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Review

Spanish Real Estate Legal Update

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PARTIAL REFORM OF THE CAPITAL COMPANIES ACT.

The recent Act 25/2011, of 1st August, introducing the Directive 2007/36/EC of the European Parliament and of the Council, on the exercise of certain rights of shareholders in listed companies, that came into force on the 2nd October in partial reform of the Capital Companies Act 1/2010, of 2nd July.

The objectives of the new Act are: i) To reduce costs in the organisation and functioning of Capital Companies; ii) To bring corporation law up to date with practical requirements; iii) To do away with certain differences existing between the system regulating Stock Limited Companies ("SA Companies") and Limited Liability Companies; iv) To transpose Directive 2007/36/EC of the European Parliament and of the Council, of 11th July, on the exercise of certain rights of shareholders in listed companies into domestic legislation.

Amongst the reforms introduced by this Act, the following are worthy of mention:

The possibility of creating a corporative web-site, following a resolution taken in the General Meeting, and registering it in the Commercial Registry unless the notification is sent individually to all of the members. The Directors are responsible for checking the accuracy of what is inserted in the content of the web and of the date on which the insertions are made.

Regarding the objective of reducing costs, the law, in certain cases, eliminates the obligation of placing announcements in the press. Specifically, it unifies the method of sending official notice of the General Meeting for both SA Companies and Limited Liability Companies ("SL Companies"), allowing both to make provision in their articles of association for the possibility of sending notice of a general meeting by way of an announcement published on the company's web-site or by any other means of individual, written communication, providing that there is guarantee of being received by all members. In this way the obligation is eliminated of publishing the official notice in the Official Gazette of the Commercial Registry and in one of the major daily newspapers in the province where the registered address is situated, with the only two exceptions being if the shares issued are bearer shares or if it is a listed company.

It is removed the legal requirement that any resolution taken by SA Companies which are intended to modify the company name, address or any other change that modifies the corporate object, have to be published in two major newspapers in the respective province where it is located, as an essential requisite for being registered into the Commercial Registry. It is also removed the legal requirement that the dissolution of a SA Company has to be published in one of the major newspapers in the municipality where it has its registered address, and also the obligation of publishing the annual statement of accounts in the Official Gazette of the Commercial Registry during the period of liquidation of the SA Company.

The Act makes it possible for SA Companies to establish in their By-Laws two or more forms of organising the company management, meaning that the company can choose one or other without the need of having to make any modification to its By-Laws.

With specific requirements, it incorporates the right of withdrawal of the members in the event of no distribution of dividends. Once five financial years have elapsed since the company's registration in the Commercial Registry, any member that had voted in favour of the distribution of company profits will have the right to withdraw from the company if the Shareholders General Meeting does not agree on "*the distribution of dividends equivalent to at least one third of own operating profits during the previous financial year that are legally distributable"*.

Regarding annual accounts, the following measures are established for reducing costs. The first one being the removal of the requirement of having notarial legalisation of the signatures of the Directors, and the second consisting of eliminating the requirement of publishing an announcement in the Official Gazette of the Commercial Registry stating the companies that have complied with the obligation of filing their annual accounts. The last one being the possibility of having online access to the Commercial Registry replaces the function that had been performed by publishing the lists of companies which had filed their annual accounts.

In turn, the regulation also eliminates the requirement that the immovable assets of a SA Company have to be sold in public auction when the company is being liquidated.

With regard to adapting the Capital Companies Act to practical requirements, special mention is made of how the law works in regulating the legal status of a director who is a legal entity. It creates the necessity of designating an individual in representation of the director that is a legal entity, who will permanently perform the functions inherent to its office, whilst at the same time emphasising the joint and several liability of the legal entity represented and its representative.

Along the same lines it establishes that the Directors representing at least one third of the components of the Board of Directors have the power to call a Board Meeting if the Chairman does not call it.

