Position of experts of the Responsible Finance Club at the European Financial Congress regarding case C-520/21

The decision in case C-520/21 requires the CJEU inter alia to address several important issues:

- whether money changes its value over time,
- whether - if the long-term contract under which the bank made capital available to its client is found, after a certain time, to have been concluded invalidly - the bank is entitled to the repayment of the capital, including the cost of the non-contractual use of capital, and
- whether the instalments repaid by the client to the bank may be treated as equivalent to the capital made available to the bank and, therefore, whether the client is entitled to claim from the bank a remuneration for the use of the capital.

These questions are related to a specific, individual case pending before the national court. However, their essence comes down to fundamental economic issues. That is why the position of the CJEU will affect the settlement of all long-term obligations, regardless of the nature of the obligation, the type of contract or the validity of its conclusion, regardless of the assessment of the legal aspects of the contract. In other words**, the position that the CJEU will take on the change of money's value in time and the cost of using capital will have universal significance**[1].

The economic principle that money changes its value over time has not been questioned in the past. It constitutes one of the elements of financial mathematics. The value of money decreases over time.

That is why people invest their savings and investment income is capitalized (i.e. added to capital), which counteracts the depreciation of money and thus provides an incentive for economic activity and the basis for functioning of investment funds, including funded pension systems around the world. Also the basic method of valuing businesses (discounted cash-flow) is based on the changing value of money over time, which changes due to risk, inflation, macroeconomic policy and many other factors. Questioning this principle would mean automatic destruction of the development mechanisms of market economy and would undermine the sense of existence of many institutions e.g. pension funds, banks, stock exchanges and others.

There remains the question of remuneration for the use of capital. The primary purpose of providing capital is to generate profit.

One of the common way of providing capital are loans. Taking out a loan, which is then repaid, is intended to allow the borrower to finance his investment more quickly. An incomparably worse alternative would be to systematically save financial means. Suppose someone who wants to buy an apartment would have to save systematically for 20 years in order to accumulate means to buy an apartment. He can achieve this goal much faster by taking out a loan that he will be repaying over 20 years. In this case, he buys an apartment right away, solves his housing problem, but for 10 years he covers the cost of the capital that the bank lent him. Similarly, the owner of an apartment that is rented

[1] Experts of the European Financial Congress have already addressed these issues in August 2019 in the Open Letter (*amicus curiae brief*) from the Experts of the European Financial Congress to the Court of Justice of the European Union (case C-260/18).

to a tenant lends the tenant the capital with which he financed the apartment. If lending capital were not to involve remuneration, the owner would never engage in such a transaction.

Anyone who uses someone else's capital pays for it. Governments that issue government bonds pay interest to investors who buy those bonds. Banks take deposits and pay depositors for the possibility of trading them. Banks finance loans, such as mortgage loans, with these deposits and charge interest on the outstanding principal. This results, inter alia, from Article 69 par. 1 of the Banking Law Act. Means obtained from interest on loans finance the interest paid to depositors. Tenant uses the property owner's capital and pays him a fixed instalment for it. Examples, perfectly known from everyday life, can be multiplied. This phenomenon is commonly present in economic turnover.

In this case, however, a specific problem must be addressed: If a loan agreement regularly serviced by the borrower is declared invalid, is the bank obliged to pay him remuneration for the non-contractual use of the capital understood as instalments repaid by the borrower? In order to answer this question, it is first necessary to refer to the cash flows associated with the loan in question.

By signing the loan agreement, the client incurred a liability to the bank. According to the agreement, the client was obliged to pay the bank the loan instalment every month. He undoubtedly did so, because otherwise the bank would have called him to repay, and in the absence of a response would have even terminated the loan agreement. Therefore it must have been obvious to each party that the loan agreement was validly concluded and effective.

Flows went both ways:

- in accordance with the loan agreement, the bank has made means available to the client and now has a claim against the client in the amount of the outstanding principal,
- the client pays the bank monthly instalments consisting of an interest instalment and a principal instalment. The instalment paid to the bank is financed by client's means. The interest instalment is the bank's remuneration for providing capital, adjusted for inflation. The remainder of the instalment, that is the principal instalment, reduces the client's debt. This does not include treating the instalment as a capital expenditure.

The above description refers to a normal situation, when the client's contract with the bank is not questioned. It is now necessary to consider the consequences of questioning the contract or even declaring it as invalidly concluded.

It is sometimes assumed - wrongly in our opinion - that in such a case, all relations between the parties to the contract disappear, except for the claims of the client against the bank (the bank's claims against the client are already supposed to be time-barred). However, the matter is more complex.

When granting a loan, the order of procedure is as follows: the client submits to the bank a credit application signed by him, in which he precisely defines his expectations. The application is then analyzed by the bank and if it is accepted, the client receives a formal credit decision from the bank, which contains all relevant economic and financial data concerning the loan. If the client accepts it, a loan agreement is drawn up based on it. It follows that if the court declares a loan agreement as invalidly concluded, it in no way affects the documents on the basis of which the agreement was drawn up. And it is from these documents that all economic and financial issues arise. Thus, a challenge to the validity of the agreement does not affect the material economic and financial terms of the agreement. There is therefore a significant inconsistency here, since it is believed that once an agreement is declared as invalidly concluded, these terms cease to apply. However, it cannot be stated that the parties did not agree on the material terms of the agreement prior to the conclusion of the

agreement. Without the client's credit application there would be no credit decision by the bank, and without the client's acceptance of the credit decision there would be no basis for drawing up a written agreement. It appears that the acceptance of the credit decision has a nature of an oral agreement in which the parameters listed above were agreed upon. This agreement was never questioned by anyone.

In particular, there is no basis for treating the loan instalments paid by the client as making capital available to the bank by the client. Only in such a case it would be reasonable to consider the bank's potential fees to the client for the use of the capital made available by him. The consumer's performance in respect of the instalments does not have such a purpose and character as the bank's performance, which consists in making capital available for use. It is a mere repayment of a borrowed capital.

The question posed by the national court has a very significant meaning, as it concerns the fundamental principles of economics. Any mistakes in this area may even lead to destabilizing the economy, and given the importance of the CJEU's decisions for the establishment of EU law, they will have an impact on the entire common market. That is why it could be very helpful for the CJEU to seek an independent opinion of recognized EU experts in the area of economics, and especially finance.

To summarize:

- any lending of capital (both contractual and non-contractual) involves remuneration, which the beneficiary pays to the owner of the means;
- in the case of a loan, such remuneration is the interest instalment, which - if the loan agreement is declared invalid - should be excluded from mutual settlements;
- the value of money changes over time and therefore the remuneration paid to the owner of the means must be adjusted to take account of the change in money's value;
- there is no justification for treating the instalments paid to the bank by the client as capital for the use of which the client is entitled to remuneration.

On behalf of the experts of the Responsible Finance Club at the European Financial Congress:

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