The Real Estate Law Review

Editor
David Waterfield

Law Business Research

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The Real Estate Law Review

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EDITOR'S PREFACE

In an age that has seen ownership of real estate become increasingly international, it is more necessary than ever to appreciate the basic framework of real estate law in different jurisdictions. This book aims to give readers a general feel and overview of some of the key substantive and practical considerations in the major markets around the world.

Each contributor to *The Real Estate Law Review* is a distinguished legal practitioner in his or her own jurisdiction, and this review represents an immediate and accessible summary of the most important and relevant issues across the many countries covered.

The Real Estate Law Review seeks to identify distinctions in practice between the different jurisdictions by focusing on key developments that highlight particular local issues – we believe that this will help practitioners to develop their understanding of practice beyond their own borders. As both domestic and international clients become ever more sophisticated in this regard, real estate practitioners need to be familiar with the issues in the markets that are most relevant to the interests of their clients. Overseas investors have for some time been key influences in most jurisdictions and it is therefore vital that practitioners are able to advise on a particular transaction in the light of an understanding of the investor's own home forum.

In addition to bringing together topical cross-border real estate issues and practical information on real estate practice around the world, *The Real Estate Law Review* also seeks to offer an overview of activity levels in each jurisdiction and, therefore, the global real estate investment market. The impact of events such as the collapse of the US sub-prime residential mortgage market and the Eurozone crisis has demonstrated how complex and inter-related investment markets have become. It is no longer possible to ignore globalisation and view real estate markets in isolation. The financial and economic turmoil of the past few years will continue to affect the international real estate investment market; the scarcity of debt finance seems likely to continue for the foreseeable future and investors with funds will increasingly look to a global real estate market for value and safety.

I wish to express my deep and sincere thanks to all my distinguished colleagues who have contributed to this first edition of *The Real Estate Law Review*. I would also like to thank Gideon Roberton and his publishing team for their tireless work in coordinating the contributions from the various countries around the world.

David Waterfield
Slaughter and May
London
February 2012

Chapter 29

SPAIN

Diego Armero and Rodrigo Peruyero[1]

I INTRODUCTION TO THE LEGAL FRAMEWORK

i Ownership of real estate

The most common type of ownership in Spain is absolute property. It is similar to the Anglo-Saxon concept of 'freehold' and grants the title holder absolute rights to transfer, use and encumber real estate.

Spanish law recognises, however, other types of ownership or real estate rights that can be used or considered when exploring investments in commercial real estate. These are as follows:

a Surface rights: These types of rights are similar to Anglo-Saxon 'ground leases' and temporally separate land ownership from that of the construction to be built over it. It grants the 'tenant' the right to build and own a construction over third-party land in exchange for consideration and for a limited period of time (up to a maximum of 99 years) after which ownership of the construction reverts back to the land owner. Surface rights are sometimes used by renewal energy companies to set up their solar and wind farms as it allows the beneficiary of the surface right to reduce the project cost (for not having to purchase the land) and to mortgage the construction over the land.

b Administrative concessions: These rights are usually granted over public land that cannot be owned by individuals or companies (i.e., sea and riverside areas, harbours, docks, green areas, etc). The public administration owning the land grants the right to use, develop and operate the public land to a third party in exchange for consideration and for a limited period of time. Even though it will not acquire ownership over the land, the third party will also benefit from other rights that are typically inherent to freehold owners such as the right to transfer

1 Diego Armero is a partner and Rodrigo Peruyero is an associate at Uría Menéndez.

or encumber the administrative concession. Such rights, however, are subject to certain limitations (usually the prior authorisation of the public administration owning the land and an obligation by the new holder of the concession to continue honouring the terms and conditions of the concession).

Spanish law recognises other types of rights over real estate such as the usufruct, which provides the legal right to use and obtain benefit from property owned by a third party in exchange for consideration and for a limited period of time but are very rarely used in commercial transactions.

ii System of registration

Freedom of form applies to real estate transfers and it merely requires a valid written contract and the delivery of possession of the property. In practice, however, transfer of real estate is always carried out in the form of a transfer deed because it is a requirement for having it recorded at the Land Registry. Although recording with the Land Registry is not compulsory, (except for mortgages and 'rights of surface', where registration is a requirement for validity), it is always advisable to do so as recording grants protection to good-faith third-party purchasers who acquire title from a registered owner in exchange for some sort of consideration. This means that ownership cannot be successfully challenged by a third party holding a right that was not recorded at the Land Registry, even if title of the registered transferor is later deemed void on grounds that do not appear at the Land Registry.

