

# PRIVATE TRANSLATION OF LAW 41/2007, OF 7<sup>TH</sup> DECEMBER, MADE BY THE SPANISH MORTGAGE ASSOCIATION

## Disclaimer:

The translation only includes those aspects related to the regulation of the mortgage market and other significant financial and tax regulations.

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**Law 41/2007, of 7th December, by which Law 2/1981, of 25th March, regulating the mortgage market and other rules of the mortgage and financial system are modified, reverse mortgages and long-term care insurance are regulated and certain tax regulations are established.**

## Preamble

### I

The mortgage market is one of the segments in the financial system with great influence on macroeconomics and financial stability. On its operations depends housing finance, which represents about two thirds of the value of the total wealth of Spanish households and conditions their consumer and investment decisions. At the same time, mortgage credits account for a large proportion of lenders' balances and amount to over half of the entire credit of the resident private sector.

It must be remembered that the recent period of extraordinary acceleration in the activity has coincided with a notable stability in the regulation of the mortgage market. The basic rules of the legal framework relating to transparency, loans' mobilisation mechanisms and subrogation and novation have not substantially changed over recent years.

This stability contrasts with the intense increased production of regulation in the other areas of the financial system; and although the durability of the regulations is always desirable, over this time some fundamental factors have changed, the implications of which must be introduced into our legal code. In particular, over the last ten years there has been a phase of expansion of residential mortgage credits in Spain. This expansion is reflected in the growth of the Spanish *cédulas hipotecarias* market which has reached the top positions in Europe in terms of volume issued. The fast development of both markets has brought forward the need to take measures aimed at their correct operation in order, on the one hand, to consolidate the growth of the mortgage securities market and, on the other hand, to prevent regulatory discrimination between the different mortgage loan or credit options at the clients' disposal. Particularly, in the current situation of a moderate rise in the reference interest rates.

The scope of action that is sought by this Law relating to the mortgage market is mainly the elimination of the obstacles preventing the offer of new products, the modernisation of the protection regime by seeking a more effective transparency, which allows the borrowers to take their decision based on the actual risk of the products, and to improve the funding instruments.

## II

Chapter I, relating to transparency in the subscription of mortgage credits and loans, establishes as its basic objective to modernise the protection regime by seeking a more effective transparency, which allows borrowers to make their decisions based on the actual risk of the products. Hence the Law modifies the authorisation which is currently attributed to the Minister for Finance and the Treasury to pass the regulations that guarantee that the contracts expressly and clearly contain the parties' undertakings and rights, extending this authorisation so that the Minister for Finance and the Treasury can regulate, in particular, the issues relating to the transparency of the financial conditions of the mortgage credits and loans.

Furthermore, an express reference is established to the pre-contractual information that the lenders must make available to their clients in order to ensure that, when it comes to contracting the different bank products, they have the most relevant details about their characteristics in order to form an informed opinion about them. Hence the Minister for Finance and the Treasury is authorised to determine the minimum information that lenders must provide to their clients prior to the signing of any contract. This pre-contractual information must permit the client to know the essential characteristics of the products that can be contracted and to assess whether said products are suitable to its requirements and its financial situation.

Both modifications are performed taking into account European regulations and practices in order to guarantee convergence on this matter.

## III

The second area of modification which is dealt with in this Law corresponds to the lenders' refinance mechanisms through the issue of *cédulas hipotecarias* and mortgage bonds. The favourable situation of our mortgage and real estate market over recent years provides a great opportunity to consolidate our mortgage securities market. This challenge requires the improvement of the regulations and techniques which promote innovation and allow for a high degree of flexibility for the institutions issuing these securities. The technical improvements which are introduced focus on two lines of action: the first is to eliminate the administrative obstacles which weigh heavily on the concept of mortgage bonds and the second, which is more profound, consists of enabling more financial sophistication of the issuance of *cédulas hipotecarias* and mortgage bonds.

Firstly, the mortgage loans and credits portfolio, which is used to cover the *cédulas*, does not include those loans or credits which serve as a collateral of an issue of mortgage bonds or have been the object of *participaciones hipotecarias* (mortgage passthroughs). In order to facilitate the segregation of the credits and loans in the covered pool from the rest of the assets of the issuer, a special accounting register is envisaged. Said register will contain all of the mortgage loans and credits which cover the *cédulas* and it will also identify those which comply with the requirements of section II of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market as this is needed in order to calculate the limit established for the issue of bonds contained in article 16. Furthermore, this issuance limit is revised in order to guarantee that the high credit quality of the *cédulas hipotecarias* is maintained, establishing the abovementioned limit at 80% of the mortgage credits and loans which comply with the requirements of the aforementioned section II.

Secondly, some administrative obstacles are removed which have hindered the development of the mortgage bonds in order to achieve a neutral administrative treatment of the bonds vis-à-vis the *cédulas hipotecarias*. Hence the requirement to enter a margin note in the Land Register for each of the mortgages serving as collateral of an issue disappears and the previously compulsory constitution of a bondholders syndicate becomes optional. Furthermore, they receive the same existing treatment for the *cédulas hipotecarias*, by including the resort to the universal asset liability of the issuer in the case that the special guarantees do not cover the amount of the debt. Lastly, it is established that all of the mortgage loans and credits serving as collateral of an issue must comply with

the requirements of section II of the Act, since the nature of this instrument is to permit institutions with greater refinance difficulties to issue high credit quality mortgage securities. .

Thirdly, a series of improvements are included for both instruments, namely *cédulas hipotecarias* and mortgage bonds, which increases the possibility of financial sophistication of the issues. One of the most significant improvements is the possibility of including substitution liquid assets in the issue portfolio, which contributes towards covering the liquidity risk in an eventual situation of bankruptcy, and reinforcing the possibility of covering the interest rate risk through financial derivative contracts associated to an issue, which is produced by entering the economic flows generated by these instruments in favour of the entity in all of the segregated assets over which the mortgage security holder is a creditor with special privilege.

#### IV

Chapter III deals with three areas of action relating to the valuation companies, under the basic principle of maintaining and reinforcing their independence.

First of all, the enhancement of the independence principle for the valuation companies becomes a reality. The aim is to establish a conduct legal framework for the valuation companies which guarantees their independence and the absence of any conflicts of interest with the lenders who finally grant the mortgage loans, through two mechanisms: the first is general, an internal code of conduct to which other measures can be added, and the second, more specific, establishment of a Technical Committee in charge of checking compliance with the independence requirements established by the said regulations and, if applicable, by other mechanisms.

Secondly, modifications are made to the sanctions regime for valuation companies. On the one hand, new cases of infringement are classified deriving from the new obligations regime contained in the Law and the penalties chart is revised in general as a result of the experience obtained from the performance of the sanctioning authority. On the other hand, on grounds of legal and systematic security, the legal seat of the said regime is changed, up until now contained in the tenth additional article of Law 3/1994, of 14<sup>th</sup> April, which adapts the Spanish legislation on Lenders to the Second Banking Coordination Directive and other modifications are introduced relating to the financial system. Hence, this Law fully revises and updates the infringements and sanctions applicable to this type of entity.

Thirdly, a significant holdings regime is established similar to that for lenders which allows for the control of the stockholder composition.

#### V

One of the objectives of this Law is to achieve neutral regulatory treatment of the different types of mortgage credits and loans on the market. There is at present a regulation about the commission for early repayment in the case of subrogation of the mortgage loan which as it is not directly linked to the economic loss suffered by the lender when there is such subrogation, artificially discriminates between the different interest rate structures possible in a mortgage loan. The current regime is also unsatisfactory from the client protection point of view as it permits them having to pay a commission to the lender even when the repayment is in the benefit of the latter.

This Law changes first of all the name of the early repayment commission to compensation as the latter is more in line with its nature. Secondly, this compensation for early repayment is divided into the compensation made to the institution due to the rescission of the contract and due to generating losses because of the loan origination costs; and the compensation for the institution's interest rate risk when the early repayment is made in a situation of falling interest rates. Two elements are introduced so that this second compensation is related to the institution's actual economic loss. The first is the establishment of a calculation base, which it more precisely reflects the institution's risk exposure. The second is the prohibition on collecting the compensation in those cases in which the repayment generates a capital gain for the lender, and it is not therefore financially motivated.

