

ERROR OF CONTRACTUAL WILL AND SYSTEM OF GROUNDS FOR INVALIDITY

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Abstract: Articles 6:90–6:93 of Act V of 2013 on the Civil Code (hereinafter, referred to as CC) settle invalidity due to the mistake of will on the part of the parties. In my study, I would like to analyse these grounds of invalidity, highlighting the meaning of ‘error of will’. As part of this, I also make relevant delimitations, including the legal institution of pseudo-representation. My aim is not only to present certain grounds for invalidity, i.e. error, deception, secrecy, sham (simulated) contract, but to summarise the most important conclusions that can be drawn upon the case law. In doing so, the issue of proof and the applicable means of proof must be examined separately, as in the case of these grounds of invalidity the principle of will as an aspect of interpretation has fundamental significance. In the second half of my paper, during the analysis of the sham (simulated) contract, a brief overview of the foreclosure contract and the demarcation of the two legal issues are inevitable, taking into account the provisions of Art. 6:120 CC and the Civil Department Opinion no. PK 1/2011. (VI. 15.) of the Curia of Hungary on certain application issues of the margin agreement. In my work, in connection with the individual grounds for invalidity, I also deal separately with the special rules for gratuitous contracts (Art. 6:93 CC).

Keywords: *principle of will, declaration principle, mistake, sham contract*

1. STARTING POINT

Act V of 2013 on the Civil Code of Hungary in Art. 6:8(1)–(2) combines the principle of will and the principle of declaration in the interpretation of legal declarations. The significance of the rule is that the Art. 6:10 CC, this level of interpretation also applies in the case of non-contractual law declarations.

However, among the grounds for invalidity attributable to an error in the contract will, the CC emphasizes the principle of will, i.e. the invalidity of a contract can be traced back to some will. In this study, I analyse the individual grounds for invalidity based on contractual intent.

2. THE CONCEPT OF WILL ERROR

It should be noted first that Art. 6:58 CC requires consensus for the conclusion of the contract. That is, in the case of dissent, we can speak of a non-existent contract.

Thus, for example, if the reciprocity and unanimity of the will of the parties are lacking [Art. 6:63(1) CC] because one of the contracting parties has not made a legal declaration at all (for example, pseudo-representation Art. 6:14 CC), or the unanimous declarations of the parties do not cover all material issues or what they consider relevant [Art. 6:63(2) CC], no contract is concluded.

In the opinion of *Attila Menyhárd*, there is a will to do so:

‘A contract may be vitiated by an error of will if the contractual statement of at least one of the parties does not reflect a genuine contractual will, or if the declaration expresses a real contractual will, but that will arise in a situation in which the party was not the party to the contract. in the possession of all the information necessary to form his intention or in the formation of his intention, volunteering did not prevail.’ (Menyhárd, 2000, p. 9)

Errors of will can be divided into groups of deliberate will errors following the classification of the legal literature (sham contract, or outside the scope of invalidity: secret provisos or hidden motives) and unperceived will errors (mistake, deception, illegal threat which are not obvious to the aggrieved party). Errors of will can also be grouped according to their legal consequences: thus, a distinction can be made between voidability (e.g. deception, unlawful threat) and nullity (legal capacity, limited legal capacity, and sham contract) (Wellmann, 2021, p. 211).

3. OCCURRENCE OF WILL ERROR IN THE CIVIL CODE

The choice of the present subtitle was justified by the fact that although Articles 6:90–6:93 CC, the law collects the grounds for invalidity due to a mistake of will, apart from these provisions, there is also an error of will in the law. The CC regulates the invalidity of certain juridical acts due to defects of will in several places:

- the legal transactions of an adult person (i.e. of legal age) who has no legal capacity to act [Art. 2:9(1) CC];
- the juridical acts of an adult person placed under guardianship and having partially limited capacity to act [Art. 2:20(1) CC];
- has limited capacity to act due to minority [Art. 2:12(1) CC];
- incapable of acting due to a minority [Art. 2:14(1) CC];
- the legal transactions of an adult person placed under guardianship with full restriction of legal capacity [Art. 2:22. § (1)] (Vékás, 2020b, p. 1585).

In my opinion, regarding an error of will, an independent reason for a challenge is the Art. 4:111(2) CC, according to which, if the presumed father made the fully enforceable acknowledgement of paternity in error, or under misrepresentation or duress, he may bring an action for challenging the presumption within one year from the date on which he detected such error or misrepresentation, or from the date of cessation of duress.

For the cases of invalidity relating to the legal transaction of an adult who is partially limited in his or her capacity to act (Art. 2:24 CC) and the juridical acts of the minor (Art. 2:17 CC), the Civil Code does not regulate challengeability but

relative nullity, i.e. a fault in the will can only be invoked in the interests of weaker parties.