The Act has equated the system governing SL Companies and SA Companies, unifying the content of certain provisions. It occurs with the official notice of general meetings, with the possibility of introducing the grounds for excluding shareholders into the By-Laws of the company, and this is contained in article 351 which establishes that "*In Capital Companies, with the consent of all of the members, the By-Laws may include certain legal grounds for the exclusion of shareholders, as well as the amendment or suppression of the already existing causes*"; with the unification of the legal causes for dissolution, and the cause relating to inactivity being applied to all Capital Companies; with the generalisation of the additional rule by which the Directors of the company automatically become its liquidators; and with the unification of the legal regulations governing the liquidators of a company that has been wound up.

With regard to the official notice for General Meetings, the following changes can be highlighted: i) if members representing a minimum of 5% of the share capital request the Management Body to call a meeting, it must be held within 2 months, ii) similarly the advance notice of the holding of the meeting is increased from 8 to 10 days in second call if it was unable to be held in the first call and no provision had been made for holding the meeting in a second call. This second call must be announced with the same agenda and the same requisites for publishing it as for the first call, within the 15 days following the date of the meeting that was not held with and at least, 10 days advance notice of the date set for the meeting. All official notices of a meeting must state the office held by the person that has called it.

THE REFORM OF THE BANKRUPTCY ACT IN THE REAL-ESTATE SECTOR.

The current economic recession has been particularly acute in one of the pillars of the national economy, the construction and real-estate sector. This sector, which had already been undergoing a slowdown in recent years following the so-called "real-estate boom", now stands in a profound and particular crisis with sales coming to a standstill, caused not only by the overall market situation, but mainly due to the restrictions placed by banks on loans, which are putting an economic brake on entrepreneurs.

Entrepreneurs in the real-estate sector find themselves in a situation in which the requirements have become stricter for loans being granted to developers, by subjecting the approval to a percentage of sales, which on occasions is more than 50% of the promotion. If we add to this the increased cost of mortgages and the fact that they are only given to individuals with proven solvency, it is making it impossible for even the most experienced entrepreneurs, in the current circumstances, to achieve the sales level required for the developer's loan to be granted.

For all of these reasons, it should be highlighted that the majority of the bankruptcy proceedings are being instigated by entrepreneurs in the real-estate sector, with 31.7% of all bankrupt companies having construction or real-estate sales as their main activity, according to data from the National Institute of Statistics, and to date, the majority of bankruptcy cases that are processed end up with the liquidation of the company and the end of the business or professional activity of the debtor.

The Bankruptcy Act 38/2011 of 10th October, in amendment of Act 22/2003 of 9th July, could imply, as indicated in the Preamble to the Act, "*an entire updating of our legislation on bankruptcy in the light of the short but intense experience and application of the 2003 Act*". This Act will come into force on the 1st January 2012, except for the following provisions: 5.bis, *Communication of negotiations and consequences of the obligation of filing a petition for bankruptcy*; 15, *Provision for the petition of another party with legal standing and accumulation of petitions*; 71.6 and 71.7, *Reinstatement Actions*; 84.2.11, Insolvency claims and claims againts the estate; 91. 6º, *Claims with general preference*; and the Fourth Adtional Provision, which will all come into force on the day following the publication of Act 38/2011 of 10th October, in the Official State Gazette.

Amongst the reforms introduced by this Act, we would highlight those relating to the so-called pre-bankruptcy institutions, offering the debtor a faster, more economic alternative through refinancing agreements.

In relation to declaring its insolvency, the regulation enables the debtor to inform the Court that it has entered into negotiations to reach a refinancing agreement *or* to obtain acceptances for an early proposal of the composition; taking into consideration the claims against the estate (claims arising after declaring insolvency), 50% of the claims that entail fresh income and have been given under the framework of a refinancing agreement, and the remaining amount being considered as preferential claims. If three months elapse since the court is informed and has not been possible to reach a refinancing agreement or to obtain the acceptances necessary for an early proposal of the composition, the debtor must apply for the declaration of the bankruptcy within the next business month, unless it is not then in a state of insolvency. This reform has been made by the introduction of article 5 bis. into the Bankruptcy Act.

