of the analysis should be that the limitation period commences when the claim falls due.[59] *Therefore, in order to determine the start date of the limitation period, one needs to determine the due date of the claim.*

As pointed out by *István Gárdos* in his critique of the rules of limitation contained in Act XXXVIII of 2014 (on the settlement of individual questions relating to the Curia's uniformity decision pertaining to consumer loan contracts of financial institutions), four kinds of claims arise from loan contracts: *(a)* the disbursement of the loan; *(b)* the maintenance of the loan for the contractual term; *(c)* the repayment of the loan; and *(d)* the payment of interest.[60] The claim related to the *disbursement of the loan* becomes due at the time specified in the contract, which marks

55 http://www.lb.hu/hu/sajto/kuria-polgari-kollegiuma-vezetojenek-2012-oktober-29-ei-korlevele-kollegiumvezetok-reszere-az

56 Section 234 (1) of the Old Civil Code; Section 6:88 (1) of the New Civil Code

57 Section 236 (1) of the Old Civil Code; Section 6:89 (3) of the New Civil Code

58 Section 236 (3) of the Old Civil Code; Section 6:89 (4) of the New Civil Code

59 Section 326 (1) of the Old Civil Code; Section 6:22 (2) of the New Civil Code

60 Section 523 of the Old Civil Code; Section 6:383 of the New Civil Code

the beginning of the limitation period (prescription). The obligation to *maintain the loan*, on the other hand, is a typical case of a continuous service obligation to which the lender is subject throughout the term of the contract, and thus its lapse is out of the question during the existence of the legal relationship. The debtor's obligation to *repay the amount of the loan* is a common monetary debt and a single payment obligation in respect of the total amount of the loan, irrespective of whether repayment is due in one sum or in instalments. Accordingly, the limitation period of the lender's claim for the repayment of the loan begins on the final deadline for repayment of the loan. Conversely, the *obligation to pay interest* may not be considered a single or continuous service. The debtor enjoys the right to use the loan amount from the date of disbursement. The interest is, therefore, the consideration for the service rendered, already earned by the lender, for which the limitation period thus commences irrespective of the limitation period of the principal.[61]

At the same time, *the applied legal consequences of invalidity also have relevance* as far as limitation is concerned, since the perception of the issue is different depending on whether restitutio in integrum has occurred or the contract has been declared in force.

### 6.2 The start date of limitation in cases where the contract is declared in force

In cases where the contract is declared in force, the court will not take into consideration services performed during the period preceding the judgment, but will rather make a constitutive judgment ordering reimbursement of the consideration for any performance that may have remained without counter-performance. *The claim referred to in the judgment is conceptually established as a result of the court's judgment, and therefore cannot lapse earlier.*

### 6.3 The start date of limitation in cases of restitutio in integrum

The situation is different in cases where restitutio in integrum occurs. As the primary legal consequence of invalidity is that no rights may be established on the

61 For more details see: Gárdos, István (2014). Resolution No. 34/2014 (XI. 14) of the Constitutional Court, which was published after the submission of this study, stated with regard to Section 1 (6) of Act XXXVIII of 2014 on limitation – unfortunately without offering any reasoning – that "contrary to certain opinions in the legal literature, it is a constitutionally acceptable position that in these cases individual claims may not lapse independently during the term of the contract." Based on the above statement, the Constitutional Court argued that "the limitation period only commences at the termination of the contractual relationship as per the contract. In other words, the limitation periods of the individual payments and claims cannot separately commence as long as the debtor's debt to the financial institution (and thus the financial institution's claim from the debtor) is outstanding, i.e. the claims associated with the payments made by the debtor cannot lapse independently." (Rationale [136].)

basis of such transactions,[62] services performed pursuant to such contracts are regarded as lacking legal basis from the date of the services, i.e. the reimbursement obligation becomes due immediately at the time of performance of the services. *It follows from the above that the start date of limitation in the case of loan contracts is the date of disbursement of the loan.*

Legal declarations related to the loan that may interrupt the limitation of a claim based on the contract *shall not interrupt the limitation* of the claim for restitutio in integrum. Consequently, the problem arises in respect of loans disbursed more than five years ago that *the claim for the repayment of the principal has lapsed.* The reason for this is that the application of restitutio in integrum disregards the circumstance whereby, in the case of a loan contract, the obligation to repay the principal does not only follow from the restitution but also applies under the original contractual terms and conditions, as the debtor only received the loan amount for temporary use (as opposed, for instance, to the obligation of the repayment of the purchase price in the case of a sale and purchase agreement). This is the root cause of the absurd consequence whereby the "same" principal claim that may not even be due under the contract could already have lapsed in the case of invalidity of the contract. We believe this is a further argument against the application of restitutio in integrum in the case of loan contracts. In fact, limitation itself leads to the same result since – in view of the fact that restitutio in integrum is only possible by the mutual restitution of already performed services – the enforcement of an objection to the limitation results in subsequent irreversibility and excludes the applicability of this legal consequence.