This new compensation regime for early repayments substitutes the previous commission regime for mortgage loans signed after this Law enters into force, so that both concepts can not be collected in any contract.

## VI

Chapter V contains the actions relating to the calculation of the tariff costs relating to the mortgage loans or credits. All of this with the general objective of reducing and encouraging the transparency of the transaction costs for mortgage market operations. Taking into account the regulation established in Law 36/2003, of 11th November, on economic reform measures, relating to the tariff costs on the deeds of modifying novation and subrogation of mortgage loan, greater transparency and the reduction of the said tariffs should be sought, as well as extending said discounts to the case of cancellations, which have not the subrogation as a purpose, and to the mortgage credits. Hence the tariffs of the notary public are determined taking as a base the fees envisaged in the «Documents without quantum» and the determination of the registry tariffs taking as a base the fees established for «Entries», with the maximum reduction established by Law 36/2003, of 11th November, on economic reform measures, of 90 percent for all types of operations.

## VII

Chapter VI makes the mortgage market more flexible by regulating the maximum-sum mortgages, also referred doctrinally to as «floating». The accessoriness and determination, which governs the ordinary mortgages, excludes from our current legal code as ordinary or trade mortgages those mortgages in which there are various secured obligations or in which present and future obligations are mixed. That necessarily determines that mortgages should be constituted for every obligation that is sought to guarantee which, apart from making the operation more expensive, is not competitive in banking practice.

This reform seeks to generalise the possibility of securing with a maximum-sum mortgage other very diverse legal relations, although it is considered appropriate to limit it to credit institutions and not to any creditor given the special supervision regulations applicable to the former. The maximum-sum mortgage will allow for the acceptance of new mortgage products which were until now refused.

The need to advance and make more flexible the legal regime on mortgages, with legal requirements and concepts which cover the new demands, also binds all of the operators that take part in the contract process and the real guarantees, particularly the notaries and the land registrars, so that as legal operators, when it comes to drafting documents and making entries, understand their task as providing guidance and facilitating access to the Register to the authorised securities through the existing legal channels, in order to achieve that the ownership and real rights over them are covered by the preventative legal regime of publicity and security, and they enjoy their benefits in any event, in accordance with the legal and regulatory rules which determine the content of the registry entry, the requirements for their extension, and their effects.

Other measures aimed at promoting the mortgage loan market are to specify the content of the entry of the real mortgage right, avoiding conflicting registry classifications, which prevent uniformity of the rights' registry configuration which imposes their mass contracting. For such purpose, it is established that on entry of the real mortgage right the amount of the debt capital is expressed and, if applicable, the agreed interest, or the maximum amount of the mortgage liability, identifying the guaranteed obligations whatever their nature and duration. The other financial clauses guaranteed by a mortgage, such as those relating to early cancellation, shall be recorded in the entry under the terms of the formalisation deed but always provided that the favourable registry classification has been obtained of the clauses with real content.

On the other hand, novation of the mortgage loans in the debtor's benefit is hindered by the restrictive interpretation of the concept of modifying novation (*novación modificativa*) made by Law 2/1994, of 30<sup>th</sup> March, on subrogation of mortgage loans. What is now adopted is a wider interpretation of when there is a modifying novation so that it will be considered that there has only been a modification and not a cancellation of the legal relationship

and the constitution of a new one in the following cases: capital increase or decrease, the provision or modification of personal guarantees, alteration of the initially agreed or valid interest rate conditions; alteration of the term, of the repayment system or method and any of the loan's other financial conditions.

It is eliminated the legal uncertainty caused by the subsistence of references to regulations expressly derogated in others that remain in force following the entry into force of the Insolvency Law 22/2003, of 9<sup>th</sup> July.

An adequate framework is established which will allow for the possibility of mobilisation of credits or loans guaranteed with first chattels mortgage or non-transferable collateral.

## VIII

As regards the new features that this Law introduces in its additional regulations, some relevant legislative backgrounds must be taken into account. First of all, Law 29/2006, of 14<sup>th</sup> December, on the Promotion of Personal Autonomy and Attention to Dependant Persons, the seventh additional regulation of which «Private Instruments to cover long-term care» states that the Government in the period of six years shall promote the legislative modifications in order to regulate the private cover of the situations of long-term care and that, in order to facilitate joint financing by the beneficiaries of the services established in the act, it will be promoted the regulation of the tax treatment of the private instruments covering long-term care .

Secondly and albeit not in chronological order, Law 35/2006, of 28<sup>th</sup> November, on Personal Income Tax and the partial modification of the corporate income tax, non-resident income tax and on net worth tax introduces a series of tax measures to promote the cover of the long-term care by private insurance and pension plans, modifying the substantive regulations of the latter.

Releasing the value of the home through financial products could contribute towards easing one of the biggest socioeconomic problems in Spain and most developed countries: satisfying the increased income requirements in the latter stages of people's lives. The reverse mortgage regulated in this Law is defined as a mortgage loan or credit from which the owner of the property makes disposals, normally periodical, although the disposal may be in a lump sum, up to a maximum amount determined by a percentage of the valuation at the time it is constituted. When said percentage is reached, the elderly person or the dependant person stops disposing of the income and the debt continues generating interest. The recovery by the lender of the credit plus the interest normally takes place once the owner dies by the heirs cancelling the debt or enforcement of the mortgage guarantee by the lender.

There is therefore no doubt that the development of a reverse mortgage market, which allows elderly people to use part of their real estate assets in order to increase their income, offers plenty of potential to generate economic and social benefits. The possibility of enjoying savings accumulated in the home during one's lifetime would enormously increase the ability to temper the income and consumption profile throughout the lifecycle with the resulting positive effect on welfare.

In relation to the long-term care insurance, its content incorporates the regulation of private instruments for long-term care cover, which can be organised either through an insurance contract signed with insurance companies, including the provident societies, or through a pensions plan.

The long-term care cover performed through an insurance contract binds the insurance company, in the event that there is a situation of long-term care in accordance with the rules regulating the promotion of personal autonomy and attention to dependant persons and under the terms set out in the law and in the contract, to comply with the agreed benefit in order to partial or totally, directly or indirectly, deal with the detrimental consequences for the insured party deriving from said situation. These insurance policies can be contracted by the insurance companies with the compulsory administrative authorisation for the performance of life and health insurance activities. As regards the pension plans, which envisage cover for the risk of this contingency, they must expressly state as such in their specifications.

The Law ends with three final regulations as well as those relating to regulatory authorisation, the basic nature and competences and the entry into force, and covers the modification of other financial regulations in order to facilitate compliance with the rules contained in the main body of this Act.

## CHAPTER I

### Transparency in contracting mortgage loans and credits

**Article 1.** Modification of Law 26/1988, of 29<sup>th</sup> July, on Discipline and Intervention of the credit institutions.

1. Article 48, section 2, letter a) of Law 26/1988, of 29<sup>th</sup> July, on Discipline and Intervention of the credit institutions, will be drafted as follows:

«a) To establish that the corresponding contracts are formalised in writing and pronounce precise regulations in order to ensure that they expressly and sufficiently clearly reflect the undertakings contracted by the parties and their rights vis-à-vis the contingencies of each type of operation, and particularly the issues relating to the transparency of the financial conditions of the mortgage credits and loans. For such purpose, it can determine the issues and contingencies that the contracts relating to typical financial operations with their clientele must expressly state or envisage, require that the institutions establish forms for them and impose some type of administrative control over said forms. The information relating to transparency of the mortgage credits or loans, when it is a residential mortgage, must be supplied regardless of their amount.»

2 A new letter h) is inserted in section 2 of article 48.2 of Law 26/1988, of 29<sup>th</sup> July, on Discipline and Intervention of the credit institutions, as follows:

«h) To determine the minimum information that the lenders must provide to their clients with enough notice before they accept any contractual obligations with the institution or accept any contract or offer to contract, as well as the operations and bank contracts in which such pre-contractual information is required. Said information is aimed at informing the client of the essential characteristics of the proposed products and to assess whether they are suitable to their needs and, when it may be affected, to their financial situation».

