

## ANALYSING THE LONG-AWAITED SPANISH MORTGAGE CREDIT LAW

This Legal Briefing analyses the changes introduced by the long-awaited Mortgage Credit Law (the “Mortgage Credit Law”), finally published in the Spanish Official Gazette on 15 March 2019. The Mortgage Credit Law will come into force three months after its publication (i.e. on 16 June 2019).

### I. Preliminary issues

The maximum period granted by the European Commission to implement the European legislation on mortgages in national law expired almost three months ago. Previous versions of the Mortgage Credit Law have been the subject of intense parliamentary debate for more than a year due to its importance and the profound effect that this law will have on current mortgage-backed facilities. Finally, on 15 March 2019, the last version of the Mortgage Credit Law was published.

The Mortgage Credit Law implements Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 in Spain. The purpose of this Directive is to enhance legal certainty, transparency and understanding in relation to certain financing agreements granted to consumers who are not acting in the course of their professional or business activity.

However, the Mortgage Credit Law has gone further, extending its scope of application to all natural persons regardless of whether they are considered consumers or not. Therefore, the Mortgage Credit Law also applies to other groups, such as self-employed workers.

The main changes introduced by the Mortgage Credit Law affect the following elements of the mortgaged-backed facilities this Law applies to: (i) early repayment and the corresponding fees; (ii) prohibition of minimum interest rate clauses (*cláusula suelo*); (iii) multicurrency mortgages; (iv) related sales; (v) default interest; (vi) appraisal value; (vii) distribution of mortgage expenses; and (viii) legal framework of the lenders, among other elements.

Some of these changes also amend the Decree of 8 February 1946 which approved the Mortgage Law (the “Mortgage Law”).

This Legal Briefing summarises the abovementioned changes introduced by the Mortgage Credit Law, divided into two categories: (i) those introduced by the Mortgage Credit Law that will only affect agreements that fall under its scope of application; and (ii) those that fall under the scope of application of the Mortgage Credit Law and which also amend the Mortgage Law.

## **II. Scope of application of the Mortgage Credit Law**

The Mortgage Credit Law applies to facility agreements (both loans and credits) granted by a natural or legal person that lends money in the course of its business (or in carrying out their profession), when the borrower or the guarantor is an individual).

In light of this, the activities that fall within the scope of application of the Mortgage Credit Law are:

- a. The granting of credit agreements which are secured either by a mortgage or by another comparable security on residential real estate property (including storage rooms, garages or other property that serves a domestic purpose).
- b. The granting of credit agreements whose purpose is to acquire or retain rights of ownership in relation to land or an existing or planned building.
- c. Intermediation in relation to entering into of one of the types of agreement referred to in paragraphs (i) or (ii) above.

## **III. Main changes introduced by the Mortgage Credit Law**

The main changes introduced by the Mortgage Credit Law that affect all financings granted under the scope of application mentioned above are:

### *(i) Transparency measures*

The transparency measures introduced by the Mortgage Credit Law are aimed at enhancing the protection and security of the borrower at all stages of the financing process, from when it is granted (including the pre-contractual phase) up to its enforcement.

In this sense, the Mortgage Credit Law requires that clear and comprehensive general information about credit agreements is made available to the borrower. Therefore, creditors must provide their clients with the European Standardised Information Sheet (ESIS) and the Advisory Information Sheet (AIS), which will ensure that the borrower is in possession of all the information they need to fully understand the terms of the financing.

Moreover, and without prejudice to the creditor's reporting obligations, the Mortgage Credit Law assigns the notary the duty of providing the borrower with impartial advice, clarifying any doubts that may arise in the process. The notary is obliged to check that the principle of material transparency is observed in all clauses and provisions of the financing agreement to be signed when the financing is granted.

The transparency measures introduced by the Mortgage Credit Law will not apply any part of the mortgage portfolio which has already been granted, except if these loans are subject to novation or subrogation after the Mortgage Credit Law enters into force (although we anticipate that the interpretation of the Mortgage Credit Law in this regard may be controversial).

Lastly, the principal changes introduced by the Mortgage Credit Law which aim to ensure transparency and protect the consumer include the following:

- a. the prohibition of related sales, i.e. selling packages comprised of the loan and other products, if the loan is not also offered to the borrower separately. The purpose of this prohibition is to encourage competition between creditors and ensure that related sales can only take place when they are in the best interests of the consumer;
- b. the right of consumers with multi-currency loans to convert a foreign currency loan into the currency in which the consumers primarily receives their income, or the currency of the Member State in which the consumer is resident; and
- c. the obligation to register any contractual clauses of mortgaged-backed loans which relate to general contracting conditions with the Registry of General Contracting Conditions. These clauses or conditions will also have to be available on the creditor's webpage (if applicable).

*(ii) Distribution of mortgage expenses*

The Mortgage Credit Law also changes the way the expenses which arise from notarising the mortgage-backed credits/loans and registering them with the Land Registry are distributed between the creditor and the borrower, and relieves the consumer of a good portion of said expenses. In this sense, these expenses shall be distributed as follows:

- a. Expenses to be borne by the creditor:
  - Agency expenses
  - The cost of the notary fees for the corresponding deed
  - The cost of registering the Mortgage with the corresponding Land Registry
  - Stamp duty
- b. Expenses to be borne by the borrower:
  - Property appraisal expenses
  - The cost of the copy of the public deed if requested by the borrower

*(iii) Early repayment*

The Mortgage Credit Law grants the borrower the power to repay part or all of the facility before the end of the agreed term of the mortgage-backed loan/credit. The only requirement is to give the creditor notice of this intention one month in advance at most.