It may also arise that the problem of limitation may be remedied by the rules of *suspension* of limitation. According to the Old Civil Code, limitation is suspended if the obligee is unable to enforce a claim for an excusable reason. An argument in favour of the application of the rules of suspension is that the parties were typically unaware of the invalidity of the contract in the case of the loan contracts under consideration. In judicial practice, however, *only an objective circumstance may be considered an excusable reason, and ignorance of the invalidity of the contract is not such a circumstance* (unless the party was prevented from becoming aware of the invalidity or from enforcing its claim for an objective reason). Accordingly, the fact that the parties were unaware of the invalidity of the contract does not result in the suspension of the limitation period.

62 Opinion, point 2.

### 6.4 The start date of limitation in the case of monetary restitution for unjust enrichment

As we have already discussed earlier, *declaration of the contract in force is replaced in the New Civil Code by monetary restitution for unjust enrichment.*[63] The fundamental concept behind declaration in force and restitution for unjust enrichment is the same: the court does not take into consideration the services already performed by both parties, but only orders the monetary restitution of services in respect of which no consideration has been paid.[64] An essential difference, however, is that while in the case of declaration in force the court settles the legal relationship between the parties by means of a constitutive judgment, in the case of restitution for unjust enrichment (similarly to the case of restitutio in integrum) *the court settles the legal relationship between the parties with a declaratory judgment.* It follows from this that, under the New Civil Code, the rules outlined above regarding the limitation period of claims for restitutio in integrum also apply to cases where restitution for unjust enrichment is ordered by the court.

## 7. DECLARATION IN FORCE IN THE CASE OF ANNUITY-BASED CALCULATION OF INTEREST

We have explained above that in the case of loan contracts it is possible to declare a contract in force until a judgment is reached, and we have pointed out that the court must accept already performed services and order reimbursement of the consideration for any performance that has remained without counter-performance in its judgment. In order for this to happen, the court, as a general rule, needs to determine the balance of the outstanding principal. *For the purposes of settlement of the legal consequences of invalidity, however, one should also bear in mind that the interest calculation method applied in loan contracts was in most cases different from the method provided for in the Old Civil Code.*

The interest calculation rule of the Old Civil Code is based on the concept that interest is the consideration paid for the right of use of the lender's money. It follows from the above rule that *the interest paid during the term of the loan gradually decreases as the outstanding principal balance also decreases.* If the loan amount is 12 million, the annual interest rate is 12%, and the debtor repays the loan over a period of 20 years, then the instalments will be as follows:

63 Section 6:113 of the New Civil Code.
64 Section 6:113 (1).

| Number of months | Principal repayment HUF | Outstanding principal HUF | Interest (12% per annum) HUF | Total instalment HUF |
|---|---|---|---|---|
| 12. | 600,000.00 | 11,400,000.00 | 1,440,000.00 | 2,040,000.00 |
| 24. | 600,000.00 | 10,800,000.00 | 1,368,000.00 | 1,968,000.00 |
| 36. | 600,000.00 | 10,200,000.00 | 1,296,000.00 | 1,896,000.00 |
| 48. | 600,000.00 | 9,600,000.00 | 1,224,000.00 | 1,824,000.00 |
| 60. | 600,000.00 | 9,000,000.00 | 1,152,000.00 | 1,752,000.00 |
| 72. | 600,000.00 | 8,400,000.00 | 1,080,000.00 | 1,680,000.00 |
| 84. | 600,000.00 | 7,800,000.00 | 1,008,000.00 | 1,608,000.00 |
| 96. | 600,000.00 | 7,200,000.00 | 936,000.00 | 1,536,000.00 |
| 108. | 600,000.00 | 6,600,000.00 | 64,000.00 | 1,464,000.00 |
| 120. | 600,000.00 | 6,000,000.00 | 792,000.00 | 1,392,000.00 |
| 132. | 600,000.00 | 5,400,000.00 | 720,000.00 | 1,320,000.00 |
| 144. | 600,000.00 | 4,800,000.00 | 648,000.00 | 1,248,000.00 |
| 156. | 600,000.00 | 4,200,000.00 | 576,000.00 | 1,176,000.00 |
| 168. | 600,000.00 | 3,600,000.00 | 504,000.00 | 1,104,000.00 |
| 180. | 600,000.00 | 3,000,000.00 | 432,000.00 | 1,032,000.00 |
| 192. | 600,000.00 | 2,400,000.00 | 360,000.00 | 960,000.00 |
| 204. | 600,000.00 | 1,800,000.00 | 288,000.00 | 888,000.00 |
| 216. | 600,000.00 | 1,200,000.00 | 216,000.00 | 816,000.00 |
| 228. | 600,000.00 | 600,000.00 | 144,000.00 | 744,000.00 |
| 240. | 600,000.00 | 0.00 | 72,000.00 | 672,000.00 |
| **Total** | **12,000,000.00** | | **15,120,000.00** | **27,120,000.00** |