Apart from the disguised stipulations and sham contracts, in case of invalidity attributable to a fault of will, it is not possible to challenge the contract, but only the legal transaction. In contrast, in the case of invalidity due to an error in the intended effect, the question is – in all cases – the validity or invalidity of the contract ‘as a whole’.

In my opinion, the discrepancy can be traced back to the fact that in the event of a will, only the validity of the legal declaration made by the given party is always called into question since the contract is a mutual and unanimous legal declaration of the parties (Art. 6:58 CC). The Civil Code is in line with this grammatical formulation: while the Art. 6:90(1) CC regulates the challenge of the contract law declaration, the Art. 6:90(2) CC already states that if the parties were in the same erroneous assumption on a material issue at the time of concluding the contract, any of them may challenge the contract. At that time, the use of the term ‘contract’ was already justified, because the ground for challenge relates to the contract, as the parties were in the same erroneous assumption. The Civil Code is based on the same argument. Under the Art. 6:90(3) CC, the contract may not be challenged by anyone who may have recognized the mistake or assumed the risk of the mistake. The legislator of the Civil Code excludes not only the contestation of the contractual declaration of rights but also the contestation of the entire contract.

Exceptions to this argument are secret provisos and hidden motives respectively sham contracts. Within the scope of a sham contract, the exception is simple: we can speak of a sham contract in the case of a bilateral error of will, i.e. precisely because of the bilateral nature of the error of will, only the nullity of the given contract (and not the contract statement) can be interpreted here. In the context of the contractual intention deliberately concealed, I refer to the case law, according to which disguised stipulations and concealed motives are immaterial concerning the validity of the contract (Curia decision No. BH 2001.384).

4. THE MANIFESTATION OF CONTRACTUAL INTENTION ERRORS

4.1. Mistake

Under the case law, a contract may be challenged on the ground of error if the party was mistaken regarding any substantial circumstances. What is relevant is a circumstance that, according to the public perception, fundamentally affects the contractual will of the parties, in respect of which the party would not have concluded the given contract with the correct content (Curia decision No. BH 2016.114.). It should be noted that Art. 6:90. CC was adopted with the same content within the scope of error.

Concerning this ground of appeal, the question to be decided is what constitutes an essential circumstance that may justify an appeal on the ground of error. By the legislature’s objective:

‘[a]s the conclusion of the contract requires the agreement of the parties on the substantial issues, it is justified that it can also be substantial only in the event of an error in which the party would not have concluded the contract with the given content’.¹

The significance of this reasoning is that the conclusion of the contract requires the agreement of the parties on the issues that are essential and considered essential by either of them [Art. 6:63(2) CC]. In other words, the conclusion of the contract occurs because one of the parties was at fault in one of the essential circumstances of the contract, and that error was the result of the other party’s conduct. The other party’s behaviour may be active (the mistake was caused by the other party) or passive (the mistake may have been recognized by the other). This distinction between an invalid contract and a non-existent contract is based on the differentiation among the types of error.

Under the case law, the relevant factor for the contract of sale of a car is whether the actual condition of the car corresponds to the data/information in the service book (Curia decision No. BH 2010.245). Furthermore, the highest judicial forum of Hungary stated:

‘[t]he insurer misleads the party – regarding the substantial circumstances – who is concluding a life insurance contract with the insurer by promising that the party will be entitled to take out a preferential home loan after a certain period if this loan scheme does not exist at the time of conclusion with the conditions communicated’ (Curia decision No. EBH 2006.1402).

The judgment concludes that ‘a contract for the sale of a racing horse may be challenged if the seller fails to inform the buyer regarding the disease of the horse, which renders the horse to be unfit for racing’ (Szeged Regional Court of Appeal decision No. BDT 2019.4099).

The case law has also established the principle that, for the purposes of a contract for selling a shareholding in a non-profit public undertaking employing a disabled person, the non-profit company continues to receive the wage subsidies which it can carry on. In the event of termination of the wage subsidy, the buyer of the business unit may challenge the contract by mistake (Szeged Regional Court of Appeal decision No. BDT 2015.3412. I.).

Following the above-mentioned case-by-case analysis, it should be noted that an error in the subject matter, person, or content may be substantial. Most often, however, an error in the quality and extent of the service is the relevant basis for the challenge. At the same time, the public perception must be taken into account, i.e., what the public perception considers (would consider) to be an important issue concerning the given contract (Benedek, 1992, p. 531).

¹ Bill on the Civil Code of Hungary No. T/7971, 2012, p. 574.