Since a transfer of ownership is usually instrumented through the execution of a notarial deed and its subsequent registration with the Land Registry, notary and registry fees have to be paid. Notary fees are calculated on the basis of the value of the transaction being recorded (however, transaction in excess of €6 million, notarial fees can be freely negotiated and agreed beforehand).

As for registry fees, although calculated on the basis of the transaction, they are capped at €2,200 per registered plot and are not negotiable. There are no other significant costs other than taxes as is explained in Section VI.iv, *infra*.

Notwithstanding the foregoing, when there is no actual transfer of ownership (i.e., conditional sales subject to conditions precedent) such transactions are not formalised through a transfer deed but in the form of a private contract (avoiding notary and registry fees). The notarial deed will be formalised on completion upon fulfilment of the relevant conditions precedent.

iii Choice of law

In commercial real estate transactions, the acquisition of assets will typically be structured through a Spanish special-purpose vehicle ('SPV') (as described in Section V, *infra*). Since the seller will most likely be a Spanish company, it is commercial practice to choose Spanish law as permitted by the principle of freedom of choice established in Regulation (EC) No 593/2008 on the law applicable to contractual obligations (Rome I).

II OVERVIEW OF REAL ESTATE ACTIVITY

The real estate and banking excesses that occurred in Spain should have been tackled at an earlier stage, but little by little they are being remedied. If 2008 to 2010 were the years of turning a blind eye to the financial problems through debt refinancings and debt-to-asset swaps, 2011 was the year of raising capital, realising capital gains and selling mortgage debt to strengthen balance sheets. As such, banks and highly indebted companies have and will continue to be the key players in the real estate market during 2012 and the next couple of years.

To eliminate or reduce risks from their balance sheets banks, for instance, are in the process of selling mortgage loans (whether performing or non-performing) as well as providing financing to purchasers of mortgaged real estate by allowing them to subrogate the seller in the mortgage debt (this has proved an excellent mechanism by which to find bank financing, which has been and will continue to be scarce).

Banks have also played an active role in shaking the market by requiring highly indebted development and real estate companies to sell assets as part of their refinancing processes, selling properties they acquired in past years in debt-to-asset swaps and even starting big sale and lease-back transactions with respect to their bank branches and corporate buildings.

With close to €200 billion of non-performing real estate loans and foreclosed assets (according to the last figures unveiled by the Bank of Spain), the new Spanish conservative government has recently approved the reform of the financial system ('the Reform'), which imposes the obligation on Spanish banks to make an additional write-down of €50 billion.

This obligation affects real estate loans and assets (acquired by way of mortgage foreclosure or as debt-to-asset deals). The coverage requirements for these assets are to be implemented through accounting provisions and capital buffers, which will be different according to the type of asset: distressed assets will be subject to specific accounting provisions for an estimated amount of €25 billion and to a capital buffer on account of non-distributed profit, capital increase or conversion of hybrid products of 20 per cent (with respect to land) and 15 per cent (with respect to ongoing developments) for an estimated amount of around €15 billion; non-distressed assets will be subject to a general 7 per cent accounting provision, for an estimated amount of €10 billion.

The deadline for implementing these measures is 31 December 2012; however, banks involved in mergers during 2012 will benefit from a 12-month extension.

Upon implementation of these measures, the banks' coverage to exposure for their distressed assets will increase from 31 per cent to 80 per cent (land positions), from 27 per cent to 65 per cent (ongoing developments) and from 25 per cent to 35 per cent (completed developments and housing units). Losses derived from the impairment of tangible assets, real estate investments and inventories will be disregarded during 2012 for the purposes of calculating the losses incurred by Spanish companies to determine whether it is in a capital impairment situation for corporate purposes, as the effects of Royal Decree-Law 10/2008 of 12 December have been extended to 2012.

These measures will force banks to make a substantial write-down of €50 billion in record time (by 31 December 2012), which will add to the €66 billion write-down already made between 2008 and June 2011. The obligation to make the provisions, together with the fact that banks involved in mergers must disinvest in real estate within three years of a merger,[2] will boost the real estate market as banks will be incentivised to place their real estate assets on the market with attractive prices.