## CHAPTER II

### Refinance Mechanisms

#### Article 2. Modification of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market.

1. Article 1 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 1.

The financial institutions referred to in this Law can grant mortgage loans and issue the securities necessary to fund them in accordance with the requirements and objectives established in it, without prejudice to the fact that these institutions or others can issue and transfer obligations, secured or not, in accordance to the current legislation.

This Law, and its regulations, shall be applied to all securities regulated therein and issued in Spanish territory.»

2. Article 2 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 2.

The credit institutions which are detailed below can grant loans and credits and issue the securities regulated in this Law, under the conditions that are determined in the regulations:

- a) banks and, when permitted under their articles of association, official credit institutions,
- b) the savings banks and the Spanish Confederation of Savings Banks (*Confederación Española de Cajas de Ahorros*),
- c) credit cooperatives,
- d) financial credit establishments».

3. Paragraphs one, two and four are redrafted and a new paragraph five is introduced to article 5 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, as follows:

«Article 5.

The loans and credits referred to in this Law shall be in every case secured by real estate mortgage constituted with first range over the full ownership of the entire property. If over the same property there are other mortgages or it is affected by disposal prohibitions, resolutive condition or any other limitation over the ownership, one and other shall be cancelled or they must be placed over the mortgage which is constituted before the issuance of securities.

The loan or credit secured by this mortgage shall not exceed 60 percent of the valuation of the mortgaged asset. When the construction, renovation or acquisition of homes is financed, the loan or credit can amount to 80 percent of the valuation, notwithstanding the exceptions envisaged in this Law.

The loans and credits referred to in this article can include those others which are secured by real estate situated within the European Union through equivalent guarantees to those defined in this Law.

The following will be determined in the regulations:

- 1. The assets which can not be accepted as guarantee because they do not represent a sufficiently stable and lasting security. Under no circumstances can officially sponsored housing under public protection be excluded as mortgageable assets.

2. The cases in which the 60 percent is exceeded between the guaranteed loan or credit and the value of the mortgaged asset, with the maximum limit of 80 percent, as well as in those where the Administration, depending on the characteristics of the mortgaged assets, may establish percentages lower than 60 percent. The maximum limit of 80 percent will under all circumstances be applied to the loans and credits guaranteed with a mortgage over officially protected housing.
3. The issue conditions for the securities issued with mortgage guarantee over real estate under construction.
4. The conditions in which the 80 percent ratio between the guaranteed loan or credit and the value of the mortgaged dwelling can be exceeded, without exceeding 95 percent of that value, using additional guarantees provided by insurance companies or credit institutions.
5. The way in which the equivalence of the real guarantees over real estate in other Member States of the European Union will be appreciated as well as the conditions for the issue of securities which are issued taking them as guarantee».

4. Article 11 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 11.

The institutions referred to in article 2 which have mortgage loans or credits with the requirements established in the previous section can issue *cédulas hipotecarias* and mortgage bonds, in series or individually and with the financial characteristics desired in accordance with what it is stated in the following articles. In particular, the *cédulas hipotecarias* and mortgage bonds can include early repayment clauses as decided by the issuer according to that specified in the terms of issue. Always provided that the applicable regulation is Law 24/1988, of 28<sup>th</sup> July, on the Stock Market, these issues will be adapted to the regime envisaged thereof.»

5. Article 12 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 12.

The *cédulas hipotecarias* can be issued by all of the institutions referred to in article 2.

The capital and interests of the *cédulas hipotecarias* shall be particularly guaranteed, without the need for registry entry, by mortgage, particularly those which at any time are entered in favour of the issuing institution and are not **servicing as a collateral of mortgage bonds**, without prejudice its universal asset liability and, if any, by the substitution assets included in section two of article 17 and by economic flows generated by the derivative financial instruments linked to each issue, under the conditions determined in the regulations.

The institution issuing the *cédulas hipotecarias* will keep a special accounting register of the loans and credits that serve as collateral of the issues of *cédulas hipotecarias* and, if any, of the substitute assets fixed that cover them, as well as the derivative financial instruments linked to each issue. This special accounting register must also identify, for the purposes of calculating the limit established in article 16, from the total registered loans and credits, those that fulfil the conditions required in the second section of this Law. The annual accounts of the issuing institution shall contain, as determined in the regulations, the essential details of said register.

The issues of *cédulas hipotecarias* will not be affected by chapter X of Legislative Royal Decree, of 22<sup>nd</sup> December, which passes the consolidated text of the Limited Liability Companies' Law. Nor shall they be entered in the Trade Register».

6. Article 13 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 13.

The mortgage bonds can be issued by all of the institutions referred to in article 2.

The capital and interests of the bonds will be specially guaranteed, without the need for entry in the register, by mortgage over the mortgage loans and credits performed in public deed, without prejudice to the universal asset liability of the issuing institution, and, if any, by the substitution assets covered in section two of article 17 performed in public deed and by the economic flows generated by the derivative financial instruments linked to each issue, under the conditions determined in the regulations.

All of the loans and credits affected by an issue of mortgage bonds must meet the requirements of section II of this Law.

The institution issuing the mortgage bonds will keep a special accounting register of the mortgage loans and credits affected by the issue and, if any, of the substitution assets included in the cover, as well as of the derivative financial instruments linked to the issue.

A syndicate of bondholders can be constituted when the bonds are issued in series, in which case the issuing institution shall designate a commissioner to attend the execution of the public deed mentioned in the second paragraph of this article on behalf of the future bondholders. Said person, whose appointment must be ratified by the bondholders' plenary, will be the syndicate's chairperson, and apart from the powers conferred in the said deed or attributed by the aforementioned plenary, will legally represent the syndicate, check that the institution maintains the percentage referred to in article 17.1 and perform the corresponding actions.

The chairperson, and the syndicate in everything relating to its composition, powers and competences, shall be governed by the rules in chapter X of Legislative Royal Decree, of 22<sup>nd</sup> December, which passes the consolidated text of the Limited Liability Companies' Law, insofar as they do not contradict the content of this Law.»

7. Article 14 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 14.

The *cédulas hipotecarias* and mortgage bonds incorporate their holder's credit right against the issuing institution, guaranteed as set out in articles 12 and 13, and shall entail execution in order to claim payment from the issuer, after they expire. The holders of the said securities shall be creditors with special preference, as indicated in number 3 of article 1923 of the Civil Code, over any other creditors as regards all of the mortgage loans and credits entered in favour of the issuer in case of *cédulas hipotecarias*, except for those that cover the mortgage bonds, and in relation to the mortgage loans and credits serving as a collateral in case of bonds and, in both cases, in relation to the substitution assets and the economic flows generated by the derivative instruments linked to the issues, if any. The bondholders of an issue shall have prevalence over the holders of *cédulas hipotecarias* over a loan or credit serving as a collateral by said issue. All of the holders of *cédulas hipotecarias*, whatever their date of issue, shall have the same prevalence over the loans and credits that guarantee them, and, if any, over the substitution assets and over the economic flows generated by the derivative instruments linked to the issues.

In the event of the issuer's bankruptcy, the holders of *cédulas hipotecarias* and the mortgage bond holders shall enjoy the special privilege established in number 1 of section 1 of article 90 of the Bankruptcy Law 22/2003, of 9<sup>th</sup> July.

Notwithstanding the above, in accordance with number 7 of section 2 of article 84 of the Bankruptcy Law 22/2003, of 9<sup>th</sup> July, during the bankruptcy, and as credits against the mass, there will be satisfied all the payments which correspond to the repayment of the capital and interest of the issued *cédulas hipotecarias* and mortgage bonds, which are pending on the date of the bankruptcy application up to the amounts received by the debtor from the mortgage loans and credits and, if any, from the substitution assets which backup the *cédulas hipotecarias* and mortgage bonds and the economic flows generated by the financial instruments linked to the issues.

