

## CHANGES TO MORTGAGE REGULATIONS

On May 15, *Ley 1/2013 de 14 de mayo de medidas para reforzar la protección a los deudores hipotecarios, reestructuración de deuda y alquiler social* (Measures to reinforce the protection of mortgage debtors, debt restructuring and social rent) came into force. The following is a summary of the sections that affect securitisation and *cédulas hipotecarias*.

- Changes to the Mortgage Market Act:
  - New +30-year loans to finance primary residences are no longer eligible for the issue limit of *cédulas hipotecarias*. Loans granted prior to the Act coming into force will still be eligible as well as those issued from such date once their term to maturity falls under 30 years. What happens to *participaciones hipotecarias* (mortgage shares) and *bonos hipotecarios* (mortgage bonds)? It is possible that as the Act's ninth *disposición transitoria* (transitory regulation) only mentions *cédulas*, mortgage loans financing primary residences with a term in excess of 30 years will no longer be able to back *bonos hipotecarios* (mortgage bonds) or *participaciones hipotecarias* (mortgage shares) (although they may be transferred through *certificados de transmisión de hipoteca* (mortgage transfer certificates)).
  - From now on, the bank will not be entitled to ask for additional guarantees or an amortisation on the loan in case the value of the guarantee falls more than 20% of the appraisal value at origination.
  - The legal framework of appraisal companies is modified, reducing their dependence from credit entities, regulating specific situations of potential conflict of interest and other matters.
- Changes affecting mortgage loans and some issues related to the manner in which they are originated:
  - Penalty interest limitation for mortgage loans financing primary residences: 3 times the *interés legal del dinero* (official public interest rate).
  - The deed of a loan must state if the mortgaged property is the primary residence. If so, upon foreclosure it will be understood, except when proof of the contrary, that the property is the primary residence. This will significantly simplify pool audit when originating *Fondos de Titulización* (Securitisation Funds) as it will only be necessary to verify that this agreement is included in the deed.
  - All mortgage loans issued after the coming into force of this Act will expressly state in their deeds of incorporation that the arrears of 3 monthly

quotas (or equivalent) may allow the creditor to set in motion the summary foreclosure procedure.

- Changes to the mortgage foreclosure procedure (mainly, changes to *Ley de Enjuiciamiento Civil*) and evictions.
  - o Changes to the out-of-court procedure have been made. We do not expect great changes as delays are not originated by the mortgage foreclosure procedure but by the process of eviction.
  - o The debtor may invoke the existence of abusive clauses under consumer protection regulations to stop the foreclosure. Several regulations have been modified to introduce new procedures to delay foreclosure proceedings. The Act introduces a new cause to oppose the foreclosure: the existence of abusive clauses under consumer protection regulations in the loan, in accordance with the consumer protection regulation. From 15 June 2013 and following the 10-day term lapsed from the foreclosure approval by the Judge, this cause will no longer be applicable.
  - o Allocation of amounts of appropriation and debt clearance.
    - The order of the allocation of the amounts to be collected has changed, regardless of whether the loan finances a primary residence or not: interest accrued by the loan, principal, arrears interest and legal costs. In the event that the loan finances the purchase of a primary residence, if we combine this rule with the one that limits the penalty interest, once the principal has been paid there will be no more interest accrued from the debt, which will be fixed from then on without penalty regardless of when it is paid.
    - Bidless auction.
      - If the property is not the primary residence, the creditor may request the appropriation of the foreclosed property at 50% of the starting auction price or the total amount owed.
      - If the property is the primary residence: the creditor may request the appropriation at 70% of the starting auction price of the property, and if the amount owed is less, at 60%. In fact, this means the valuation of properties at a minimum of 60% of the starting auction price and, depending on the number agreed upon the loan origination, it could mean that in order to materialise the appropriation of the property the creditor may have to pay. This is surprising if we consider the possibility of an auction that was initiated and in which no bidders were found...

