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Economic Crisis – Contractual Relations in Hungary and in Europe

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Abstract. With the conclusion of a contract of civil law, the parties may take some reasonably unforeseeable economic risks that might disrupt the synallagmatic character of the contract; therefore, disproportionate, unviable extra burden may appear in the contractual relations on the side of some parties. The sudden increase of inflation or prices, the intense reduction of the purchasing power of wages, the radical changes in the relations between supply and demand, the collapse of the product market, the insolvency of the economic actors (especially in case of a contractual party), the negative changes of the market and financial relations and the production and liquidity problems of the economic sector shall result in this incalculable risk. In case of maintaining the original contractual content, an economic crisis affecting the whole economy and society of one or more countries may cause any or all the parties to take inequitable and intolerable risks.
In the following, we intend to analyse those reasons in the Hungarian judicial practice that are based on the Hungarian Civil Code and referred by the parties in order to get rid of the contractual obligation in the name of economic/business risk. Then we examine the importance of economic/business risk in those contractual relations that cannot be found in the Hungarian Civil Code and finally, we make a conclusion with respect to the current European regulations.

Keywords: economic/business risk, atypical contracts, Hungarian civil law, European regulation

I. The Legal Reasons of Obviating the Economic/ Business Risk According to the Hungarian Civil Code

In case of the framework contract about the sales of natural gas, because of the Russian-Ukrainian dispute on natural gas at the beginning of 2006, the gas service was hampered, therefore, for supplying heat, the plaintiff produced the necessary quantity by oil heating, while the defendant could not receive any subsidy for gas

prices during the period of suspension; the legal action taken by the defendant was based on the Section 4 of the Hungarian Civil Code.[1] There is no subsidy referring to that amount of gas which was not consumed, however, the defendant had the possibility to enforce his economic interests in connection with the potential business risk emerging by changing to oil heating: the plaintiff is not responsible for missing this opportunity by the defendant. The court held that the party neither violated the principle of good faith and integrity nor realised unfair conduct on the market by not warning his partner of the possible economic consequences, business risks of facts known by both parties.[2]

In order to pass on or share the business risk, the parties intended to use the legal term of implied conduct:[3] in the above mentioned suit,[4] in the second half of 1989 the parties had negotiations about concluding an agreement in principle about a partnership of which aim was to set up a joint venture, but at the time of the conclusion of the contract, the Soviet market collapsed.

The party losing the investment wished to get compensation for the outstanding profit based on the above mentioned rule of 'implied conduct'. The court held that the company itself had to cover the costs belonging to ordinary business risk that could emerge at the time of preparing the contract (e.g. in case of an investment that cannot be realised because of the bankruptcy of the product market of a country). In another judgment[5] the court held that in general it had no legal base to refer to the rule of 'implied conduct' so as to pass on the business risk.

In many litigations[6] the same mistaken assumption (Civil Code § 210 (3))[7] was the legal base for those contractual conditions to be voidable that became disadvantaged because of the business failure due to the negative economic circumstances; notwithstanding the court declared several times that – in theory – the expectations and ideas falling under the business risk cannot mean that the

1 (1) In the course of exercising civil rights and fulfilling obligations, all parties shall act in the manner required by good faith and fairness, and they shall be obliged to cooperate with one another.
(4) Unless this Act prescribes stricter requirements, it shall be necessary to proceed in civil relations in a manner that can generally be expected in the particular situation. No person shall be entitled to refer to his own actionable conduct in order to obtain advantages. Whosoever has not proceeded in a manner that can generally be expected in the particular situation shall be entitled to refer to the other party's actionable conduct.

2 BDT 2008. 1900. [Casebook of the Courts]

3 The court may award damages payable in full or in part by a party whose willful conduct has explicitly induced another, bona fide person to act in a manner that has brought harm to this person through no fault of his own.

4 BH 1996.586. [Court Order]

5 BH 1994. 179. [Court order]

6 2003/1. Arbitration decision.

7 If the parties had the same mistaken assumption at the time the contract was concluded, either of them may contest the contract.

contract can be voidable based on vitiated consent,[8] if the parties estimated the future increase of the prices of the contractual object to be less then it was in the reality, cannot be regarded as same mistaken assumption.[9]

In the following case the plaintiffs considered the contract about purchase of business shares to be voidable based on deceit.[10] Before concluding the contract the defendants informed them in writing about the financial situation of the ltd. The plaintiffs omitted to check if the future expectations of the defendants, the estimated economic results were realistic or the value of the business share reflected their expectations or not. The conclusion of the contract about the purchase of the business share happened in November, 1994, while the so called 'Bokros-package' came into force from December, 1994. This economic event which was unforeseeable by the ltd. and the defendants meant the economic milieu and the changes of the relations, therefore, the arbitration held that the risks emerging in the operation of the association after the conclusion of the transaction and influencing the financial situation of the association in a negative way, must be taken by the buyer of the business share.