In the event that, temporarily, the revenue received by the debtor is insufficient in order to meet the payments set out in the previous paragraph, the bankruptcy administration must pay them by liquidating the substitution assets serving as collateral of the issue, and if these are insufficient, funding/financial operations must be performed in order to comply with the payment obligations to the holders of *cédulas hipotecarias* or bondholders, subrogating the financial backer in their position.

In the event that the procedure is to be followed according to that indicated in number 3 of article 155 of the Bankruptcy Law 22/2003, of 9<sup>th</sup> June, the payment to all of the owners of *cédulas hipotecarias* issued by the issuer shall be done proportionally, regardless of the issue date of their securities. If the same credit is affected by payment of *cédulas hipotecarias* and to an issue of bonds, the bond owners will be paid first.»

8. Article 16 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 16.

The institutions shall not issue *Cédulas Hipotecarias* for an amount greater than 80 per 100 of the non-repaid mortgage loans and mortgage credits in their portfolios fulfilling the requirements stated in Section II, after the amount of those loans serving as a collateral of mortgage bonds has been deducted.

The *cédulas hipotecarias* can be backed up to a limit of 5 percent of the issued capital by the substitution assets listed in section two of article 17.»

9. Article 17 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 17.

One. The updated value of the mortgage bonds must be at least 2 percent less than the updated value of the affected mortgage loans and credits. The calculation method for the updated value will be determined in the regulations.

Two. The mortgage bonds can be backed up to a limit of 10 percent of the capital of each issue by the following substitution assets:

a) Fixed-income securities represented by notes on account issued by the State, other Member States of the European Union or the Spanish Official Credit Institute,

b) *Cédulas hipotecarias* listed on an official secondary market, or on an administered market, provided that said *cédulas hipotecarias* are not guaranteed by any loan or credit with mortgage collateral granted by the issuer of the bonds or by other institutions in its group,

c) Mortgage bonds listed in an official secondary market, or on an administered market, with a credit classification equivalent to that of the Kingdom of Spain, provided that said securities are not guaranteed by any loan or credit with mortgage guarantee granted by the issuer of the bonds or by other institutions in its group

d) securities issued by Mortgage Securitisation Funds or Asset Securitisation Funds listed on an official secondary

market or on an administered market, with a credit classification equivalent to that of the Kingdom of Spain, provided that said securities are not guaranteed by any loan or credit granted by the issuer of the mortgage bonds or by other institutions in its group,

e) other fixed-income securities listed on an official secondary market or on an administered market, with a credit classification equivalent to that of the Kingdom of Spain, provided that said securities were not issued by the issuer of the mortgage bonds or by other institutions in its group,

f) other low risk and high liquidity assets determined in the regulations».

10. Article 18 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 18.

One. The issuer is bound to maintain at all times the percentages referred to in the previous two articles.

Two. If due to the repayment of the loans and credits, the amount of the issued *cédulas hipotecarias* and bonds exceeds, respectively, the established limits, the institutions can opt to acquire their own mortgage bonds, *cédulas hipotecarias* or *participaciones hipotecarias* (mortgage passthroughs) until the proportion is re-established or, in the event that there is the cancellation of mortgages affected by an issue of bonds, to substitute them for others that meet the required conditions, through the corresponding public deed.»

## CHAPTER III

### Valuation Entities

#### **Article 3. Promotion of the independence of the valuation entities.**

1. The Heading of Section 1 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Section I.

Financial institutions and valuation companies».

2. Article 3, of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, will be redrafted as follows:

«Article 3.

1. The valuation companies and the valuation services of the lenders shall be subject to the prior approval, independence and secrecy requirements that are established in the regulations.

2. The valuation companies which provide their services to lenders of their same group, and the valuation companies which derive at least 25 percent of their total revenue, during the time period established in the regulations, from one lender or from all of the lenders in the same group, must, provided that any of these lenders has issued or has in circulation mortgage securities, have suitable mechanisms in place in order to favour the independence of the valuation activity and to avoid conflicts of interest, particularly with the lender's managers or units which, without specific competence in the analysis or management of risks, are related to granting or marketing mortgage credits or loans.

These mechanisms shall at least include an internal code of conduct which establishes the incompatibilities of their managers and administrators and the other issues which are most adequate according to the institution's size, business type and other characteristics. The Bank of Spain shall check said mechanisms and can establish the minimum requirements that must be generally fulfilled and require the entities, in a well-reasoned manner, to adopt the additional measures which are deemed necessary in order to preserve their professional independence.

The obligation to have those mechanisms will also affect the lenders' own valuation services and those valuation companies controlled or, where there is a significant influence over its management, by shareholders with specific interests in the development or marketing of real estate, or in activities which, in Bank of Spain's view, are analogous in nature.

3. The credit institutions which have issued or have in circulation mortgage securities and have valuation services or entrust valuations to a valuation company in its own group, must set up a technical committee to verify the compliance with the independence requirements contained in the mechanisms mentioned in the previous paragraph. Said committee will prepare an annual report on the degree of compliance with the said requirements which must be sent to the institution's board of directors or equivalent body. The said annual report must also be sent to the Bank of Spain.

#### **Article 4. Sanctioning regime**

A new article 3 bis is incorporated into Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, which will be written as follows:

«Article 3 bis.

1. The valuation companies and the lenders which have their own valuation services must comply with the regulations applicable to estate valuations for the mortgage market or other financial purposes to accurately draft the certificates and reports that they issue and to perform at any times with professional diligence. Breach of any of the obligations will lead to the application of the sanctioning regime set out in this article.

2. The infringements are classified as very serious, serious and minor.

a) Very serious infringements are considered as:

1.<sup>a</sup> The breach, for a period of over six months, of the minimum share capital requirement in order to perform the valuation activity set out in the mortgage market legislation, and, during the same period, the absence of the civil liability insurance, or for a lower cover limit than that established, as set out in the regulation.

2.<sup>a</sup> The performance of activities other than the legally established corporate purpose, unless it is merely occasional or a one-off.

3.<sup>a</sup> Having deficiencies in the administrative organisation, be it technical or staff ones, including deficiencies in the minimum requirements for qualified administrators or professionals, or in the internal control procedures, when due to such deficiencies the institution's capacity to know the situation and conditions of the real estate market in which they operate, the uniform compliance with the applicable valuation regulations, their professional independence from shareholders' or clients, or the control of the secrecy obligations or incompatibilities affecting the professionals in their service is not ensured .

4.<sup>a</sup> The breach by the signatories of the valuation reports of the professional qualification requirements set out in the regulations.

5.<sup>a</sup> The issue of valuation certificates or reports which contain in a clear manner:

a) The lack of truth in the valuation and, in particular, the lack of consistency with the details and tests obtained in the valuation activity.

b) The lack of caution in the valuation when the issue of said document is to value assets eligible as guarantee for credits that are or will be part of the cover for mortgage securities, or for the cover of technical provisions of the insurance companies or for the real estate assets of the pension funds, or for any other purpose in which the principle of valuation caution is applicable.

In any event, the clear lack of truth or, if applicable, the clear lack of valuation caution will be assumed when, as a result of the valuations contained in any of said documents leads to a false appearance that a credit institution, an insurance company, a pension fund or any other financial institution complies with the financial guarantees required therein.

6.<sup>a</sup> Resisting, refusing or obstructing inspection by the Bank of Spain, the National Stock Market Commission or the Directorate General for Insurance and Pension Funds within their respective competences, provided that there has been an explicit, written request.

7.<sup>a</sup> The breach of the independence rules contained in the internal regulations envisaged in section 2 of article 3 of this Act.

8.<sup>a</sup> Endangering the safe and cautious management of a valuation company through the owner of a significant interest exerting influence, in accordance with that set out in the regulations.

9.<sup>a</sup> The serious infringements, when during the five years prior to their commission there was a firm sanction imposed for the same type of infringement.

b) Serious infringement is considered as:

1.<sup>a</sup> The breach of the minimum capital requirement to perform the valuation activity set out in the mortgage market legislation, when it is not a very serious infringement, as well as the deficiencies that are appreciated in the civil liability insurance policy, unless they are merely occasional or isolated or involve exception exclusions for certain damages in accordance with normal insurance cover practice.