In turn, article 71 of the Bankruptcy Act has been modified, regulating the cancellation of any acts carried out by the debtor that are considered to be detrimental to the estate, and establishing that "*Refinancing agreements reached by the debtor may not be cancelled, nor any business, dealings or payments*, *(…), if, as a result, they bring about, at least, a significant increase in the credit available or the modification of its obligations (…), providing that they are part of a viability plan that permits the professional or business activity to continue in the short and medium term",* all of this with the proviso that before the declaration of insolvency, certain requisites have been met.

The most noteworthy aspect of the refinancing agreements is that, once the law has come into force, the agreements will be judicially comparable providing that they are signed by creditors representing at least 75% of the debt held by the financing institutions at the time of adopting the agreement and that, within certain limits, those agreements will be extended to the creditors in dissent.

Also, the conditions for becoming a bankruptcy administrator are tightened up, with the requirement that, in addition to a professional career such as lawyer or economist with at least 5 years experience, specialised preparation must be demonstrated in bankruptcy law, including the possibility that a legal entity may be appointed as a bankruptcy administrator.

Under the causes for concluding the bankruptcy proceedings contained in article 176 of the Bankruptcy Act, the reform introduces a new circumstance that can lead to the conclusion of the proceedings, which is the lack of assets to satisfy the claims against the estate.

The reform, in turn, applies to bankruptcy liability, establishing that, once in the liquidation stage, the Judge can "*find all or some of the Directors, liquidators, de iure or de facto, or attorneys with general powers of the body corporate in bankruptcy, if they have been declared persons affected by the classification of bankruptcy, liable for the total or partial cover of the deficit"*, introducing the figure of the attorney with general powers as one of the persons liable in bankruptcy.

Finally, under this reform, the Law on Value Added Tax is modified, the objective being that in the sale or disposal of immovable assets, carried out during both the common phase and the liquidation phase of the proceedings, "*this tax shall be paid by the purchaser, applying the reverse charge mechanism*".

ACT 22/2011, OF 28TH JULY, ON WASTE AND CONTAMINATED SOILS.

Directive 2008/98/EC of the European Parliament and of the Council, dated 19th November 2008, which sets out the legal framework for the prevention and management of waste, has recently been implemented into our domestic legislation through the Waste and Contaminated Soils Act 22/2011, of 28th July.

Act 22/2011, that came into force on 30th July 2011, replaces the previous piece of legislation in force, the Waste Act 10/1998, of 21st April.

The objectives of this new law are to adapt domestic legislation to EC legislation on matters concerning waste, and to bring up to date and improve the legal regulations on the issues of waste production and management, promoting the introduction of measures for the prevention, re-utilisation and recycling of waste.

With regard to the regulation of contaminated soils, under Heading V of the new Act, the current set of regulations are maintained, with certain aspects being qualified in respect of determining the parties responsible for the decontamination of the soil, regulating the obligations of the persons responsible for potentially contaminating activities to provide information and of the owners of the contaminated soils, and the creation of a national inventory of contaminated land.

The modifications introduced under this Act are the following:

Firstly, and regarding the obligation to provide information on the part of the persons responsible for potentially contaminating activities, which are approved and published by the Government, these persons are obliged to regularly inform the corresponding Regional Authorities through reports giving details of the information necessary for the declaration of contaminated land.

In respect of land being delared to be contaminated, at the initiative of the pertinent Regional Authority this fact shall be noted in the margin of the Land Registry entry, and in the terms that are set out in Government regulations. In addition, provision is made that this declaration can entail the suspension of the enforceability of building rights and other uses made of the land in the event that they are incompatible with the measures stipulated for the cleaning and recuperation of the land until they have been carried out or until the land is certified to be uncontaminated.