III DEVELOPMENTS IN PRACTICE

i Non-recourse mortgage financing

Spain is one of the jurisdictions where lenders have full recourse to all assets of the defaulting borrower (not just the mortgaged property). The Spanish mortgage-financing system, however, has been recently shaken to its core after the Regional Court of Navarra upheld in 2011 a ruling admitting that relinquishing title of a mortgaged property to the bank is sufficient to cancel the mortgage debt. The court found it 'morally repellent' that the bank could pursue additional claims on the borrower because the property's fall in value was a direct result of the financial crisis stemming from financial malpractices. This court resolution ignited a debate that led the mainstream political parties to push for a reform of the current mortgage system towards a non-recourse mortgage-financing system. There is already a proposal for the amendment of the Spanish Procedural Act ('the Proposed Amendment'), which is currently under discussion in the Spanish parliament, which aims at stemming the tide of foreclosures of homeowners by providing the court with a means of weighing the different interests in the dispute (those of the bank to have sufficient guarantees and those of homeowners) when a property has to be foreclosed. As it is currently drafted, the Proposed Amendment aims to protect homeowners and not borrowers within commercial transactions where the bank will still benefit from full recourse.

It is still too soon to ascertain whether the Proposed Amendment will succeed (and if it succeeds, how), but the idea that the full-recourse system should be changed or at least watered down is permeating Spanish society, and some changes might be seen in the near future. As previously mentioned, any future amendment to the Spanish Procedural Act will most likely apply to loans granted to individuals to finance the acquisition of their homes and not to commercial loans; however, since the Proposed Amendment has not yet been approved, whether or not full recourse exists in commercial transactions is a matter that any prospective investor should verify as part of its due diligence.

ii Bank restructuring and real estate opportunities

Even though investors are flocking into Spain looking to buy assets from struggling lenders in need of cash, this has not always been welcomed by willing sellers when the prices offered were far from their price expectations. Sellers have not adjusted their expectations to the new market conditions and such a valuation gap is the roadblock to the much-needed correction of real estate prices.

This state of denial may end soon as the measures that the new government will take (as outlined above) will be a call for banks to initiate a merging process and such

2 According to a disinvestment plan to be included in the relevant merger authorisation application to be filed by 31 May 2012.

mergers are in turn expected to result in the banks getting rid of properties (then mark to market) in order not to overcharge the balances of the resulting banks.

The need to shed real estate may ultimately shake the market as it may very likely lead to banks setting up structures where real estate properties will be contributed (and where investors could participate) to setting up the conditions to develop, manage, operate and sell the contributed properties.

iii Valuation of land

On 24 October 2011, Royal Decree 1492/2011 on valuation of land was approved in order to implement the Spanish Land Act by defining the factors that should be taken into account in the determination of the value of a piece of land. Its ultimate goal is to combat speculative practices and to set up an efficient and transparent land market. This Royal Decree will apply to expropriation procedures to be carried out by the public authorities and has been welcomed by infrastructure companies who now see that the uncertainty surrounding the expropriation costs they had to assume will disappear. It will not, however, apply to the transactions carried out by banks with respect to the portfolio of land they are building as a result of debt-to-asset deals agreed with developers or foreclosure of mortgages where the value is calculated pursuant to Order ECO 805/2003 of the Ministry of Economy.

iv Spanish real estate investment trusts

Spanish real estate investment trusts ('SOCIMIs') were introduced two years ago. Essentially, SOCIMIs (which have to be listed) are similar to the real estate investment trusts ('REITs') existing in other jurisdictions and their purpose is, roughly, to acquire or develop real estate for its subsequent lease to third parties or to hold a stake in other SOCIMIs or foreign REITs whose profits are necessarily distributed to their shareholders. It was believed that investors and small savers would favour these instruments as a mechanism that would allow them to participate in the real estate income from properties or projects in which they would otherwise never be able to participate. Unfortunately, the obligation to pay out dividends contemplated in the SOCIMIs Act and the favourable tax regime applicable to their shareholders have not been enough to convince investors, and no SOCIMI has been created since the SOCIMIs Act was passed.

Despite the foregoing, during 2012 it could be worth exploring the possibilities with the Spanish banks (who, as explained above, will be obliged to reduce exposure to real estate) of the creation of SOCIMIs with properties already producing income as a way to instrument indirect investments in the Spanish real estate market once the capital markets turmoil finally ends.