2.<sup>a</sup> Presenting deficiencies in the administrative organisation, be it technical or staff ones, including the minimum requirements for qualified administrators or professionals, in the internal control procedures, once the period granted by the competent authorities for their correction has expired and provided that it is not a very serious infringement.

3.<sup>a</sup> The issue of valuation certificates which are not in accordance with the valuation report, unless it is merely occasional or isolated.

4.<sup>a</sup> The issue of valuation certificates or reports which contain:

a) The lack of truth and, in particular, the lack of agreement with the details and tests obtained from the valuation activity, as well as the continuous breach of the valuation principles, procedures, checks and instructions set out in the applicable regulations.

b) The lack of caution in the valuation when the issue of said document is to value assets eligible as guarantee for credits that are or will be part of the cover for mortgage securities, or for the cover of technical provisions of the insurance companies or for the real estate assets of the pension funds, or for any other purpose in which the principle of valuation caution is applicable, unless said failure is occasional or isolated.

In both cases provided that the conduct does not constitute a very serious infringement.

5.<sup>a</sup> Any other breach of the valuation rules which could cause financial damage to third parties or to the person to whom the service is provided.

6.<sup>a</sup> The failure to send the details which must be provided to the Bank of Spain, the National Stock Market Commission or the Directorate General for Insurance and Pension Funds, or their lack of truth when this hinders the appreciation of the activity performed by the institution or its asset or organisational situation. For these purposes, it will be understood that there is a failure to send when it is not done within the period granted for such purpose by the competent body, when the latter sends a written request for compliance with the obligation or the request is repeated.

7.<sup>a</sup> The breaches of the duties of professional secrecy, independence and incompatibility in the performance of their functions which do not lead to very serious infringement, unless they are merely occasional or isolated.

8.<sup>a</sup> The minor infringements when during two years prior to their commission there was a firm sanction imposed on the valuation services and companies for the same type of infringement.

c) Minor infringement shall be considered the other acts and omissions which breach the applicable regulations.

3. The valuation companies and the credit institutions which provide valuation services, as well as their administrators and managers, may be subject to the sanctions set out in Chapter III of Heading I of Law 26/1988, of 29<sup>th</sup> July, on Credit Institutions Discipline and Intervention, with the following modifications:

- a) The sanction to revoke the authorisation shall be held replaced by the definitive loss of the authorisation to provide valuation services.
  - b) For very serious infringements the sanction of suspension of the authorisation to provide valuation services can also be imposed for between one and five years, and for serious infringements suspension of said authorisation for up to one year.
  - c) The disqualification sanctions set out in article 12 shall be understood as referring to both credit institutions and to valuation companies.
4. The sanctioning procedure applicable shall be regulated in Royal Decree 2119/1993, of 3<sup>rd</sup> December, on the sanctioning procedure applicable to the persons acting on the financial markets.

The sanctioning competence shall be as set out in article 18 of the Law 26/1988, of 29<sup>th</sup> July, on Credit Institutions Discipline and Intervention with the following modifications:

- a) The Bank of Spain shall obligatorily instigate sanctioning proceedings when there is a reasoned communications with grounds from another administrative body or authority which states that the irregular provision of valuation services has had repercussions within their scope of administrative action.
  - b) In the case set out in the previous letter, before a sanction is imposed the competent administrative body or authority shall have to report.
5. In the other issues relating to the sanction regime, the set out in Law 26/1988, of 29<sup>th</sup> July, on Discipline and Intervention of the Credit Institutions shall be applied, with the adaptations established in the regulations will be applicable.
6. The Tenth Additional Regulation of the Law 26/1988, of 29<sup>th</sup> July, on Credit Institutions Discipline and Intervention,, in accordance with its subsequent regulations, shall be applicable to those individuals or legal entities who, without being authorised to develop valuation activities, provides these services to the public.

**Article 5. A new article 3 bis I) is incorporated into Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, which will be drafted as follows:**

«The credit institutions, even those with their own valuation services, must accept any valuation of a property provided by the client, provided that it is certified by a valuer approved in accordance with this Law and it has not legally expired, and without prejudice to that fact , the lender can carry out the checks that it deems relevant; under no circumstances can the cost thereof be passed on to the client which provides the certificate. »

**Article 6. Significant shareholdings' regimes.**

A new article 3.3 is incorporated into Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, which will be drafted as follows:

«1. Every individual or legal entity that wishes to directly or indirectly acquire a significant shareholding in a valuation company must previously inform the Bank of Spain. Furthermore, the Bank of Spain must be informed, as soon as it becomes aware, of the acquisitions or transfers of interests in their capital which exceed the level indicated in section 2 of this article.

2. For the purposes of this Law significant shareholdings in a valuation company shall be understood as that which directly or indirectly reaches at least 15 percent of the capital or of the voting rights of the company.

They are also considered significant shareholdings those that, without reaching the indicated percentage, allow for the performance of a notable influence over the company

3. The Bank of Spain shall have a maximum period of three months counting from the date on which it was informed to, if applicable, deny the authority for the acquisition. The denial can be based on the fact that the acquirer is not considered suitable. Amongst other factors, the suitability will be appreciated according to:

- a) The commercial and professional honourableness of the shareholders. This honourableness shall be presumed when the shareholders are Public Administrations or entities depending on them.
- b) The asset resources that the said shareholders use to cover their commitments.
- c) The lack of transparency in the structure of the group that the company may possibly belong to, or the existence of serious difficulties in inspecting or obtaining the necessary information about the development of its activities.

If the Bank does not pronounce in the said period, it shall be understood that the plan is accepted.

4. When one of the acquisitions referred to in section 1 of this article is performed without having previously informed the Bank of Spain or, having informed it, the three month period has not passed as set out in the previous section, or if the Bank expressly opposes, the following effects will occur:

- a) In all cases and automatically, the political rights corresponding to the irregularly acquired interest can not be performed. If however they are exercised, the corresponding votes will be null and the agreements can be challenged through the courts, as set out in section 2 of chapter V of legislative Royal Decree 1564/1989, of 22<sup>nd</sup> December, which passes the consolidated text of the Limited Liability Companies Law, for which the Bank of Spain has authorisation.
- b) Furthermore, the sanction set out in article 3 bis of this Act can be imposed.

## CHAPTER IV

### Early repayment compensation regime

#### Article 7. Scope of application.

This chapter will be applicable to the mortgage credit or loan contracts subscribed after the entry into force of this Law and even when they do not include the possibility of early repayment, when one of the following circumstances occurs:

1. It is a mortgage credit or loan and the mortgage is secured by a residential property and the borrower is an individual.
2. The borrower is a legal entity subject to the taxation system of reduced sized enterprises, under the Corporation Tax.

In this mortgage credit or loan contracts it can not be claimed a commission for total or partial early repayment.

In any case, the institution will be bound to issue the bank documentation which proves the payment of the loan without collecting any commission for it.

#### Article 8. Compensation for withdrawal.

1. In the total or partial subrogated and non-subrogated cancellations which occur in the mortgage credits or loans referred to in the previous article of this Law, the amount to receive by the creditor for compensation for withdrawal, can not exceed:

- i) 0.5 percent of the early repaid capital when the early repayment is done within the first five years of the life of the credit or loan, or
- ii) 0.25 percent of the early repaid capital when the early repayment is done at a time after that indicated in previous point.

2. If compensation for withdrawal is agreed equal to or lower than that indicated in the previous section, the compensation to receive by the credit institution shall be as agreed.

#### Article 9. Compensation for interest rate risk.

1. In the total or partial subrogated and non-subrogated cancellations of the mortgage credit or loans that occur within an interest rate revision period whose agreed duration is equal to or less than twelve months, the credit institution will not be entitled to receive any amount by way of compensation of interest rate risk.
2. In the total or partial subrogated and non-subrogated cancellations of the other mortgage credits and loans, the compensation for interest rate risk shall be as agreed and shall depend on whether the cancellation generates a capital gain or loss to the institution. Capital gain due to exposure to interest rate risk shall be understood as the positive difference between the capital outstanding at the time of the early cancellation and the market value of the loan or credit. When said difference is negative it shall be held that there is a capital loss for the credit institution.