The borrower is entitled to a reduction of the total amount of the loan/credit, which will include the interests and costs corresponding to the remainder of the loan period.

Moreover, the circumstances in which the creditor may charge the corresponding early repayment fee are limited to the following:

a. Loans or credit at variable interest rates.

In these cases, the parties may agree on an early repayment fee in one of the following two mutually exclusive instances of early repayment: (i) a 0.15% early repayment fee to be applied to the repaid amount in the event the early repayment takes place during the first five years of the loan; or (ii) a 0.25% early repayment fee to be applied to the repaid amount in the event the early repayment takes place during the first three years of the loan.

b. Loans or credit at fixed interest rates.

In these cases, the parties may agree on a 2% early repayment fee to be applied to the repaid amount in the event the early repayment takes place during the first ten years of the loan; or a 1.5% early repayment fee in the event the early repayment takes place after this point.

*(iv) Legal framework for creditors, credit intermediaries or appointed representatives*

The Mortgage Credit Law will oblige creditors and credit intermediaries (excluding credit institutions, financial institutions and their branches) to be registered with the corresponding registry as indicated by law. The Bank of Spain will manage the registration.

The second Transitory Provision of the Mortgage Credit Law grants existing creditors, credit intermediaries and appointed representatives a six-month period to apply to be recognised as such. Before receiving this recognition, their compliance with the requirements needed for their registration must be evaluated.

*(v) Prohibition of minimum interest rate clauses*

The Mortgage Credit Law will definitively prohibit the application of a minimum interest rate clause (*cláusula suelo*) on variable interest rate facilities. The default minimum rate will be 0%.

#### **IV. Main changes introduced by the Mortgage Credit Law (that affect the Mortgage Law)**

The Mortgage Credit Law includes a series of changes that go beyond its scope of application and that also expressly amend various provisions of the Mortgage Law, which applies to any mortgage-backed loans or credit.

The changes discussed below will affect any loan or credit, regardless of whether the borrower is a consumer, self-employed or an individual. Therefore, these changes will also apply to financings granted between legal entities which are secured by a mortgage, even if the property is not used for residential purposes.

*(i) Default interest*

The Mortgage Credit Law amends the default interest rate in cases where the loan or credit is granted to a natural person and secured by a mortgage on residential immovable property. In this sense, the default interest rate will be set at the ordinary interest rate plus three percentage points.

Moreover, the Mortgage Credit Law prohibits the capitalisation of default interest.

*(ii) Appraisal value*

In the event of extrajudicial enforcement, the current Mortgage Law permits the rate at the auction of the mortgaged property to be at least 75% of the value established in the appraisal report that may have been drafted for the property.

The Mortgage Credit Law takes a tougher stance on the matter, as it establishes that the rate at the auction may never be lower than the appraisal value established in the corresponding report (i.e., it removes the 25% margin that was previously permitted).

*(iii) Early termination*

The Mortgage Credit Law regulates in a strict manner the early termination of facility agreements secured by a mortgage over a residential real estate property (or when the purpose of said facilities is to acquire or retain rights of ownership in relation to land or an existing or planned building for residential use) when the borrower is an individual.

In this sense, in order for the creditor to take the corresponding action, the following conditions must be met simultaneously:

- a. The borrower must default on repayment of part of the principal amount of the loan or the corresponding interest.
- b. The creditor must have demanded payment from the borrower and granted them a period of at least one month to pay.
- c. The amount of the instalments due and not paid by the debtor must be equivalent to: (i) 3% of the amount of the loan granted (or a number of instalments equivalent to 12 months) if the default occurs within the first half of the term of the loan; or (ii) 7% of the amount of the loan granted (or a number of instalments equivalent to 15 months) if the default occurs within the second half of the term of the loan.

*(iv) Retroactive effects?*

The Mortgage Credit Law expressly establishes that the changes and amendments introduced will not have retroactive effects with respect to agreements entered into prior to its entry into force, with the exception of two specific provisions:

- a. the interest rate to be applied in the event of early repayment (which will be capped at 0.15%) in the event that the agreement is amended from a variable interest rate loan to a fixed interest rate loan; and
- b. the early termination of pre-existing agreements (except where: (a) the termination occurs before the Mortgage Credit Law enters into force; (b) enforcement has been initiated; or (c) the agreements have been the subject of novation or subrogation the law enters into force), unless the borrower claims that the content of the pre-existing agreement with respect to early termination was more favourable to them.

## V. Conclusions

The entry into force of the Mortgage Credit Law will establish a protective framework for the debtor in relation to mortgage-backed facilities entered into, mainly, with consumers.

The Mortgage Credit Law introduces significant amendments, among which it is worth highlighting the noteworthy extension of the requirements for early termination, the reduction of the early repayment fees, the distribution of mortgage expenses which are to be borne mainly by the creditor, and the definitive prohibition of minimum interest rate clauses.

The information contained in this Legal Briefing is of a general nature and does not constitute legal advice. This document was drafted on 25 March 2019 and Pérez-Llorca does not undertake any commitment or assume any duty to update or review its content.

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