IV FOREIGN INVESTMENT

As explained in Section V, *infra*, the acquisition of commercial real estate in Spain by foreign institutional investors or funds will typically be structured through a Spanish SPV owned by a foreign company. The acquisition of the SPV by the foreign company is not subject to prior authorisation but it must be reported to the Ministry of Economy within 30 days of the date the shares are acquired through the filing of form D1-A. This declaration is used for statistical purposes and merely demands corporate information on the foreign company (corporate name, registered address, nationality), the Spanish SPV (corporate name, registered address, share capital and reserves, whether the foreign shareholder has the ability to appoint its directors) and the value of the transaction. If the foreign company is a tax-haven resident, form DP-1 will have to be filed prior to the acquisition of the Spanish SPV (again, just for information purposes and not for obtaining authorisation) followed by form D-1A after the purchase of the shares has been completed.

There are very few exceptions where the acquisition of real estate may be subject to prior clearance. These will affect investments in state defence-related properties (or properties located near certain defence sites), or investments from tax havens or by foreign sovereign bodies.

V STRUCTURING THE INVESTMENT

Each investor is different and has its own goals, targets and demands when considering real estate investments.

Real estate investments can either be made by acquiring the property directly (asset deal) or indirectly by purchasing the share capital of the legal entity owning the real estate (share deal). The decision to choose between direct or indirect investments is usually tax-driven.

i Asset deals

Real estate investments are normally structured as an asset deal where a Spanish SPV owned by a foreign company (typically, a company incorporated in the Netherlands) purchases the asset.

On the Spanish tax side, the acquisition of a property by the Spanish SPV will be subject to VAT if certain requirements are met (see Section VI.iv, *infra*) and not to non-recoverable transfer tax, and the Spanish SPV will be subject to the Spanish corporate income tax, generally at a 30 per cent rate on its net income (and capital gains). Interest, amortisation and expenses are generally deductible, provided that they are linked to the company's business activities and transfer pricing rules are complied with.

The use of Spanish SPVs by Dutch companies is very common in real estate transactions for the following reasons:

a capital gains realised upon divestment will not be taxed in Spain when made through the sale of the stake of Spanish SPV, provided that the shareholder is entitled to the benefits of the Spanish–Dutch double taxation treaty (which is generally the case); and

b profits distributed by Spanish SPV to a Dutch company will be exempt from withholding tax in Spain, provided that certain requirements established in the Spanish Tax Law are met (mainly the Parent-Subsidiary Directive requirements).

Other EU jurisdictions, such as Ireland or Luxembourg can also be taken into consideration (although capital gains by an Irish or Luxembourg company derived from the alienation of shares in a Spanish real estate company are taxed in Spain).

ii Share deals

Share deals are generally disregarded because the acquisition of more than 50 per cent of the shares of a company with more than 50 per cent of assets as real estate is subject to non-recoverable transfer tax (payable by the purchaser) at a rate of between 3 and 10 per cent over the market value of the property (depending on the region in which the real estate is located); however, even though payment of transfer tax is the main drawback for going through a share deal (in addition to becoming potentially liable for any contractual, tax and legal matter attributed to the acquired company), due to the economic crisis, investors are currently considering share deals if the companies they acquire have embedded losses that could offset any gains resulting from the future sale of the property.

iii Sale of the property

Profits from real estate investments are subject to the general direct taxation rules. Capital gains obtained as a consequence of the transfer of property will be determined by the difference between the transfer price and the net book value of the property. Spanish corporate tax law allows a reduction of the effective tax rate from 30 per cent to 18 per cent in the event of reinvestment under certain conditions.

VI REAL ESTATE OWNERSHIP

i Planning

Planning is a matter on which the different autonomous regions have exclusive competence (except for some very basic aspects in the hands of the central state). In terms of planning, Spain has 19 different jurisdictions, and, as a consequence of their different needs, geographical configuration and economic development, some regions have a more liberal approach than others.

While the regulatory power lies with the regions, their implementation is handed over to the municipalities (although the most important matters will be subject to some control by the regions). This will require the cooperation of a number of administrations and other parties including local authorities (who will ultimately decide if and under what conditions the land can be developed), regional authorities (who will play a supervisory role), and to a lesser extent the state authorities (who will legislate and supervise matters under state control such as main roads, harbours, coastal areas, aviation liens and airports). Due to the different authorities and pieces of legislation involved, planning matters in Spain are complex (particularly when purchasing a piece of land for its subsequent development) and should be carefully addressed with a planning expert.

ii Licences

Usually (although requirements are not the same in all municipalities throughout Spain), the licences and permits required for the construction and operation of buildings will be as follows:

a a works and activity licence, which must be obtained prior to starting construction works;

b a first occupancy licence, which will verify that the construction complies with the terms authorised by the works licences; and

c operating licences, which will verify that the use carried out in the building complies with the relevant zoning regulations as well as health and safety and environmental matters.

