

Consumer Rights in the Credit Contract

Richard Szabó

Institute for Organization and Management
Károly Keleti Faculty of Economics
Budapest Tech
Népszínház u. 8, H-1081 Budapest, Hungary
szabo.richard@kgk.bmf.hu

Introduction

In Hungary from World War II there is a permanent need for new flats and houses. During the 2nd World War high proportion of the flats and houses were destroyed. In the so called socialist era, there were huge building programs for blocks of flats. These flats were built in bigger cities by state subsidy and most of them were in the possession of the Hungarian state. Flats were distributed and sold by the state or municipalities(soviet). Rental fees were very low, they did not even cover the maintenance costs. There was also possibility for building or buying houses, mainly in the countryside and without subsidy. The impeachment of waste was on the shoulders of the state and municipalities, but they, in permanent lack of financial resources, could only concentrate on building as much new flats as possible.

As a part of the transition period after 1990, the state sold the flats at reduced prices for the tenants so as to get rid of the burdens. At the same time there is a considerable demand for good quality new flats. As far as the quantity of the flats and houses are concerned, it seems to fulfill the needs, but the inner structure is different from the real demand. The Hungarian state has almost entirely withdrawn from building, new flats are built on market basis. Because of the restricted purchasing power, a modern credit system has to bridge over the gap between the demand and purchasing power.

In developed countries it is much easier to obtain a flat, because because of the low required own contribution, the long term financing and the suitable amount of credit. In contrary to this, in Hungary the minimum own contribution required by banks, is minimum 50%, which seems to be the most important retaining factor of the expansion of credits for flats. That is why government offers state subsidy at different conditions for buying or building flats or houses. In previous years these conditions have almost continuously been altered according to the concepts of different governments. In the past six years the maximum of accessible subsidised credits was reduced from 30 million HUF(appr. 120.000 EUR) to its half. The

existing system makes difference between used and new buildings. While 6 years ago the maximum amount was at the disposal of the people, both for used and new flats. According to the existing rules, the reduced maximum (15 million HUF) amount can be drawn only for new flats. Those who want to buy a flat at a price less than 12 million HUF, may get a subsidised loan up to 5 million HUF. Above 5 million HUF one has to apply for loan with market interest rate. In Hungary the prices of newly built flats are over 300.000 HUF, while the net average monthly wages are not more than 85.000 HUF (appr. 340 EUR). At the above mentioned prices very good quality used flats are available. Unfortunately the existing system does not support the buying and renovating of used flats and houses. This short introduction seems to be necessary for foreigners to be able to get a comprehensive picture on the Hungarian situation.

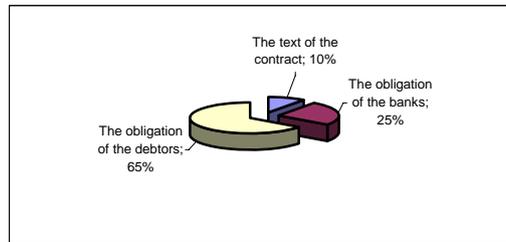
The system is complicated, the interests are different. By the help of our research we would like to examine the relationship between the two actors, the client, the consumer who applies for credit and the bank, who offers the credit. They exist in a kind of asymmetric interdependence, because there is a mutual dependence between the two parties, but in this relation banks have advantageous positions.

The Research

The research focused on the substance of the contract made between the two parties. In Hungary the financial services sector consists of banks, specialized credit institutions, mutual savings banks and credit unions. The total number of the banks and different kind of credit institutions is approximately 50. They all have the right to give loans for flats, but approx. two thirds of them do it in practice. In our research we overlooked the available general credit contracts used by Hungarian financial sector as standards. We were curious if there are possible individual alterations from the general conditions. We examined the proportion of obligations for the contracting parties beyond the mere facts concerning the credit.

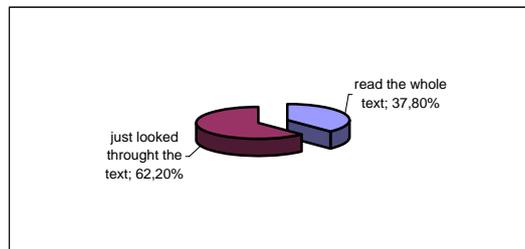
Outcomes of the Research

The general conditions of the contracts are worked out by systematic, long and prudential lawyer's work so as to minimize the banks' own risks. The documents are long, with complicated legal phraseology, not easy to understand for every day people. It is necessary to read them carefully from the beginning to the end, because all parts contain essential elements. As far as the division of different elements are concerned, approx. 10% of the texts of contracts cover the nomination of contracting parties, 20-30% the obligations of the banks, 60-70% the obligations of the debtors.



we asked the clients of six institutions. Out of them four are banks, two belong to credit unions. Out of 167 trials, we got 124 answers in the framework of personal interviews. We do not know, how many of them really got a loan. Although our questions were very simple and did not touch any personal element of their own contracts, we were surprised to see the distrustful behaviour of the potential debtors. Of course they did not know in advance, what kind of questions did we want to put them.