The market value of the loan or credit shall be calculated as the sum of the current value of the instalments outstanding until the next interest rate revision and the current value of the capital outstanding which would remain at the time of the revision should the early cancellation not occur. The interest rate for the updating will

be the market rate applicable to the remaining period up until the following revision. The loan contract shall specify the index or reference interest rate which will be used to calculate the market value from those determined by the Ministry of Finance and Treasury.

In case of partial cancellation, the percentage of the capital outstanding that is being prepaid will be applied to the result of the previous formula.

3. The credit institution can not receive any compensation for interest rate risk in the event that the cancellation of the credit or loan generates a capital gain in its favour.
4. The contract must specify which of the following two methods for calculating the compensation for interest rate risk shall be applied:
  - A fixed percentage established in the contract, which must be applied to the capital outstanding at the time of the cancellation.
  - The total or partial loss that the cancellation generates to the institution, calculated in accordance with section two. In this case the contract shall anticipate that the institution compensates the borrower in a symmetric manner in the case that the cancellation generates a capital gain for the institution.

## CHAPTER V

### Tariff costs

#### **Article 10. Calculation of the tariff costs.**

1. Article 8 of Law 2/1994, of 30<sup>th</sup> March, on subrogation and modification of mortgage loans, is redrafted as follows:

«Article 8. Notary and registry fees in the subrogation, modification and cancellation of mortgage credits and loans.

In order to calculate the notary fees for the subrogation, modification and cancellation deeds of the mortgage credits and loans, the tariffs shall be applied corresponding to the "Documents without quantum" established in number 1 of Royal Decree 1426/1989, of 17<sup>th</sup> November, which approves the notaries' tariffs.

In order to calculate the registry fees for the subrogation, modification and cancellation deeds of the mortgage credits and loans, the tariffs shall be applied corresponding to number 2, "Entries", of appendix I of Royal Decree 1427/1989, of 17<sup>th</sup> November, which approves the tariffs for the land registrars, taking as a base the amount of the capital outstanding, with a reduction of 90 percent.»

2. The heading of article 9 of Law 2/1994, of 30<sup>th</sup> March, on subrogation and modification of mortgage loans, is redrafted as follows:

«Article 9. Tax Benefits.»

## CHAPTER VI

### Improvement and relaxation of the mortgage market

#### Article 11. Modification of the Mortgage Law of 8th February 1946

1. Article 12 of the Mortgage Law of 8<sup>th</sup> February 1946 shall be drafted as follows:

«The entry of the real mortgage right shall state the amount of the capital of the debt and, if applicable, the agreed interests, or the maximum amount of the mortgage liability (*responsabilidad hipotecaria*), identifying the guaranteed obligations whatever their nature and their duration.

The early expiration clauses and the other financial clauses on the obligations guaranteed by mortgage in favour of the institutions referred to in article 2 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, in the case of favourable registry judgement of the clauses of a real state nature, shall be recorded in the entry under the terms resulting from the deed.»

2. Article 130 of the Mortgage Law of 8<sup>th</sup> February 1946, shall be drafted as follows:

«The direct enforcement procedure against the mortgaged assets can only be exercised as a realization of a registered mortgage, on the basis of those issues contained in the title which are been stated in the respective entry».

3. The first paragraph of article 149 of the Mortgage Law of 8<sup>th</sup> February 1946, is drafted as follows:

«The credit or loan guaranteed by mortgage can be completely or partially ceded in accordance with that stated in article 1526 of the Civil Code. The cession of the ownership of the mortgage that guarantees a credit or loan must be performed in a public deed and be entered in the Land Register».

4. A new Article 153 bis is introduced in the Mortgage Law, of 8<sup>th</sup> February 1946, according to the following terms:

“Article 153 bis.

Maximum sum mortgages may also be created:

a) in favour of the financial institutions referred to in article 2, Law 2/1981 of 25<sup>th</sup> March, regulating the mortgage market, as a collateral of one or several debts, of any nature, present and/or future, without the need for novation covenant of them.

b) in favour of public administrations holding a Tax or Social Security Credit, without the need for a novation covenant of them.

The statement of the following in the mortgage deed and in the registration deed will be sufficient: its denomination, and when required, the general description of the basic legal acts of which the secured debt come or may come from in the future; the maximum amount secured by the property; the mortgage term; and the calculating method of the liquid final secured balance.

It can be agreed in the title deed that the demanded amount in the event of an enforcement process is the resultant from the liquidation carried out by the creditor financial institution, in the way agreed by the parties in the deed.

Upon the expiration date agreed by the signatories, or any deferral, the mortgage action may be executed according to articles 129 and 153 of the Law hereof, and to concordant ones of the Spanish Civil Procedure Law.

**Article 12. Modification of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market.**

1. Article 4 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, shall be drafted as follows:

«Article 4. The objective of the loan operations referred to in this Law shall be to finance, with ordinary or maximum sum mortgage secured on real estate, the construction, renovation and acquisition of dwellings, urban development and public infrastructure work, construction of agricultural, tourism, industrial and commercial buildings and any other building work or activity as well as any other loans granted by the entities mentioned in article 2 and guaranteed by real estate mortgage under the conditions established in this Law, whatever their purpose.

The disposals of the loans, the mortgage collateral of which correspond to real estate under construction or renovation, can be fixed to a calendar agreed with the lender according to the execution of the building work or the investment and the evolution of the sales or allocations of the housing.»

2. Article 10 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, shall be drafted as follows:

«Article 10. The mortgages registered in favour of the institutions referred to in article 2 can only be rescinded or contested under that set out in article 71 of the Bankruptcy Law 22/2003, of 9<sup>th</sup> July, by the bankruptcy administration which will have to prove the existence of fraud in the constitution of the burden. Third party rights in good faith will however survive.»

3. Article 15, paragraph seven, of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, shall be drafted as follows:

«In the case of bankruptcy of the institution issuing the participation, the business of issuance of the participation can only be contested under the terms of article 10 and therefore the holder of that participation will enjoy an absolute right of separation.»

4. Two new articles 26 and 27 are added to Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market, which shall be drafted as follows:

«Article 26.

The credits or loans guaranteed with first chattel mortgage or first non-transferable collateral can be moved under the terms and with the requirements determined in the regulations.

Article 27.

The same specialities that may be established in the regulations shall be applied to the secondary chattels market securities issued in accordance with that set out in articles 11 to 18 of this Law, although the references to the Land Register shall be understood as referring to the Registry of Personal Property.»

**Article 13. Modification of Law 2/1994, of 30<sup>th</sup> March, on subrogation and modification of mortgage loans.**

1. Article 2 of Law 2/1994, of 30<sup>th</sup> March, on subrogation and modification of mortgage loans, shall be drafted as follows:

« The debtor shall be able to subrogate with another financial institution than those mentioned in the previous article, without the creditor's consent, when, in order to pay the debt, he previously has borrowed the money from said financial institution, through a public deed, stating his intentions according to the provisions of article 1.211 of the Civil Code.

The institution ready to accept the subrogation shall submit a binding offer to the debtor in which the financial conditions of the new mortgage loan shall be stated. When there is more than one mortgage credit or loan over the property registered in favour of the same creditor, the new institution must be subrogated in all of them.

The debtor's acceptance of the offer will imply its authorisation so that the offering institution can notify, through a notary public, the creditor of its willingness to be subrogated, and can request it to deliver, in the maximum period of seven calendar days, the certification of the amount of the debtor's debit under the mortgage loan or loans in which it is to be subrogated.

Once the certification is delivered, the creditor will be entitled to enervate the subrogation if, in the period of fifteen calendar days, counting from the notification of the request and in response to it, it appears before the same notary public who made the notification referred to in the previous paragraph and gives a binding declaration to the effect that it is willing to formalise with the debtor a modification of the conditions of the loan which are equal to or improve the binding offer. The notification certificate will state this declaration.