The Regional Authorities, in charge of drawing up the inventory of land declared to be contaminated, will send the inventory to the Ministry of the Environment and Rural and Marine Affairs within the space of one year from when this act enters into force, and will send updated information each year. In turn, once a piece of land has ceased to be contaminated and this has been certified by the Regional Authority, this certification will be included in the inventory that has been drawn up by them.

For its part, the Ministry of the Environment and Rural and Marine Affairs will draw up a national inventory of contaminated land on the basis of the information that it receives from the Regional Authorities.

Regarding the parties responsible for the decontamination and recuperation of contaminated land, in the case where there are several parties who have caused the contamination, they shall be jointly liable for assuming the obligations, and then the owners of the contaminated soils and the occupants of the land, in this order, shall be subsidiarily liable. In the case of property in the public domain under concession, the occupant and the owner, in this order, shall be subsidiarily liable in the absence of the party causing the contamination.

The persons with subsidiary liability may pass on the cost of the measures taken for recuperating the land that has been declared to be contaminated to the party or parties causing the contamination.

Similarly the recovery of the costs of decontamination may never be demanded in excess of the levels of contamination associated to the use of the land at the time when the contamination was produced by the party causing it.

With regard to the remediation of the land through conventional methods, as a new way of carrying out the actions of cleaning and recuperation, the law adds the use of the contracts provided for in the Public Sector Contracts Act 30/2007, of 30th October. Similarly, the granting of economic incentives to help the financing of the costs for cleaning and recuperation of contaminated soils must take place according to the provisions in legislation for operations of decontamination and recuperation of contaminated soils with public funding.

Lastly, we mention the contribution that this law has made in the aspect of the recuperation of contaminated soils, making it possible to proceed with what is known as “voluntary recuperation of the soil” for the decontamination of the land, without it previously being declared to be contaminated by the Regional Authorities, all of this through a project of voluntary recuperation to be approved by the compentent body of the Regional Authority. Once the project is completed, a certificate will be given saying that the decontamination has been carried out according to the project. The competent authority will keep an administrative register of the decontamination action that is carried out voluntarily.

REGARDING THE LATEST COURT DECISIONS IN RELATION TO THE “FLOOR LIMIT CLAUSES” IN MORTGAGE CONTRACTS.

In the past months there have been several court rulings that have brought the famous floor limit clauses into the line of fire, i.e. the clauses that set a minimum limit on the variable interest rates in loan contracts with mortgage guarantee.

The ruling of the Commercial Court No. 2 of Seville, on 30th September 2010, was the first that held the clause to be unfair, as it prevents interest from going lower than a minimum limit, either directly or indirectly, depending on the different types set out in the mortgage contracts that are the subject of the claim filed by a well-known consumers association.

In that ruling the judge established that both the mentioned floor limit clause and the ceiling limit are not mere interest conditions, but added clauses that do not involve free negotiation between the parties, and are imposed as a normal practice, and that as these are general contracting conditions, they can be considered to be unfair.

As a result of the above, the mentioned ruling says the clauses contained in the mortgage contracts only provide “cover that markedly and freely covers the risk of one party to the transaction, the Bank, and do not cover in the same way the risk of the borrower, therefore they have to be considered null and void due to unfairness”.

As in the preceding case, the ruling given by the Commercial Court No. 1 of León, centres the reason for the unfair nature of the floor limit clause on the underlying disproportion between the minimum limit (floor) and the maximum limit (ceiling) established by the defendant banks in the variable interest rates. So, while the downward rates are maintained at a reasonable threshold taking into account the historic Euribor (taken as a reference rate), the upward rates are set at thresholds that will be very difficult, if not impossible, for the mentioned reference rate to reach.

As a consequence of the above, both rulings highlight the fact that the unfairness of the floor limit clause depends on the proportionality between this and the ceiling limit, so that there is reciprocity and this covers the mortgage holder against the upward trend of the Euribor.

