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THE ISSUE OF INTEREST RATES ON FOREIGN CURRENCY LOANS. A CASE STUDY

Mariana Rodica ŢÎRLEA[1], Rodica PERCIUN[2]

[1]*Dimitrie Cantemir Christian University, Faculty of Economic Sciences, Cluj-Napoca , E-mail: rodica.tirlea@cantemircluj.ro*
[2] *INCE, Republic of Moldavia*

Abstract

The legal framework for establishing the interest for bank loans represents the bank lending contracts under which there are mentioned the contracting parties, the loan value, credit price, the rates term of payment of the contracted loan. The price of short-term bank loans and long term is represented by interest, taxes and bank fees. The amount of interest and bank charges is directly proportional to the risk of the relevant customer respectively the borrower, the size of the bank credit, the interest rates and the maturity term of bank credit. The calculation manner of interest, fees and bank charges needs to be clarified by the banking credit agreement. Practice has proven that through amendments to banking contracts or even unilaterally, the bank adjusts the interest or bank charges, fact which leads to unfair terms in contracts bank lending.

Key words:
Client, loan amount, interest rate, reference rate, daily interest rate

JEL Codes:
G21

I. The conjugation of the interest rate with an index. Case Study

On 01/01/2007 the loan agreement no. 000001/ 01.01.2007 ends, between X client (borrower) and Bank Y acting as mortgage lender. The object of the contract materializes into a loan amounted to 95.000 CHF (Swiss francs currency). The destination of the loan is for personal needs. In the credit agreement No. 000001/ 01.01.2007, Cap. 4, INTEREST AND FEES, are equipped that at the contract signing date, the interest rate is set at 6.3% per year. Until 01.01.2010, the bank has complied with contractual clause on the interest rate stipulated in the banking credit agreement. On 01.01.2010, the bank proceed to conclude a credit agreement Addendum, no. 000001/01.01.2007, mentioned above, in which it occurs a novelty consisted in the fact that during the art. 1 it is provided that as a manner of calculating the annual percentage rate shall be respected the following formula:

$$\text{Rd} = \text{CHF LIBOR 3 months} + \text{fixed margin} \qquad (1)$$

According to literature, the terms contained in the formula applied by the bank have the following meanings:

LIBOR (WWW.*stiri-economice.ro*). LIBOR Evolution din 16.09.2015), is the interest rate determined based on the interest offered by banks on the London financial market for term deposits of their customers.

CHF **(**www.efin.ro/glosar_*economic*, of 26.10.2015) represents Swiss franc, the official currency of Switzerland;

Fixed Margin **(**www.conso.ro/glosar, of 26.10.2015). represents the amount in percentage points, which is added to basic banking interest rate or to a monetary reference index to calculate the interest rate on a loan. The margin remains fixed throughout the contract, such as the interest rate changes only according to interest used as a basis for reporting (in the present case is CHF LIBOR interest).

The interest rate "can be presented in the following: a) fixed rate for the entire repayment period (the" Fra'= Future Rate Agreement) b) placing a ceiling for the length of credit use with a variable rate (system Cap). c) Interest can be changed unilaterally by the bank depending on certain factors. d) Interest shall be renegotiated in certain situations" (Turcu, 2009:198-201).

„In addition to variable rate and revisable, some bank contracts also introduce an interest concept of variation depending on market conditions. Such a clause allows the bank to discretionally modify the interest rate whenever it is desired. The reverse is a rare case of failure to comply with the clause of interest variation in relation to the market when the market interest rate is declining. A way to control interest rate change can be the conjugation with a domestic or international index with a margin (e.g. LIBOR + 5%). Like EURIBOR, LIBOR is the interest rate of the interbank market. LIBOR is practiced especially on the London interbank market. If there is a possibility of option between a fixed and a variable interest rate and the difference between them does not exceed two percentage points, it is preferable the fixed interest" (Turcu, 2009:198-201).

In our case, the initial repayment chart dated 01.01.2007, attached to the loan agreement no. 000001/01.01.2007, by enrolling Addendum, 1 there are mentioned the following:

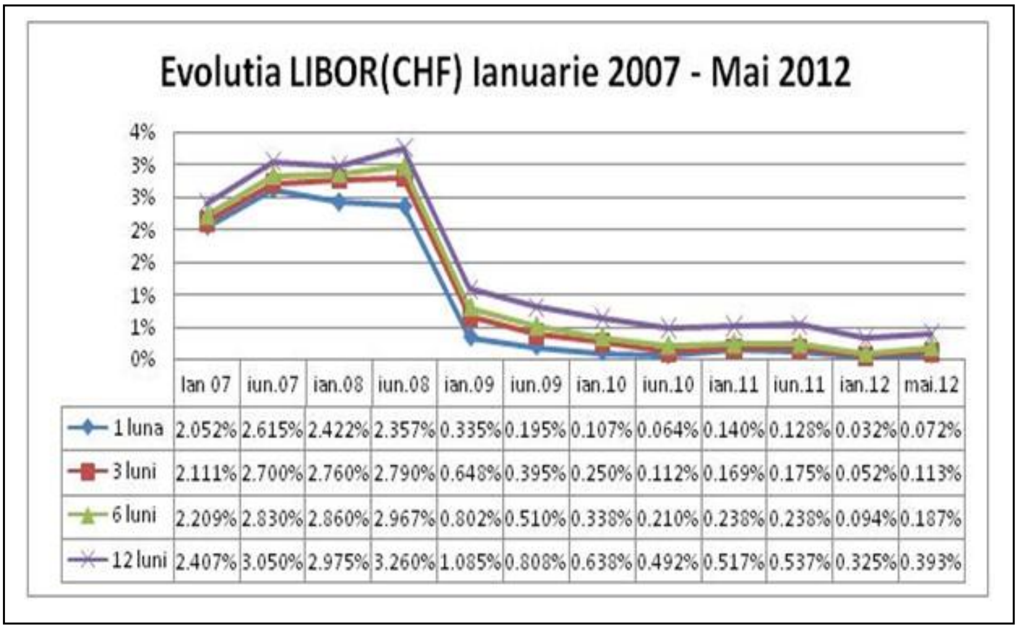
Fixed margin = 3%;
The percentage of interest contractually agreed = 6,3%;