There is also an important limitation regarding an error, according to which, a person who may have recognized the error or assumed the risk of the error may not challenge the contract [Art. 6:90(3) CC]. Referring to the legislature's objective:

'The case law on error has so far examined whether or not the party alleging the error could have recognized the error with due diligence. This aspect, as a legal condition for error, is set out in the Proposal as an itemized provision and excludes the right to challenge an error even if the party to the error has assumed the risk of error (for example, if the contract contains a chance element, i.e., aleatory contract).'²

This provision is set out in Art. 1:4 among the principles. Under this Art. 1:4(2), a person who may have recognized the error but entered the contract, would – by challenging it later – rely on his attributable conduct to obtain an advantage (Vékás, 2016, p. 122).

Therefore, the contract of sale cannot be challenged on the grounds of error and the rights arising from the defective performance cannot be exercised, if the buyers became aware of the existing defects of the property to be purchased, before concluding the contract (Curia decision No. BH 2011.221). And the phrase 'risk of error' can be relevant for contracts that are dependent on chance (aleatory contract).

4.2. Misrepresentation, unlawful threat

Concerning misrepresentation(deception), it is primary to distinguish it from error. According to the Ministry Explanatory Notes on the 1959 Civil Code³, *'the cause of an error is not the same as that of deception: an error may be caused in good faith or through negligence, without the intention of the party causing the error being to circumvent the other party'*. This also means that deception is a special, more serious case of causing an error, which requires wilful and deliberate conduct expressed or implied by the party.

It is relevant that misrepresentation may take the form of both active and passive conduct, but in each case, it must relate to a circumstance relevant to the contract. The difference with the error is that the possible negligence of the deceived person is not relevant, so the deceptive party cannot claim that the other party could have recognized the deceptive conduct with due diligence (Wellmann, 2021, p. 214).

At the same time, a decision containing an opposite opinion is also known, according to which, the contract of sale has not been challenged on the grounds of error, and the rights arising from the defective performance cannot be exercised if the buyers became aware of the defects of the property to be purchased before concluding the contract (Curia decision No. BH 2011.221).

In judicial practice, the most common question regarding misrepresentation is that if the deceptive conduct constitutes a criminal offence (typically fraud), it is a

² Bill on the Civil Code of Hungary No. T/7971, 2012, p. 574.

³ Act IV of 1959 on the Civil Code of the Republic of Hungary.

prohibited contract (and thus void), or a contract that can be challenged due to invalidity based on misrepresentation. Following the case law, a deceptive and fraudulent legal transaction that also constitutes a criminal offence does not automatically render the legal transaction null and void. The contract thus concluded can be challenged only by those who were in error or who have been deceived (Curia decision No. BH 1996.200). In its content, the criminal offence of ‘fraud’, in relation to a contract, refers to misrepresentation or deception, which is not a ground for nullity but a ground for avoidance (Curia decision No. BH 1996.253).

This important principle is stipulated from time to time in the judgments of the judicial fora. Accordingly, the buyer of the real estate property, who makes a purchase statement at the time of concluding the contract with the knowledge and intent not to pay the purchase price, committed fraud under the scope of criminal law, however, from the viewpoint of civil law, his actions resulted in the fact that the sale contract is to be challenged on the ground of misrepresentation. In such a case, a final judgment establishing criminal offence is not required to establish the facts relevant to the civil law legal consequences (Szeged Regional Court of Appeal decision No. BDT 2008.1903, Part I.)

It should be emphasized, that if one of the parties has misled the other party in concluding the contract, this fact alone does not mean that the contract is also contrary to good morals. To establish that the contract is immoral, it is necessary to establish the additional circumstances in addition to the deception (Budapest-Capital Regional Court decision No. BDT 2009.2168).

Misleading conduct may be committed not only by the contracting party but also by a third party, as Article 6:91(1) and (2) CC shall apply even if the misrepresentation or unlawful threat was committed by a third party and the other party knew or ought to have known of it.

In the case of an unlawful threat, a characteristic circumstance is that the party is persuaded to conclude the contract with the prospect of some disadvantage. This also means that there is a causal link between the unlawful threat and the contractual intent of the party, thus the conduct which constitutes an unlawful threat must be specifically expressed for the contract to be concluded. It should be highlighted that the illegal threat may be directed not only to the contracting party but also to a third party having a legal relationship with the contracting party, the decisive factor being that the unlawful threat (regardless of its direct addressee) should lead to the conclusion of the contract.

The legal literature emphasizes that the disadvantage affected by a characteristic threat can be both material and moral. For example, entering into a contract for reporting an infringement as an illegal threat. That is, if the party does not sign the contract, a complaint will be filed with the competent authority about the actual violation. It is important, that the threat of a lawful act is the basis of the 6:91(2) CC provided that it is abusive (Wellmann, 2020, p. 214).

The case law includes, for example, if the lessor forces the lessee to amend the contract to the detriment of the latter by failing to hold an event organized by the

lessee in the lessee's business as part of the lessee's business (Budapest-Capital Regional Court decision No. BDT 2012.2651).