Otherwise, in order for the subrogation to take effect it will be enough that the subrogated entity states in the same deed that it has paid to the creditor the amount proven by the latter of the pending capital and interest and commissions that are yielded but unpaid. A receipt of the bank operation performed for such purpose will be incorporated into the deed and it will expressly indicate that it was made for such purpose. The authorising notary public will check the existence of said bank document proving payment to the original creditor, and that there has been no enervation as referred to in the previous paragraph, for the purpose of which the subrogated entity must present a copy of the notarial certification of notification of the subrogation offer which shows that there has been no response at all with the effect of enervating the subrogation.

However, if the payment has still not been made because the creditor has not communicated the proven amount, or refuses for whatever reason to accept its payment, it will be sufficient that the subrogated entity calculates it, under its responsibility and accepting the consequences for its mistake, which can not be passed on to the debtor, and, after stating it, deposits said sum in the power of the notary public authorising the subrogation deed, at the disposal of the creditor entity. For such purpose, the notary public shall on its own initiative notify the creditor entity by sending an authorised copy of the subrogation deed, and the latter can plead mistake in the same way within the next eight days.

In this case, and without prejudice to the fact that the subrogation takes on all its effects, the judge who is competent to execute the enforcement process, on request by the creditor entity or the subrogated entity, will summons them, within eight days, to appear at court and after having heard them will admit the documents that they present and will agree, within three days, as he deems appropriate. The decision will be appealed to one effect.»

2. Article 4 of Law 2/1994, of 30<sup>th</sup> March, on subrogation and modification of mortgage loans, shall be drafted as follows:

«Article 4. Public deed.

- 1 The subrogation deed can only agree the modification of the ordinary and delay interest rate conditions initially agreed or in force, as well as the alteration of the loan term, or both.
- 2 When the borrower is one of the institutions referred to in article 1 of this Law, the public deed of modification

of mortgage loans can refer to one or various of the following circumstances:

- i) Capital increase or decrease;
- ii) the alteration of the loan term;
- iii) The initially agreed or valid interest rate conditions;
- iv) The repayment method or system and any of the loan's other financial conditions;
- v) The provision or modification of the personal guarantees.

3. The modifications envisaged in the previous sections can not under any circumstances involve an alteration or loss of the rank of the registered mortgage except when they involve an increase in the amount of the mortgage liability or the extension of the term of the loan for this increase or extension. In these cases there must be acceptance by the owners of the previously registered rights, in accordance with the current mortgage regulations, in order to maintain the rank. In both cases, they will be recorded in the Register by a note in the margin of the mortgage object of the modifying novation. Under no circumstances will this be possible when there is a request in the register for information about the amount pending in execution of subsequent charges.»

## **FIRST ADDITIONAL REGULATION. Regulation relating to the reverse mortgage**

1. For the purposes of this Law, reverse mortgage is held as the loan or credit guaranteed by mortgage over a real estate asset which is the applicant's habitual abode and provided that they comply with the following requirements:

a) that the applicant and the beneficiaries that the former may designate are persons who are 65 years old or older or affected by severe long-term care or great long-term care,

b) that the debtor disposes of the amount of the loan or credit through periodical or single disposals,

c) that the debt is only demandable by the creditor and the guarantee enforceable when the borrower dies or, if thus stipulated in the contract, when the last of the beneficiaries dies,

d) that the mortgaged property has been valued and insured against damage in accordance with the terms and requirements established in articles 7 and 8 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market.

2. The mortgages referred to in this regulation can only be granted by the credit institutions and by the insurance companies authorised to operate in Spain, without prejudice to the limits, requirements or conditions that the sector regulations impose on the insurance companies.

3. The reverse mortgage transparency and marketing regime shall be established by the Minister for Finance and Treasury.

4. Within the framework of the clients transparency and protection regime, the entities established in section 2 which grant reverse mortgages must provide the applicant of this product with independent advice services, taking into account the applicant's financial situation and the economic risks arising from subscribing this product. Said independent advice must be performed through the mechanisms determined by the Minister for Finance and the Treasury. The Minister for Finance and the Treasury shall establish the conditions, form and requirements for the performance of these advisory functions.

5. On death of the mortgage debtor or if thus stated in the contract, on death of the last of the beneficiaries, the heirs can cancel the loan in the stipulated period, paying the mortgage creditor all of the due debt, with its interest, without the creditor being entitled to demand any compensation at all for the cancellation.

In the event that the mortgaged asset has been voluntarily transferred by the mortgage debtor, the creditor can declare the early termination of the guaranteed loan or credit, unless the guarantee is substituted sufficiently.

6. When the loan or credit regulated by this regulation is cancelled and the heirs of the mortgage debtor decide to not repay the due debts, with their interests, the creditor can only obtain recovery up to the amount of the inherited assets. For these purposes that stated in paragraph two of article 114 of the Mortgage Law shall not be applied.

7. The public deeds documenting constitution, subrogation, modifying novation and cancellation will be exempt from the gradual mode of "*Actos Jurídicos Documentados*" or stamp duty on notarial documents.

8. In order to calculate the notary fees for the constitution, subrogation, modifying novation and cancellation deeds, the tariffs will be applied corresponding to the «Documents without quantum» envisaged in number 1 of Royal Decree 1426/1989, of 17<sup>th</sup> November, which passes the notary tariffs.

9. In order to calculate the register fees for the constitution, subrogation, modifying novation and cancellation deeds, the tariffs will be applied corresponding to number 2, «Entries», in appendix I of Royal Decree 1427/1989, of 17<sup>th</sup> November, which passes the registrar's tariffs, taking as a base the amount of the capital pending repayment, reduced by 90 percent.

10. Likewise, reverse mortgages may be constituted against any other properties, other than the usual home of the applicant. The previous paragraphs of the provision herein shall not apply to these reverse mortgages.

11. For everything not envisaged in this regulation and the rules that develop it, the reverse mortgage will be governed by that set out in the applicable legislation in each case.

#### **SECOND ADDITIONAL REGULATION. Regulation relating to long-term care insurance.**

1. Long-term care cover can be instrumented either through an insurance contract signed with insurance companies, including the mutual social welfare companies, or through a pension plan.

2. The long-term care cover performed through an insurance contract binds the insurer, in the event that there becomes a situation of long-term care, in accordance with that set out in the regulations promoting personal autonomy and attention to persons in a situation of long-term care, and within the terms established in the law and in the contract, to comply with the agreed benefit in order to, totally or partially, directly or indirectly, deal with the detrimental consequence for the insured party as a result of said situation.

The long-term care insurance contract can be articulated either through individual or group policies.

If there is no express rule referring to long-term care insurance, the rules regulating insurance contracts and the regulation and supervision of private insurance shall be applied to it.

In accordance with that established in article 6 of the consolidated Private Insurance Regulation and Supervision Law, passed by Legislative Royal Decree 6/2004 of 29<sup>th</sup> October, the insurance companies must have the compulsory administrative authorisation and other requirements necessary in order to provide life or health insurance in Spain.

In order for the mutual social welfare companies to cover the long-term care contingency, which stated in articles 64, 65 and 66 of the consolidated Private Insurance Regulation and Supervision Law, passed by Legislative Royal Decree 6/2004 of 29<sup>th</sup> October, and the rules developing it, shall be applied.

3. The pension plans which envisage the long-term care contingency cover must be expressly stated as such in their specifications. For all not expressly envisaged the consolidated Pension Plans and Funds Regulation Law, passed by Legislative Royal Decree 1/2002, of 29<sup>th</sup> November, and the rules developing it, shall be applied.

#### **THIRD ADDITIONAL REGULATION**

Section 3 of article 693 of the Civil Procedure Law 1/2000, of 7<sup>th</sup> January, is modified as follows:

«3. In the case referred to in the previous section, the creditor can request that, without prejudice to the fact that the enforcement affects the entire debt, the debtor is informed that, up until the day set for the auction, it can release the asset by paying into court the exact amount of the principle and interest due on the date the claim is presented, increased if applicable by the loan's due dates and the delay interest incurred during the proceedings and which are totally or partially unpaid. For these purposes, the creditor can request that the procedure follows that set out in section 2 of article 578.