37,8% of the potential debtors read the whole text of the contract, the others just looked it through. They said 'it is no use complaining, we can not influence the general rules.' 6,14% had comments on the text, but they were also convinced that the bank will not take their opinion into consideration.



The Obligations of the Banks

Basically from the banks' side it is the only obligation to set the loan at the debtors disposal. In 98% of the cases the bank performs by remitting the sum of the loan to the debtors accounts. If cash is required, it has an extra fee.

The Obligations of the Debtors

The obligations of the debtors begin with submitting the claim for a loan. Banks require full supply of information including personal data. It is also a basic condition in banks' practice, that the debtor has to show the invoice of telephone.

Previously cable telephone was required. Potential debtors without cable telephone had to order this type of service. This type of practice was totally against the law. Today mobile phone is accepted, but prepaid ones are not accepted. Banks refer to international business experiences, according to which the best indicator for willingness of payment is the payment of telephone bills. Who goes out of money, starts with not paying the telephone bill.

Obligations during the Credit Process

During the crediting process some costs and fees occur. E.g. fee of the judgement of credit, estimation of the value of the flats, notary fees. The credit contract itself has to be signed by Public Notary. Out these costs for the estimation of value the potential debtor has to pay in every case, before granting the credit. Public Notary fees also occur before getting the loan, but at least in this phase the credit is sure. Judgement costs and other fees are deducted from the sum of the credit.

Obligations after Getting the Loan

The obligations of the clients become even more serious after getting the loan. A very complex system of financial security defends the bank, which is a burden on the client's shoulders.

The usual general elements of the security system are as follows:

Prompt incasso

Mortgage

Guarantee of the expert of value estimation

Insurance for the

Out of them prompt incasso is very rarely used for citizens.

Mortgage is used in every case, it is registered on

The guarantee of the expert of value estimation means that he has to buy the flat from the bank in case the debtor does not pay, at the value he estimated. But is a possible solution just at the final stage of collection process.

The insurance for the coverage of the credit means that a special insurance contract is made with a specialized insurance company for the sum of the loan and the costs have to be covered by the client.

Most of the bank, 86% of the ones we asked, lets prepayment by instalments. In these cases clients have to pay for the alteration of the contract. It is mostly 2% of the contract value, and it has a minimum amount.

For the question 'Which is the most painful burden for you?' 79% of the potential debtors said, that banks mislead them before and at making the contract by calculating in their interest rates only basic costs(mainly interest) and afterwards new types of costs 'come up from the cellar'.

As a reaction for the continuous complaints, Hungarian Financial Supervisory Authority, which is responsible for the protection of the consumer citizen's rights from government side, ordered the compulsory use of 'Total Credit Fee Ratio', which contains all costs and fees. It happens many times that very low interests rates are advertised, while the Total Credit Fee Ratio is by 5-50% higher. The difference comes basically from the so called 'Credit Handling Fee'.

The other main problem about which 84% of the clients complained the lack of information given by the banks' employees. Clients have to stubborn enough to put again and again awkward questions. After a time it is inconvenient but important to know all the details. Bank executives like to emphasize the 'sunny' side of the contract, just shortly mentioning the costs elements as if they were natural for anybody. They do not like to speak about Total Credit Fee Ratio.

Summary

All in all the position of the Hungarian Consumer Citizens become better on the financial markets in the past 15 years. Consumer Citizens become more self-conscious, and they can vote by their feet, because the number of banks increased. Competition seems to be fierce, but clients and also experts suspect that there has to be a close cooperation between different banks. Clients, consumer protection organizations, schools, universities etc. have a lot to do for reaching an acceptable balance between rights and obligations. Not only in case of financial institutions.

References

- 1995. évi XCVI. törvény A biztosítóintézetekről és a biztosítási tevékenységről.
- 1996. évi LVII. törvény A tisztességtelen piaci magatartás és a versenykorlátozás tilalmáról.
- 1996. évi CXII. törvény A hitelintézetekről és a pénzügyi vállalkozásokról.
- 1997. évi CLV. törvény A fogyasztóvédelemről.
- 1999. évi CXXIV. törvény A Pénzügyi Szervezetek Állami Felügyeletéről.
- 2001. évi CXX. törvény A tőkepiacról.
- www.fogyasztovedelem.hu
- www.pszaf.hu
- www.otpbank.hu
- www.im.hu
- www.meh.hu