In loan contracts, however, instalments are normally determined in a way that *the amount of the instalment is the same every month (annuity-based calculation of interest).* The ratio of the interest within the instalment decreases gradually while the ratio of the principal keeps increasing in parallel. In the case of annuity-based calculation of interest, the debtor pays mainly interest at the beginning of the loan term. The following table illustrates the instalments payable in the case of annuity-based calculation of interest using the same parameters as the previous example.

| Number of months | Principal repayment HUF | Outstanding principal HUF | Interest (12% per annum) HUF | Total instalment HUF |
|---|---|---|---|---|
| 12. | 153,843.02 | 11,846,156.98 | 1,431,721.01 | 1,585,564.03 |
| 24. | 173,354.17 | 11,672,802.81 | 1,412,209.86 | 1,585,564.03 |
| 36. | 195,339.82 | 11,477,462.99 | 1,390,224.22 | 1,585,564.03 |
| 48. | 220,113.80 | 11,257,349.20 | 1,365,450.24 | 1,585,564.03 |
| 60. | 248,029.73 | 11,009,319.46 | 1,337,534.30 | 1,585,564.03 |
| 72. | 279,486.11 | 10,729,833.35 | 1,306,077.92 | 1,585,564.03 |
| 84. | 314,931.95 | 10,414,901.40 | 1,270,632.09 | 1,585,564.03 |
| 96. | 354,873.20 | 10,060,028.20 | 1,230,690.83 | 1,585,564.03 |
| 108. | 399,880.01 | 9,660,148.20 | 1,185,684.03 | 1,585,564.03 |
| 120. | 450,594.80 | 9,209,553.40 | 1,134,969.23 | 1,585,564.03 |
| 132. | 507,741.50 | 8,701,811.90 | 1,077,822.53 | 1,585,564.03 |
| 144. | 572,135.83 | 8,129,676.07 | 1,013,428.20 | 1,585,564.03 |
| 156. | 644,696.97 | 7,484,979.10 | 940,867.06 | 1,585,564.03 |
| 168. | 726,460.69 | 6,758,518.41 | 859,103.35 | 1,585,564.03 |
| 180. | 818,594.08 | 5,939,924.33 | 766,969.95 | 1,585,564.03 |
| 192. | 922,412.30 | 5,017,512.03 | 663,151.73 | 1,585,564.03 |
| 204. | 1,039,397.27 | 3,978,114.76 | 546,166.76 | 1,585,564.03 |
| 216. | 1,171,218.86 | 2,806,895.90 | 414,345.17 | 1,585,564.03 |
| 228. | 1,319,758.73 | 1,487,137.17 | 265,805.30 | 1,585,564.03 |
| 240. | 1,487,137.17 | 0.00 | 98,426.86 | 1,585,564.03 |
| **Total** | **12,000,000.00** | | **19,711,280.65** | **31,711,280.65** |

A key difference between the two methods of interest calculation with relevance to the legal consequences of invalidity is that *annuity-based calculation of interest only reflects the agreement between the parties if the contract terminates upon repayment under the original terms and conditions* (duration, number of instalments, date of maturity), *as in such cases, overall, the debtor actually pays the interest due on the principal.* If, however, repayment is not made pursuant to the contract because, for example, the court declares the contract in force in view of its invalidity and orders the repayment of the outstanding principal in one sum, then

*the debtor will have made an overpayment as they will be paying interest on principal that remains unused as a result of the court's judgment.* Based on the above example, if the court declares the contract in force at the end of the fourth year, then the debtor will find themselves having made an "overpayment" of 271,604 compared to the principal-based calculation of interest (as in the case of time-proportionate repayment they would have paid 5,328,000 in interest), while in the case of annuity-based calculation of interest they will have paid 5,599,605, with the overpayment being the difference between the above two amounts.