In the period 2007-2012, CHF LIBOR index, recorded the following evolution:

During the credit contract no. 000001/01.01.2007 the evolution of CHF LIBOR index is shown in the graph in Annex. C.

Note that CHF LIBOR index had increased in January 2008 to 2.76% in June 2008 to 2.79% and then a strong downward trend, reaching in 2012 to 0.113% in June 2010, reaching 0.638%.

Graphic 1. LIBOR (CHF) evolution January 2007-May 2012



Regarding the interest rate of the loan agreement no. xxx:
Considering that the interest rate is LIBOR CHF for 3 months, this at the baseline of granting the loan was 2.7% and the bank margin was 3%, the first interest rate should be 5.7 % so that, even from the moment the credit was granted it was not taken into account by the bank, the formula for calculating the interest rate formula mentioned above. As shown above, in the first graph of reimbursement of 01.01.2007, it was calculated with an interest rate of 6.3%, not taking into account the developments of CHF LIBOR Index.

On 01.01.2008, is drawn up a new repayment schedule with a current interest rate of 6.75%, where FIXED MARGIN mentioned in the repayment schedule is 4%. If you calculate according to the formula for calculating the interest rate mentioned in the Addendum to the credit agreement (Index CHF LIBOR 3 months + fixed margin), on 01.01.2008, the interest rate should be 3% (FIXED MARGIN) + 2.79% (CHF 3-month LIBOR index) 5.79%.

Since January 2009, the interest rate should be decreased, according to the evolution shown in the graph in Annex. 1. As shown in the Addendum no. 1/01.01.2010 the loan agreement no. XXX/01.05.2007, art. 2 stipulates that the annual interest rate (Rd) be equal to CHF LIBOR 3 months + FIXED MARGIN.

In Annex No. 1 to Addendum No. 1, it is provided that the fixed margin should be 4% and the effective annual interest rate is 6.3%.

In the graph reimbursement prepared in 01.01.2010, are stipulated the following: fixed margin of 3% and 8.15% current interest.

We notice several changes to the loan agreement, changes that disadvantage the bank customer.

II. Conclusions

In the present case, there are several changes to the repayment schedule of the loan and the loan agreement mismatches disadvantage the bank's client. Analyzing the data, it results differences between the interest calculated by the bank and that determined on the basis of the calculation formula. After 15.06.2008, the evolution CHF was detrimental for the borrowed part, this difference in percentage increased. The differences in interest found were higher than fixed margin set by the repayment schedule of granting the loan.

These differences between the interest calculated by the accounting expertise by using the formula and that calculated by the bank can be explained by the fact that the index CHF LIBOR at 3 months, had an upward trend during the period 13.08.2007 to 15.12.2008, after which the trend was downward, in the period 12.15.2014 to 06.15.2015 and recorded a negative value. These mismatches were aimed at misleading the customer's bank, respectively the borrower. It was not respected by the bank the concept of fixed margin in the following papers emanated from the bank, i.e. repayment in graph 1, 2007, In the Repayment Schedule No.2 in year 2008. Repayment Schedule No. 3 of 2010; in the graph reimbursement no.4 of 2015.

Bank credit agreement is a contract of adhesion of the bank. Once it was signed, it is born a debt to the bank's client. The receivable consists of the loan amount, bank charges and interest on the bank loan (current interest, penalty interest, account maintenance fees, penalties for late fees). Extinction of the claim is completed only when all the elements that form the payment are being paid. The inability of payment of the loan entails forced execution. The client in the instant case reached the impossibility to repay the loan, together with the fact that he could not freely express his will, that has been put in this situation without prior notice and the changing of interest was converted into an abusive clause. (Popescu, 2013: 83-90).

We appreciate that the interest on bank loans renegotiation must be done according to certain factors, in full knowledge of both sides, transparent and not unilaterally by the bank. Changing the behaviour of the bank towards customers is vital "to ensure long-term success. The initiator of change, the change agent, subject to change, type of change, people affected by the change and the assessment of the change are the main factors to be taken into account if it is desired an effective management of an organization change process" (Bîncă *et al.,* 2011:81).

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