Based on § 241 of the Civil Code, the court may modify the contract under three conjunctive conditions: the aim of the agreement must be a persistent legal relation, after concluding the contract the contractual relation must change, therefore, the contract interferes with an important and justified interest of one of the parties.[11] In the judicial practice it occurred several times that the alteration of the contract by the court based on the economic crisis could not be applied in default of one of the conjunctive conditions: (1) the circumstance itself that some contractual provisions can be mistaken due to the unexpected changes of the market and financial relations cannot be used as a legal base for the modification of the contract by the court, as an extra condition, the important and justified offense of interests of the party is required;[12] (2) in case of a legal action that aims to modify the persistent legal relation, it is not enough to refer to general circumstances (e.g. to changes of the price level) that emerged after the conclusion of the contract, but its influence on the contract has to be specified too.[13] In connection with the modification of the contract by the court, not only § 241 of the Civil Code was analysed but the conditions were interpreted too:[14] if the parties considered the future insecurity of the level of production and the way how the profit turned out to be a mutual risk at the time of the conclusion of the contract, the parties, when they specified the contractual conditions, had to calculate with these types of changes in the circumstances that

8 BH 1998.272. [Arbitration decision]
9 BH 1983.205. [Court order]
10 1997/6.
11 Török 2006. 319; *Gellért* 2007. 905; *Petrik* 2008. 423.
12 BDT 2007. 1707. [Casebook of the Courts]
13 BH 1977.118. [Court order]
14 BH 1984.489. [Court order]

were expected in the certain situation and which did not exceed the limits of taking risk; in this case the modification of the contract based on important and justified offense of interests cannot be claimed. Neither can be suggested the alteration of the contract by the court with reference to § 241 of the Civil Code if it is about the widespread consequences of the basic social-economic changes.[15] The inflation and the changes of the relations of supply and demand belong to the economic risk, which shall not entitle any party to suggest the modification and these do not lead to automatic modification of the contract.[16] The ordinary changes of the market cannot be cited as a legal base for the alteration of a unique contract by the court: by concluding a contract both parties take business risk, the alteration of the contract by the court cannot be considered as a possibility to eliminate or redistribute the business risk taken by the parties.[17] In conclusion, the Civil Code does not entitle the courts to alter the unique contracts in case of changes that affect the whole economy or the subjects of agreements that belong to different contractual types:[18] changes in the economic milieu, the collapse of the market of certain products can be considered as a significant change in the circumstances of the conclusion of the contract that cannot be expected at the time of the conclusion of the contract and of which risks have to be borne mutually by the parties.[19]

The obligated party has tried to refer to economic impossibility[20] in order to get rid of the contractual relations that became disproportionate because of the negative economic and market circumstances. The court held that the economic impossibility was not absurd, however, in case of bank loan contracts, the economic changes or changes affecting the market during the period of repayment can be considered as business risk that cannot be ignored by the borrower (debtor) at moment of concluding a long-term contract of loan, therefore he must take this risk.[21] In another suit the court held that the modification of the contract by the court cannot be suggested based on economic impossibility since according to § 241 of the Civil Code, the judicial modification and the declaration of the impossibility shall be regarded as two different provisions of the judgment that exclude each other mutually.[22]

We can mention examples when the obligated party gave notice of termination[23] (unilateral termination) in order to get rid of the contract which meant extra

15 BH 1992.123. [Court order]; Török 2006. 323; *Nochta* 2010. 211.
16 BH 1996, 145. [Court order]; BH 1993. 670. [Court order]; Török 2000. 325; *Nochta 2010.* 211.
17 2003/1. Arbitration decision; BH 1988.80. [Court order]; BH 1988.80. [Court order]; BH 1985.470. [Court order]
18 Gellért 2007. § 241 of the Civil Code.
19 BDT 200.277. [Casebook of the Courts]
20 Code Civil § 312 (1) *If performance has become impossible for a reason that cannot be attributed to either of the parties, the contract shall be extinguished.*
21 FIT 4.Pf.21.148/2009./4. [Decision of the High Court of Appeal of Budapest]
22 BDT 2000.277. [Casebook of the Courts]
23 The defendant terminated a contract of loan concluded with a credit institution based on § 525 (1).

burden for him. The court held,[24] the defendant (debtor) breached the contract by terminating it since he cannot refer to the unfavorable tendencies of which existence he knew when he concluded the contract as a reason of the notice of termination. When judging the financial situation, the loss of revenue, the negative changes of the market and liquidity problems cannot be accepted, the real reason of the termination must be considered by the facts revealed later.