*The difference between the two methods of interest calculation* is depicted in the two diagrams below, illustrating the different principal and interest content of the repayment instalments of the loan granted under the above terms and conditions.

**Chart 1**
**Principal-based calculation of interest**

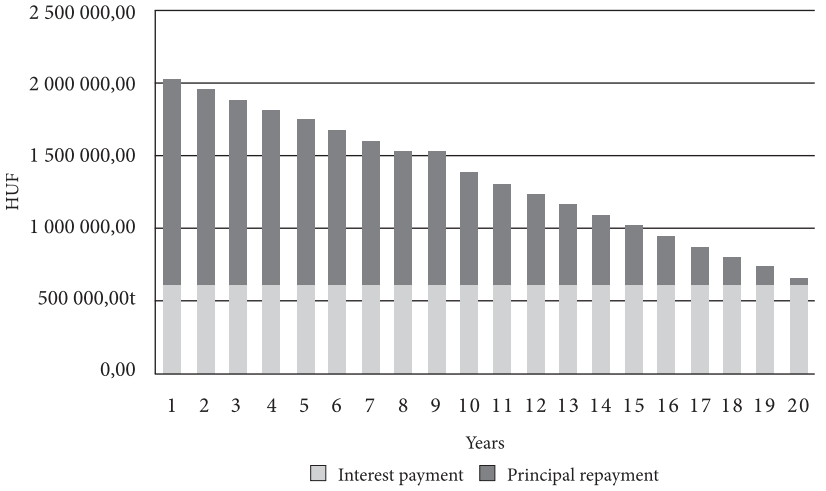
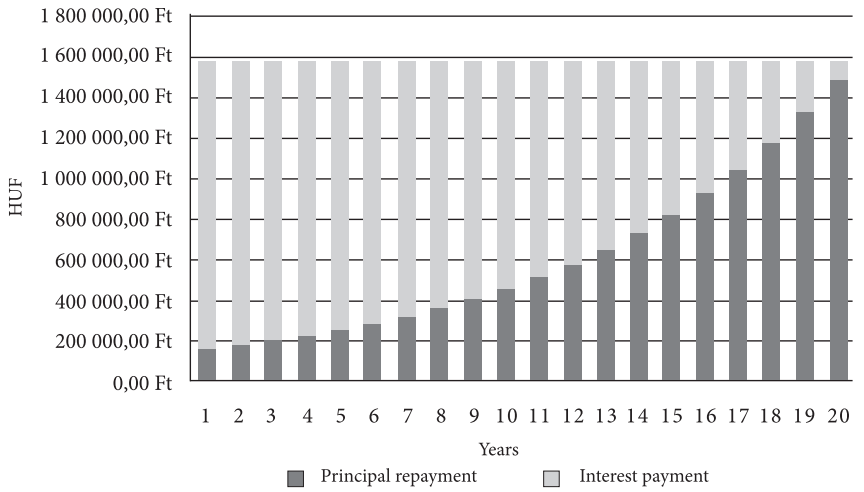


**Chart 2**
**Annuity-based calculation of interest**




*In this way, if the court declares the contract to be in force as a legal consequence of invalidity, then in the case of annuity-based calculation of interest, the outstanding principal must be determined in a way that also takes into account the extent of the debtor's overpayment in respect of the interest.*

## 8. SUMMARY

Based on the foregoing, in our opinion, a loan contract is a legal relationship that is aimed at the acquisition of the right of use of the lender's money by the debtor, rather than the transfer of ownership of an asset. Consequently, restitutio in integrum is impossible due to the original irreversibility of the service, in accordance with point 3 of the Opinion. Even if we set the above aside, in the majority of lawsuits arising as a result of the 2008 economic crisis the impossibility of restitutio in integrum should be established due to subsequent irreversibility, since the party claiming restitutio in integrum would not be able to repay the loan received. Finally, the impossibility of restitutio in integrum also follows from the (partial) limitation on claims arising under the legal relationship.

As a result of the impossibility of restitutio in integrum (if the cause of invalidity cannot be remedied by the court), the contract must be declared in force until the date of judgment. In such cases, the court will determine the amount of the outstanding principal in its judgment, taking the money of account as a basis, and will oblige the debtor to pay this amount.

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