The mentioned court rulings make it clear that the incorporation of a clause of this kind comes as a complete surprise for the holder of a mortgage loan regarding the cost of the loan that he thought he was taking out at the beginning, to the extent that it could be contrary to good faith on the part of the defendant banks, apart from the possible lack of transparency having a bearing on the situation, and all of this because, according to the judges, the possible fraud arises from the information or the lack of information provided by the lending banks.

As opposed to the two rulings commented so far, the Commercial Court No. 9 of Madrid considered over twenty clauses forming part of the collective complain filed by the Consumers Association (OCU) against the two banks, to be in compliance with the law.

In this respect, the Judge did not hold that this kind of clause is to the exclusive benefit of the bank, which in the case of the first bank, imposed a floor limit of 2.25 per cent and a ceiling limit of 15 per cent, whilst in the case of the second bank, it only included a floor limit clause of 4.5 per cent. He considered that in these cases the clients were benefited because the limit was below market rates (set at 6 per cent) and held that they do not affect the reciprocity of the negotiation between the parties.

Given the uncertainty that is generated as a result of the contradiction between the court rulings cited, we need to keep abreast of future case-law and the effects that this could have on the holders of mortgage contracts that include the floor limit clauses mentioned.

RESOLUTIONS OF THE GENERAL DIRECTORATE FOR OFFICIAL REGISTERS AND NOTARIES AND RECENT CASE-LAW.

Provincial High Court of Girona. Division Two. Ruling No. 119/2011 of 16th September 2011.

With the Ruling given on 16th September the Provincial High Court upheld that the surrender of the mortgaged property pays off the mortgage debt assumed by the borrower with the lender. The circumstances surrounding this appeal are those of a family who were evicted from their house and, in spite of this, the bank continued claiming the debt from them as being the difference between the outstanding amount of the mortgage and the amount for which the bank had been awarded the property in auction. The Ruling upholds the appeal lodged by the appellant against the decision of the Court of First Instance, invalidating the foreclosure issued by the Court of First Instance, cancelling the attachments and other measures of guarantee that had been approved originally.

This Ruling rekindles the legal debate that was left open in this respect by the Provincial High Court of Navarra in its Ruling No. 111/2010 of 17th December, making it possible, through case-law, for the exception provided for in article 140 of the Mortgage Act, which permits the parties to agree that the guaranteed debt shall only be enforced on the mortgaged properties, without the debtor's liability extending to the rest of his assets, to become the general rule.

In the case in question, the Court of First Instance did not uphold the arguments of the appellant pursuant to the provisions of article 579 of the Law on Civil Procedure. This rule entitles the bank to proceed with the foreclosure if "once the auction of the mortgaged or pledged property has taken place, the product from the auction should be insufficient to cover the debt".

The Provincial High Court disagrees with the legal reasoning given in the First Instance on the basis of the following grounds: In the first place it holds that it cannot be considered that the "product" obtained by the lending bank as a result of the foreclosure on the property is insufficient to cover the debt because what the bank obtains is not the amount raised in the auction (which in the event of being settled is half the value of the property), but the value corresponding to the mortgaged property and that was established in the deed that granted the mortgage loan. This argument is backed up by "the doctrine of estoppel", sustaining that the bank, the strong party in the standard contract that it signs with the borrower, is who had the property valued at a certain figure, and therefore, it cannot at a later date, take possession of the auctioned property without giving the value that the bank itself had established in the mortgage deed.

It also says that article 579 of the Law on Civil Procedure cannot be interpreted without taking into account the provisions of the Leg. RD. 1/2007, of 16th November, approving the revised text of the general law for the defence of consumers and users. In this respect it recalls that unfair terms are those that "*without being negotiated individually or specifically accepted, give rise to a serious imbalance for the consumer or user in the rights and obligations assumed contractually by the parties*", and also those that impose a disproportionally high indemnity on the consumer or user, which is what the Provincial High Court holds has happened with the subject of the appeal.