- Primary residence: release from the unpaid debt upon auction: the debtor may be released from the remaining debt if 65% of such debt is paid in the next 5 years or 80% in the next 10 years. These amounts will be increased in accordance with the *interés legal del dinero* (official public interest rate).
- Primary residence. Gains from the sale of the properties appropriated by the creditor in the auction, regardless if a *cesión de remate* (transfer of the appropriation rights derived from the auction) has taken place, within the following 10 years: the remaining debt will be reduced in 50% of the gains, minus all justified expenses. Although it seems like the Act includes a material error, our interpretation is that in the event of gains that fully cover the debt (or the amounts from which the debtor may be released within the 5 and 10 years following the allocation), the remaining amount will be returned to the debtor.
- Rules related to evictions that affect the effective new ownership of properties and the requirement necessary to recover a default through its sale.
  - Evictions are suspended for 2 years (until 15 May 2015) if the primary residence has been appropriated by the mortgage creditor or a third party acting on its behalf:
    - If the debtor is in a personal situation of economic and social vulnerability (included in Art.1.2. of the Act).
    - Family unit income does not exceed 3 to 5 times IPREM (public index of individual income).
    - If in the past 4 years the family unit has experienced a significant alteration to its financial situation in terms of access to housing. We're unaware of the existence of others, but the mortgage effort of the family unit being multiplied by 1.5 is considered a significant alteration.
    - That the quota is higher than 50% of the net income of the family unit.
    - That the foreclosed loan was issued to purchase the only property owned by the debtor.
  - It looks like this moratorium will not be automatic but must be requested by the debtor with the corresponding accrediting documents.
  - *Fondos de Titulización* (Securitisation Funds) in possession of the properties auctioned are subject to this moratorium if they are considered to be creditors; technically they are not (they share the loans through a sort of mortgage share), but it looks like this is the

real intention of a rule that, again, has not considered in its wording the great number of mortgage loans that are currently securitised.

- In accordance with the Act's first *disposición transitoria* (transitory regulation), these rules will be applied to all the procedures that have not yet initiated the eviction, even if the foreclosure was launched prior to the coming into force of the Act.
- *Código de Buenas Prácticas* (Code of Good Practices) for the restructuring of primary residence debt with mortgage guarantee: *Ley 1/2013* consolidates the measures enacted by *Real Decreto ley 6/2012 de 9 de marzo*. Thus, debtors on the so called "exclusion threshold" will enjoy qualified protection if the affected credit entity (or any entity that professionally issues loans or mortgage loans) supports it voluntarily. These rules will be compulsory for participating entities and will imply a series of material obligations to the debtors and formal obligations to the public administration: thus, the entity will apply the rules of renegotiation, restructuring, debt condonation and, ultimately, release from the debt via in-lieu-of-payment of the property as contemplated in the Code of Good Practices. Finally, *Ley 1/2013* introduces Art.15 to *Real Decreto Ley 6/2012* by which said obligations will be considered subject to *Ley 26/1988 de 29 de julio, sobre Disciplina e Intervención de las Entidades de Crédito*, with the corresponding associated penalties in case of violations.

Some circles defend the compulsory application of the rules included in the Code of Good Practices to *Fondos de Titulización* (Securitized Funds) whose assets are serviced by Credit Entities that have joined the Code. In our opinion, this interpretation is inadmissible from a contractual and private relations point of view but also from the point of view of the public administration:

- *Fondos de Titulización* (Securitized Funds) are not credit entities and neither do they issue loans professionally, therefore they are not the recipients of the rule.
- The banks servicing the loans transferred to *Fondos de Titulización* (Securitized Funds) are mere managers, with limited decision making capacities in relation to issues that have an impact on the value of the credit rights held by such *Fondos*. We must not forget that both novations forced by the Code and debt in-lieu-of-payments have an impact on the affected *Fondo*, and the Mortgage Market Act itself requires the consent of the *Fondo* as holder of the mortgage share (and, by extension, of the mortgage transfer certificate) for any type of waiver, transaction or guaranteed debt cancellation.
- We don't believe the legislator really had this in mind:
  - On the one hand, Art.5.7 specifically states that the content of the Code of Good Practices will only be applied if the following two

elements concur: subjects (supporting credit entities on the one hand and debtors on the other), and object (mortgage loan agreements): *Fondos de Titulización* (Securitised Funds) are not credit entities and their relation with the mortgage loan agreement is indirect, through a mortgage share or mortgage transfer certificate.

- On the other, *Fondos de Titulización* (Securitised Funds) are not (and by nature cannot be) subject to the prevailing legislation of *Ley 26/88*.

In any event, an expressly exclusion within the Act itself would have been desirable in order to avoid too many distortions.