

**TECHNICAL NOTE ON THE JUDGEMENT OF THE COURT OF JUSTICE OF THE EUROPEAN UNION 14 MARCH 2013.**

**LIMITS TO THE GROUNDS OF OPPOSITION IN MORTGAGE ENFORCEMENT PROCEEDINGS AND ASSESMENT OF UNFAIR TERMS IN CONTRACTS IN THE SPANISH MORTGAGE MARKET**

*March 2013*

**I. INTRODUCTION**

On the 14th of March 2013 the Court of Justice of the European Union delivered a judgment on the Spanish mortgage enforcement proceedings, in particular on the limits to the grounds of opposition of a debtor allowed in these proceedings.

Since this judgment has captured media attention, the Spanish Mortgage Association (Asociación Hipotecaria Española) would like to provide a contribution to the debate by assessing not only the judgment itself, but also its actual impact.

The judgment is given as a result of a preliminary ruling proceedings, a procedural mechanism that allows the Court of Justice of the European Union (hereinafter the Court) to determine whether a given national law is contrary to European Union Law. Its unique feature is that the Court intervention is required by a national court (juzgado de lo mercantil No 3 de Barcelona –Commercial Court No 3, Barcelona) before which the case was brought, who considers that the applicable national law is not compatible with the European Union Law.

Although the preliminary ruling does not decide the national dispute itself since the case has to be disposed by the national court, the answer of the Court is binding not only on the national court but on all courts before which a similar issue is raised. Furthermore, the Court's consideration that a national legislation is contrary to the European Union Law requires national public authorities (legislative and executive) to change the legislation in order to remove such a contradiction between national and EU Law, by virtue of the prevalence of the latter.

The judgment answers **two different preliminary ruling questions**, with different scopes and thus, with very different consequences. For both questions, the reference EU legislation upon which the decision is based is Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts.

The two questions raised by the national court are the following:

a) To determine whether the solution contained in Arts. 695 and 698 of the Spanish Code of Civil Procedure (Ley de Enjuiciamiento Civil – LEC) is compatible with the European Union Law. Under these provisions, the court hearing the declaratory proceedings seeking that a term is unfair is not allowed to adopt as interim measures the staying of the enforcement proceedings and it is not possible to invoke as grounds of opposition within the mortgage enforcement proceedings that said term is unfair.

b) To examine the unfairness of certain contractual terms in mortgage credit agreements brought before the national court, especially those referred to

- 1) Unilateral quantification of the unpaid debt by the bank, which will prevent the debtor from being heard in this proceeding.
- 2) Setting the default interest rate in 18.75%, regarded as unfair because it is excessive.
- 3) Possibility of accelerating the loan and calling in the totally of the loan in the event of a **single** default, regarded as disproportionate.

## **II. INCOMPATIBILITY BETWEEN NATIONAL PROCEDURAL RULES WHICH LIMIT THE GROUNDS UPON WHICH A DEBTOR MAY OBJECT TO MORTGAGE ENFORCEMENT PROCEEDINGS AND THE COUNCIL DIRECTIVE ON UNFAIR TERMS**

The judgment is very clear in this regard. The national procedural rules of the Spanish Code of Civil Procedure, under which it is not possible to **simultaneously**:

- a) Invoke the unfairness of a term of the loan agreement in mortgage enforcement proceedings,
- b) Stay the enforcement proceedings as an interim measure adopted by the court hearing a declaratory procedure seeking to determine whether a clause is unfair

infringe European Union legislation and, in particular, the Council Directive on unfair terms in consumer contracts.

The judgment refers to the “principle of effectiveness”, a very relevant principle when interpreting European Union Law, which in short means that although Member States are autonomous to implement mechanisms for enforcement at their discretion, the legislation “must not make it in practice impossible or excessively difficult to exercise the rights conferred on consumers by EU law” (basically the Directive on unfair terms in consumer contracts).

According to the Court, the final vesting of the immovable property in a third party is, in principle, irreversible and the compensation that the consumer may obtain after the declaratory proceedings if the term in question is deemed unfair is insufficient. In contrast with several decisions made by the Spanish Constitutional Court (the last Decision 113/2011 of 19<sup>th</sup> July) defending the suitability of the Spanish mortgage enforcement system as “those questions could be widely assessed” “subsequently” in the declaratory proceedings, the Court considers ineffective such “subsequent” protection, purely compensatory, of the declaratory judgment when the family home is at stake.