The above mentioned analysis following the dynamics of the contract demonstrates well that Hungarian courts regard the economic-financial crisis as a contractual risk and they use the principle *pacta sunt servanda*[25] instead of a broader sense of the *clausula rebus sic stantibus*. Similarly to the domestic courts, the European Court – the judicial practice of which affects the domestic judicial practice of the member states[26] – also considers the business-financial crisis to be contractual risk and the different actors of the economy shall take the risks in connection with their activity. For in every contractual relation there is a risk that one of the parties may not fulfil the agreement in an adequate way or becomes insolvent, in this case the parties must reduce the risk suitably in the contract itself.[27]

II. The Importance of the Economic/Business Risk in Case of Contracts not Included in the Hungarian Civil Code

In the following, we analyse the atypical and business association contracts from the aspect whether the business/financial crisis can be considered to belong to contractual risk.

In case of some atypical contracts we can deduce that the economic/business risk is part of the contractual risk:

– in case of distance contract, the consumer is not entitled to the right of objective cease (if not agreed otherwise) in connection with the changes of the prices or charges depending on a fluctuation that cannot be controlled by the salesman of the financial market;[28]

– the independent commercial agent must act in accordance with the principle of due diligence expected in a given situation in order to perform the independent commercial agency contract: this refers to the careful selection of the third party as well, the agent must examine the bonity of the client, however, he does not

24 BH 2005.63. [Court order]
25 On the historical roots of this principle see *Nótári 2011. 247; Nótári 2008. § 719.*
26 *Gombos* 2009. 27.
27 C-47/07; Masder Ltd. (UK) v the European Communities Committee.
28 *Papp* 2009. 45.

have to bear the liability for the creditability of the client (if the third party does not perform, the agent shall not be entitled to get profit);[29]

– in case of consort contracts (agreement with the purpose of taking part in the consumer group), to meet debt obligations are not impossible only because of the difficult financial situation of the consumer;[30]

– in connection with real factoring, debts shall be realised in the name and at the risk of the factor (if the factor cannot receive the debt from the debtor later on, he must take the risk), the invoice seller is not liable for the solvency of the debtor (in case of the unreal factoring, the factor does not bear the *del credere* risk).[31]

In case of concession contract, the economic/business risk may already be taken into consideration during the announcement of the tender (it can participate among the 'other, necessary information according to the tenderer'), however, if the tender does not mention about this, then, based on section (1) of § 19 of the Concession Act,[32] the rules of alteration of the contract according to the Civil Code shall be applied.[33]

There are some atypical contracts where the economic-financial changes that emerged after the conclusion of the contract may result in the termination of the contract:

– in case of timeshare contracts, if the property affected by the consumer's right to use is before or under construction and from the information of the company or by inspecting the property it becomes obvious that the property will be suitable to move in only with a significant delay that results in the loss of interest in part of the consumer or it will not be suitable to move in after 3 years after the conclusion of the contract, the consumer can rescind[34] (subjective right to rescind that sanctions the breach of the contract irrespectively of the reason);

– termination without successor due to the insolvency of any party may result in the termination of the license contract;[35]

– in case of a delayed incomplete or non paying of the leasing fee (even the financial-economic changes in the position of the lessee can result this), the lessor is entitled to terminate the contract immediately.[36]

The contract on business associations, due to the special nature of this legal relation, is an organisational (it creates a legal entity) and co-operational (it organises economy), *sui generis* agreement.[37] The general economic function of the

29 *Papp 2009.* 73.
30 FIT-H-PJ-2009-117. [Decision of the High Court of Appeal of Budapest]
31 BH 2005.72. [Court order]
32 Act XVI of 1991 about concession.
33 *Papp 2009.* 130.
34 *Papp 2009.* 91–92.
35 *Papp 2009.* 140.
36 *Papp 2009.* 165; 172.
37 *Farkas–Jenovai–Nótári–Papp* 2009. 52.

business association is realised by the contract, in other words, the organisation of the resources for a common goal.[38] The subjects of the contract form a special community of same interests (cooperation for the profit in a system of relations covered by a matrix of interests of many factors) that takes the risk for aiming the goal: liability for the result, for the risk of the jointly done management (liability for risk).[39] From the aspect of the contract of company law, the appearance and handling of the economic-financial crisis is a phenomenon that belongs to the operation of business associations. Besides, taking risk in an obviously not reasonable and unjustified way can lead to sanctions (e.g. the liability of the executive officer for the damage caused for the company): if the executive officer invests in buying or extracting diamonds in distant African countries hit by civil war in a way that cannot be controlled and by violating the rules of company law and also with a capital that originates from the so called 'pyramid scheme', from the money of more than twenty thousand retail investors, then it must be considered as a seriously unreasonable usage which is obviously opposite the interests of the company.[40]

III. European Overview in Respect of the Economic/ Business Risk

In connection with handling the imbalance arisen by the occurrence of some events that were unforeseeable at the time of the conclusion of the contract, the domestic rules of private law of the European countries and the codes (or the draft codes) aiming to integrate the European private law show us different pictures.