At the same time it holds the opinion that the bank has committed an abuse of law and that its action constitutes an anti-social exercise in so much as, through its interpretation of article 579 of the Law on Civil Procedure, it is attempting to profit from an unjustified benefit that the rule does not seek to safeguard, because, as included in the legal arguments: "*after having recovered the amount owed, it could, with no just cause, obtain other amounts to which it would not be entitled and for which it would be seeking safeguard through a rigid interpretation of the law in question*".

Finally, the Provincial High Court bases its decision on a line of reasoning that it considers "*consistent with the material justice of the case",* recalling that in the *"interpretation and application of the laws, the courts must seek the solution which, without contravening them, is the most consistent with a fair decision, which is what the citizen, ultimately, expects from a "court of justice"*.

We make mention of the dissenting vote of one of the Judges who disagreed with the decision taken in that Ruling, and felt that the appeal filed by the appellant should have been dismissed.

In this respect, the Judge based his decision on the Supreme Court Ruling of 25th September 2008, which set out that "*there is no unjust enrichment of the creditor who been awarded the property if the price for which it was awarded was less than the valuation figure. It is evident, and this has always been acknowledged by this Court, that there is no unjust enrichment for those who act in accordance with the law*". At the same time it holds that the creditor did not act in abuse of law by collecting from the debtor and his guarantors the outstanding amount of the debt for which it foreclosed, if in the mortgage foreclosure procedure it did not obtain sufficient funds to completely satisfy the debt, all of which providing that there was no limited liability clause in the mortgage that limits the liability of the debtor to the amount of the properties mortgaged.

Against the Court's ruling, the Judge considered that the full liability of the debtors is supported by articles 1.911 of the Civil Code ("To comply with his obligations the debtor is answerable with all his present and future assets") and 105 of the Mortgage Act ("The mortgage can be set up in guarantee of any kind of obligation and shall not alter the personal unlimited liability of the debtor that is established in article 1.911 of the Civil Code") whereby it also cannot be considered unfair in respect of the legislation for the protection of consumers and users.

Ruling 14th July 2011, of the General Directorate of Official Registers and Notaries

In this Ruling given by the General Directorate of Official Registers and Notaries (referred to as, "GDRN"), the appellant, after presenting in the Land Register a certified copy of a final judgment which invalidated certain entries made on a number of properties, and an order for their corresponding cancellation, the Registrar refused to cancel the entries for two of the properties, as they were registered in a different name from that of the defendant, since the latter had sold the two properties in question to a third party.

The appellant argues in his appeal, based on article 33 of the Mortgage Act, that the transfer of the properties took place subsequent to the judgment, and that the invalidation can never be validated.

This article sets out that "Registration does not validate documents or contracts that are invalid according to law".

In relation to the above, we have to differentiate the content of the article cited from that of the immediately following article, i.e. article 34 of the Mortgage Act, which provides that "The good faith third party who, for valuable consideration, acquires a right from a person who appears in the Register as having the power to transfer it, shall have his acquisition maintained, once his right has been registered, even if subsequently the right of the transferor is invalidated or cancelled pursuant to causes that are not recorded in the same Register".

In effect, in addition to the fact of this latter article not being an exception of No. 33, the GDRN established that the invalidation of an act cannot affect a god faith third party buyer if the cause of that invalidation does not arise from the Register itself.

Similarly, the GDRN reminds us of the existence of a cautionary registration of claim, which the appellant could have made use of and did not. In this respect, during the time elapsed since the filing of the claim and the registration of the order for the cancellation of the act of transfer of the property, the appellant could have applied to the Judge precisely to have a cautionary registration made to the effect that the properties in question were involved in a lawsuit, so that any person who was to acquire a right from the defendant registered owner could see a record of the existence of that lawsuit.

On the basis of all of the above, the GDRN ruled to dismiss the claims of the appellant, as there was no unfairness, due to the simple fact of not having exercised all the legal mechanisms established for the purpose, and which in this case, consisted of applying to the pertinent judge for a cautionary registration of claim.

FOR FURTHER INFORMATION

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