The judgment is clear and these are the effects it will cause regarding the first preliminary ruling question:

- With regard to Courts, and until a new legal framework is available, on the one hand it should be accepted as grounds of opposition in mortgage foreclosure proceedings the hypothetical unfairness of a term (even ex officio) and, on the other hand, courts hearing declaratory proceedings involving

these terms may stay the enforcement proceedings. **The implementation of the abovementioned may not be always easy and hence the urgency of finding a legal solution.**

- With regard to legislation, it is obvious that an amendment of the Spanish Code of Civil Procedure is needed, but it is important to note that the judgment does not obliges to adopt the double measure of –on the one hand- allow the court hearing a declaratory proceedings assessing the unfairness of the term in question to stay the enforcement proceedings and –on the other hand- also to introduce in the enforcement proceedings as a new ground for opposition the unfairness of a term. It is sufficient to implement one of both measures. **From our point of view, the preferable option is the second one, taking the opportunity to regulate the incident provided for by Art. 695 of the Spanish Code of Civil Procedure** (that lists the present grounds upon which a debtor may object to mortgage enforcement proceedings) and seeking to eliminate the legal uncertainty as soon as possible. **By introducing this legal amendment, the debtor is endowed with a greater and efficient protection mechanism, in line with the judgment, without prejudice to the efficiency and responsiveness that unpaid mortgage debt collection management demands.**

### **III. PRELIMINARY RULING ON THE UNFAIRNESS OF THE THREE SPECIFIC TERMS IN QUESTION: DEFAULT INTEREST CLAUSE, ACCELERATION CLAUSE AND CLAUSE ON UNILATERAL QUANTIFICATION OF THE UNPAID DEBT.**

The scope of the judgment regarding this second preliminary ruling question is very different. **The Court makes no ruling on whether individual terms of the loan agreement are unfair**, but sets out criteria in the light of the Directive that shall be taken into account by the national court to assess those terms.

Firstly, the judgment interprets in very general terms the concepts of “significant imbalance” in the parties’ rights and obligations and of “requirement of good faith” as referred to in Article 3 of the Directive on unfair terms in consumer contracts.

Apart from these general considerations, the Court refers separately to the terms in question, although in a brief manner. The judgment outlines that the assessment of the hypothetical unfairness of the term made by the national court must be made taking into consideration the rules applicable under national law. It is worth noting in this regard that the judgment 792/2009, of 16<sup>th</sup> December of the Spanish Supreme Court (which contains case law established by previous rulings) ruled on the fairness of the clause on unilateral quantification of the unpaid debt (FD IV) and the acceleration clause (FD X), case law and doctrine that have not been questioned by the judgment of the Court which, has mentioned above, merely establishes very general criteria. In the light of the abovementioned considerations we believe that:

- The Spanish Supreme Court has clearly determined that the acceleration term is valid, since the failure to meet a due payment constitutes the non-compliance with an essential obligation of the contract. In any case, it seems that in Parliament –in the discussion of the draft of the *Royal Decree Law 6/2012 on urgent measures to protect low income mortgage debtors*- it is going to be required more than one single default to start enforcement proceedings.

- As regards to the default interest term, references made by the judgment to the statutory interest rate and other Law (i.e. Consumer) raise some doubts as to the unfairness of the agreed default interest of 18.75%. In any case, this issue shall also be resolved in Parliament, setting a limit to default interest rates for mortgages on main residence.
- Finally, we consider that the term on unilateral quantification of the unpaid debt by the lender does not make “difficult for the consumer to take legal action and exercise rights of the defense”. This has been stated by the Court as the only general caution and it was declared fully admissible by the Spanish Supreme Court.

#### **IV. FINAL COMMENTS**

Taking into consideration the abovementioned, the Spanish Mortgage Association shares the general assessment of the judgment as a step forward in the protection of the consumer in mortgage enforcement proceedings. However we would like to make some comments:

- We insist on finding **an urgent legal solution** in order to avoid regulatory gaps and/or premature and contradictory court decisions.
- The judgment does not assess at all whether the terms of a loan are unfair.
- In any case, it has a limited scope. Our mortgage subscription, registration and enforcement proceedings provide safety and confidence to our system.
- And, finally, we would like to highlight the importance of continuing paying when due. This is one of the maximum strengths of our market, as acknowledged by investors in Spanish covered bonds and, to this extent, it is important to avoid misinterpretations and even confusions regarding the scope of the judgment.