4.3. Secret provisos, sham contract

Concealed motive is also a question of contractual intent, however, to which private law does not attach legal relevancy. Thus, it is also hammered out in the case law that a secret proviso does not affect the validity of the contract (e.g., Curia decision No. BH 2014.177; Curia decision No. BDT 2001.390). The intentional lack of will does not be governed by the rules for challenging the contract, but for contracts concluded with secret provisos or concealed reasons and for sham contracts (Curia decision No. BH 2001.234. point II).

Within the scope of a sham contract, a bilateral and deliberate error of will can be established (which is why the law does not provide for the nullity of the contract statement, but of the contract). A contract is fictitious if the contracting parties, by common will and agreement, make a legal declaration that does not correspond to their real will, giving a false appearance to a third party (Vékás, 2020b, p. 1591). However, the contract of sale does not imply that the parties enter into it for a specific purpose (e.g. to obtain a soft loan) if at least one of them has a real intention to acquire property (Curia decision No. BH 2013.339).

Similarly, a contract for the transfer of property in which the parties had a real and common intention to transfer the property was not a pretended motive for concluding the contract, therefore, it is not deemed as a sham contract. However, their common aim to be achieved with this contract was to deprive a third party from the basis of satisfying his claim, entirely or in part. That means that an action for challenging the contract based on invalidity due to the fact of this fraudulent purpose must be dismissed (Curia decision No. BH 2013.299). That is, the sham contract and the fraudulent contract differ in both factual and legal consequences. The supreme court of Hungary summarized the difference between the two rules as follows:

‘Contract aimed at concealing assets to the detriment of a creditor is a valid contract, its relative ineffectiveness towards the third party, the creditor, can be established only if the contract was not fictitious with regard to the intention to transfer the debtor's assets, so the other party actually acquired it, which was the basis for the satisfaction of the creditor's claim. The situation is different if, to prevent the recovery of the claim, the debtor wishes to give the impression that the given assets in his property are not owned by him anymore but by a third party. Such a contract is a sham contract due to the lack of a contractual intention aiming to transfer property, therefore, this contract shall be deemed null and void. Without a real transfer of property under such a contract, this asset serves as a basis for the satisfaction of the creditor's claim’ (Curia decision No. BH 2001.62).

The relationship between the sham contract and the contract aimed at concealing assets is also explained in Civil Department Opinion no. PK 1/2011. (VI. 15.) in detail, especially point 10 and its justification.⁴

Under Art. 6:92(2) CC, sham contracts shall be null and void; if a sham contract disguises another contract then the parties' rights and obligations shall be assessed based on the disguised contract. The court stipulates that, if there is another contract that is concealed, there is no place to apply the legal consequences of invalidity. Nevertheless, if the concealed contract is also invalid, the consequences of invalidity take place within the framework of the latter contract (Curia decision No. BH 2010.148).

Accordingly, the court also considered a contract as invalid which was aimed at the division of joint property of spouses where the spouse wanted to transfer a half proportion of his ownership registered as a whole to his spouse to avoid the possible consequences of criminal proceedings initiated against him (Curia decision No. BH 2012.195).

4.4. The relevancy of the legal declaration of the false representative

In the era when the 1959 Civil Code was in effect, it was controversial how the legal declaration made by the pseudo-representative (acting without powers of representation) should be dealt with. It is also known that due to the missing contractual intention of the contracting party, the invalidity of the given legal transaction could be established. According to another approach, the contract is non-existent, with the interpretation that the contract concluded by the pseudo-representative was not concluded at all, since there is no contractual declaration on the part of one of the parties, i.e. there is no consensus between the parties (Curia decision No. EBH 2004.1146). This interpretation is based on the opinion that the pseudo-representative has not made a juridical act on behalf of the party to the contract, so, his act cannot be regarded as an act made by the party (Kisfaludi, 2021, p. 60).

The Art. 6:14(1) CC also states this principle, i.e. if a person makes a legal declaration without the right of representation or exceeding his or her powers of representation, his statement shall produce legal effects subject to the approval of the party being represented.

It may be disputed whether the third party is required to await clarification of the right of representation with a statement, i.e. whether or not the represented person approves the statement of the pseudo-representative. According to the interpretation of the supreme judicial forum, if a pseudo-representative unilaterally terminates the contract, meanwhile it is obvious that he or she has no powers to represent the contracting party, this notice does not result in any legal effect. That means, this situation cannot be deemed as a pending legal situation until the 'represented' person has approved the juridical act, it does not trigger the analogous application of the

⁴ Pursuant to Point 1 of the uniformity decision of Curia No. 1/2014. PJE, this PK opinion shall be deemed to be relevant to the application of the new Civil Code of Hungary.

legal consequences of a pending condition of a contract, nor does it create an obligation for the presented party to make a declaration (Curia decision No. EBH 2009.2038; see also Vékás, 2020a, p. 1465).

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