If the mortgages asset is a family home, the debtor can, even without the creditor's consent, release the asset by paying into court the amounts stated in the previous paragraph.

Once an asset has been released for the first time, it can be release on more occasions provided that at least 5 years have passed between the date of release and the judicial or extrajudicial summons for payment made by the creditor.

If the debtor makes the payment under the conditions set out in the previous sections, the costs shall be liquidated and once they are paid the court will pass judgment declaring the proceedings over. The same will be agreed when the payment is made by a third party with the executor's consent.»

#### **FOURTH ADDITIONAL REGULATION. Assurance of future incomes by the constitution of a reverse mortgage.**

The periodic disposals that the beneficiary may obtain as a result of the constitution of a reverse mortgage can be totally or partially used to contract a secure income plan, under the terms and conditions set out in section 3 of article 51 of the Personal Income Tax Law and the partial modification of the laws on Corporate Tax, Non-Residents Income Tax and Net Worth Tax. For these purposes, the survival of the holder after ten years have passed since the payment of the first premium of the said secure income plan will be the same as the retirement contingency set out in letter b) of section 3 of article 51 of said Law 35/2006.

The mathematical provision of the secure income plan can not be moved to another welfare instrument, and neither can the consolidated rights or the mathematical provision of other welfare systems be moved to it.

(.....)

#### **SOLE TRANSITIONAL REGULATION. Transitional Regimes.**

1. Until the subsequent regulation referred to in section one of article 17 of Law 2/1981, of 25<sup>th</sup> March, Regulating the Mortgage Market is developed, the entities can not issue mortgage bonds for over 90 percent of the non-repaid capital of the affected credits.
2. Until the subsequent regulation referred to in section two of article 9 of this Law is developed, the reference interest rate to be used in order to calculate whether there is a capital gain for the purposes of said section, regardless of the remaining term of the mortgage loan or credit, shall be the internal yield rate in force in the public debt secondary market with residual maturity of between 2 and 6 years, regulated by Decision of the General Treasury and Finance Policy Department of 5<sup>th</sup> December 1989.
3. Any capital increase, without alteration or subordination of the rank of the registered mortgage, according to article 13, section 2 of the Law hereof, amending article 4, Law 2/1994, of 30<sup>th</sup> March on subrogation and modification of mortgage loans, shall only apply to those mortgages constituted after the present Law comes in force.

#### **DEROGATORY REGULATION**

On this Law's entry into force the following are derogated:

- a) The tenth additional regulation of Law 3/1994, of 14<sup>th</sup> April, which adapts the Spanish legislation on credit institutions to the Second Directive on banking coordination and introduces other modifications relating to the financial system;

b) The second paragraph of article 9 of Law 2/1994, of 30<sup>th</sup> March, on subrogation and modification of mortgage loans.

Also, all regulations of the same or lower level which go against that stated in this Law are derogated.

**FIRST FINAL REGULATION. Modification of Law 3/1994, of 14<sup>th</sup> April, which adapts the Spanish legislation on credit institutions to the Second Directive on banking coordination.**

Paragraph three of section two of the fifth additional regulation of Law 3/1994, of 14<sup>th</sup> April, which adapts the Spanish legislation on credit institutions to the Second Directive on banking coordination, is redrafted as follows:

«The institutions referred to in article 2 of Law 2/1981 of 25<sup>th</sup> March, Regulating the Mortgage Market, can make third parties participate in all or part of one or various mortgage loans or credits in their portfolio, even though these loans or credits do not fulfil the requirements established in Section 2 of said Law. These securities, called "mortgage transfer certificates" (*Certificados de transmisión hipotecaria*) can be issued amongst qualified investors or be grouped in asset securitization funds. The regulations established for mortgage participation in Law 2/1981, of 25<sup>th</sup> March, shall be applicable to these certificates, except as set out in this section.»

**SECOND FINAL REGULATION. Modification in the Consolidated Private Insurance Regulation and Supervision, passed by Royal Decree 6/2004, of 29<sup>th</sup> October.**

The following articles from the Consolidated Private Insurance Regulation and Supervision, passed by Royal Decree 6/2004, of 29<sup>th</sup> October, are modified as follows:

One. Section 2 of article 6.1.a) becomes drafted as follows:

«2. Illness (covering health assistance and long-term care).

The provisions in this branch can be in a lump sum, reparation and a mixture of both.»

Two. Section a) of article 6.2.A becomes drafted as follows:

«a) The life insurance, both for death and for survival, or both together, included in the survival annuity insurance; the life insurance with reinsurance; the "marital status" insurance, and the "birth" insurance. It also covers any of this insurance when they are linked with investment funds. It can also cover long-term care insurance.»

Three. Section d) of article 6.2.B becomes drafted as follows:

«d) When the complementary area is illness, it does not cover health care benefits or long-term care benefits.»

Four. The first paragraph of article 65.1 is modified and becomes drafted as follows:

«In personal risk provision, the contingencies that can be covered are death, widowhood, orphanage, retirement, and long-term care and they will guarantee economic benefits in the form of capital or income. They can also benefits for marriage, motherhood, children and death. And they can perform insurance operations for accidents and disability to work, legal defence and assistance, and provide family benefits to subsidy requirements due to legal facts or acts which temporarily prevent performance of the professional activity.»

**THIRD FINAL REGULATION. Modification of the Chattels Mortgage and Non-Transferable Collateral Law, of 16<sup>th</sup> December 1954.**

1. Article 2 of the Chattel Mortgage and Non-Transferable Collateral Law, of 16<sup>th</sup> December 1954, is modified and shall become drafted as follows:

«1 (new). The agreement not to re-mortgage or re-pledge already mortgaged or pledged assets shall lack effect, and as such chattel mortgage and non-transferable collateral can be constituted over assets already mortgaged or pledged, albeit with an agreement not to re-mortgage or re-pledge.

Chattel mortgage or non-transferable collateral can also be constituted over the same mortgage or pledge right and over embargoed assets or whose acquisitions price has not been fully paid out.

This section does not have retroactive effect. »

2. A Paragraph 4 is introduced into article 8 Chattel Mortgage and Non-Transferable Collateral Law, of 16<sup>th</sup> December 1954, as follows:

«The credits guaranteed with chattel mortgage or non-transferable collateral can be used to cover the issues of securities on the secondary market».

3. Paragraphs 2 and 3 are introduced into article 54 of the Chattel Mortgage and Non-Transferable Collateral Law, of 16<sup>th</sup> December 1954, as follows:

«The credits and other rights corresponding to the holders of administrative contract, licences, awards or subsidies can be subject to non-transferable collateral provided that the Law or the corresponding constitution title authorises their transfer to a third party. Once the security is constituted, the Registrar shall on its own accord communicate this circumstance to the competent Public Administration by means of a certification issued for the purpose.

The credit rights, including future credits, provided that they are represented by securities and are not considered as financial instruments for the purposes of that set out in Royal Decree Law 5/2002, of 11<sup>th</sup> March, on urgent reforms to promote productivity and in order to improve public contracting, can also be subject to non-transferable collateral. In order to be properly constituted, they must be entered in the Personal Property Register».

(.....)

**EIGHT FINAL REGULATION. Regulatory Authorisations.**

Without prejudice to the authorisation contained in this Law, in particular relating to those of the Minister for Finance and the Treasury, the Government is authorised to develop, execute and comply with that set out in this Law.

**NINTH FINAL REGULATION. Basic nature and conferring of competence**

1. This is a Law of basic legislation in accordance with that stated in article 149.1.11.<sup>a</sup> and 13.<sup>a</sup> of the Constitution, with the exception of Chapter V which is exclusively pronounced under article 149.1.8.<sup>a</sup>. of the Constitution.

2. Apart from the basic character established in the previous section, Chapters II, III and VI, the First Additional Regulation and the First, Second and Third Final Regulations, are also pronounced in accordance with that set out in article 149.1.6.<sup>a</sup> and 149.1..8.<sup>a</sup> of the Constitution.

**TENTH FINAL REGULATION. Entry into Force.**

This Law will enter into force on the day after it is published in the «Official State Gazette».

***7th December 2007.***