The French regulation[41] persists in the principle *pacta sunt servanda*, based on the belief that a judge cannot measure the effect of his judgments on the national economies, therefore, he is not entitled to alter the contract ('modifying the contract entails the risk of threatening the performance of the obligation committed by the other party in connection with another contract, hence, through an unstoppable and unforeseeable chain reaction it results in a general lack of imbalance […]').[42]

According to the Dutch, Italian and Serbian rules,[43] there is a difference between the ordinary contractual risk, arisen after making an agreement and originated from the character of the contract, and those changes of the circumstances that are irrespective of the nature of the agreement, as for the latter, the person under

38 *Kisfaludi* 2007. 42.
39 *Novotni* 1989. 65–73. *Kisfaludi* 2009. 119; *Farkas–Jenovai–Nótári–Papp* 2009. 38–39.
40 BDT 2004.959.II. [Casebook of the Courts]
41 BDT 2004.959. II. [Casebook of the Courts]
42 Code Civil Art. 1148, Art. 1134.
43 *Kadner-Graziano–Bóka* 2010. 435.

an unfair obligation in The Netherlands may ask the court for the modification or termination of the contract, while in Italy and Serbia the party for whom the completion of the contract is more burdensome, can only suggest the court terminate the contract.

In virtue of the Greek civil law regulation[44] and the draft of the common reference framework[45] (in this case only under conditions) – the same solution is implemented in the Rumanian civil law[46] –, the modification or termination of the contract because of extraordinary changes in the circumstances that affect the contract are allowed irrespectively to the relation of the risk factors to the contract.

The German Civil Code[47] provides the possibility of modifying a contract if – after its conclusion – an unforeseen change occurred according to which the contract would have not been concluded or it would have been concluded with different content and one of the parties cannot be expected to maintain this agreement in the same way. If the modification of the contract is not possible or it cannot be reasonably expected from the party, the one in a disadvantaged situation may rescind (or in case of permanent obligation he may cancel it).

In connection with the unforeseen events happening after the conclusion, English law introduced the legal terms 'frustration' and 'hardship'. In order to solve the economic-financial crisis, the following preferences have been defined: principally, the parties should create adequate provisions in their own contract (*'hardship clauses'*), in absence of these, there is a possibility to modify or terminate the contract by the court (*'intervene clause'*).[48]

The Civil Code of Gandolfi,[49] the Principles of European Contract Law[50] and the Principles of International Commercial Contract[51] urge the parties to negotiate again in connection with the contract in case of the occurrence of events that cannot be foreseen at the time of conclusion of the contract and that can cause contractual imbalance. If the parties cannot make an agreement in a reasonable time,[52] they can ask the court for alteration or termination.

According to the new Hungarian Civil Code,[53] which has not come into force yet and the Technical Proposal,[54] for the judicial modification of a contract, the above mentioned regulations require the possibility of any changes in the

44 § 388; *Kadner-Graziano–Bóka 2010.* 428.
45 Principles 2008. III/1. 110.
46 Codul civil Art. 1.271; *Veress* 2012. 110–113.
47 Bürgerliches Gesetzbuch § 313 Störung der Geschäftsgrundlage
48 *McKendrick* 1997. 255–256; 266–271; 282–284; *Kadner-Graziano–Bóka 2010.* 438–439.
49 European Contract Code 2001 (Academy of European Private Lawyers) Articles 97; 157.
50 Principles of European Contract Law 1995-2002 6. §111.
51 Principles of International Commercial Contract (UNIDROIT Convention, Rome, 2004) §§ 6.2.1; 6.2.2; 6.2.3.
52 3 or 6 months according to the Civil Code of Gandolfi.
53 Act CXX. of 2009. 5. § 168 (1)
54 5. § 175 (1)

circumstances not to be foreseen, this change in the circumstances is not due to the parties and it cannot belong to the ordinary business risks of the parties.[55] Analysing the last condition, there is a possibility to avoid considering the economic crisis and its effects as 'ordinary business risk', but it is necessary to change the current judicial practice.

Conclusion

We agree with Tibor Nochta[56] on the fact that the extra risks emerging after the conclusion of a contract need to be divided equitably and in our opinion, the Civil Code of Gandolfi, the Principles of the European Contract Law and the Principles of International Commercial Contracts provide the best instrument to realise it.

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55 Vékás 2008. 845. *The Proposal based on the requirements of the professional economic actors makes it clear that everybody should measure the business risks in connection with the conclusion of the contract on his own and there is no possibility to reduce it in a judicial way.*

56 *Nochta 2010.* 216.

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