In addition to the foregoing, other permits and licences may be required by the regional governments depending on the activity to be carried out. For instance, some regions will require a commercial licence for an operator to open large retail scheme (i.e., those exceeding a minimum sales surface area foreseen in the relevant legislations) or a tourism authorisation in case of hotels.

iii Environment

In order for a piece of land to be declared polluted, the contamination detected must exceed the parameters set out by Royal Decree 9/2005; these parameters have been determined taking into consideration the use (industrial, residential, etc.) of the land. The competent authority to declare a soil polluted is the environmental department of the regional government where the site is located.

Whenever a piece of land is formally declared polluted, the polluter will be ordered to carry out the cleaning and remedial activities required for the decontamination of the site; when there are several polluters involved, they will be obliged jointly and severally. As a general rule, in the absence of the polluter; the obligation to carry out cleaning and remedial activities falls on the owner and thereafter on the possessor of the site.

Finally, it must be noted that there is an obligation for the owner of a site where an activity potentially polluting of the soil (listed in Annex I to Royal Decree 9/2005) has been carried out to declare such circumstance in the public deed of transfer; this must be registered with the Land Registry. Only upon completion of the remedial activities and subsequent validation of the decontamination works by the regional government will the information about the pollution be removed from the Land Registry.

iv Tax

VAT and transfer tax

As a general rule, the transfer of properties by sellers in the course of a business activity is subject to value added tax ('VAT') at a 18 per cent tax rate (however, the rate in the case of transfer of dwellings is 4 per cent in the case of new dwellings or 8 per cent in the case of used dwellings). In all other cases, transfers are subject to transfer tax at a rate ranging between 3 per cent and 10 per cent of the purchase price (depending on the region where the property is located).

Second and subsequent transfers of built properties, however, made in the course of a business activity are technically subject to but exempt from VAT and thus, subject to transfer tax; however, the VAT exemption can be waived by the parties when the seller and the buyer are taxable persons for VAT purposes and the purchaser is entitled to a 100 per cent VAT credit allowance. If the VAT exemption is waived, VAT (not transfer tax) will be levied upon the transfer.

Meeting the requirements to validly waive the VAT exemption is relevant since input VAT incurred upon the acquisition of real estate is, generally speaking, fully deductible. This is not the case with transfer tax, which is a final cost for the acquirer. Therefore, where the conditions are met, the VAT exemption is waived to avoid paying transfer tax (which will be a sunk cost) and recover the VAT incurred.

Stamp duty

Stamp duty will be levied upon the notarial deed:

a if the transfer is subject to and not exempt from VAT, in which case stamp duty will be levied at a rate between 0.25 per cent and 1.2 per cent, depending on the region in which the real estate is located; or

b if the transfer is subject to but exempt from VAT and the VAT exemption is waived, in which case stamp duty will be levied at a rate between 0.25 and 2 per cent, depending on the region in which the real estate is located.

Stamp duty is paid by the acquirer. In addition, stamp duty is paid on many other occasions, including the creation of mortgages and certain other charges in the Land Registry, at a rate ranging from 0.25 per cent to 1.2 per cent.

v Finance and security

Spanish law sets forth a wide range of security packages similar to those used in other jurisdictions (e.g., mortgages, pledges of the bank account(s) held by the borrower to administer the income generated by the property, pledge of receivables held or to be held by the borrower, such as the lease rent, insurance compensations and VAT refund rights, and pledges over the borrower's shares).

Mortgages are the preferred and most commonly used security interest. Mortgages are security interests, enforceable with regard to third parties, which enjoy significant privileges and can be granted over any type of real estate. The mortgagee is entitled to enforce the collateral to the exclusion of most other creditors following relatively simple and expeditious foreclosure proceedings. A mortgage can secure all kinds of payment obligations, including, in particular, principal, interest, default interest and fees in respect of loans and credit facilities. It is worth noting that in the case of insolvency of the borrower, the lender will not be able to foreclose on the mortgage until one year has elapsed from the date the insolvency was declared or the date a composition agreement with the creditors was approved.

A mortgage must be formalised in a notarial public deed and be recorded with the relevant Land Registry for it to be valid and enforceable. This will trigger the obligation to pay notarial and registry fees as well as the obligation to pay stamp duty at a rate ranging from 0.25 per cent to 1.2 per cent of the maximum secured amount by the mortgage (this will typically amount to 140 per cent of the loan principal).

VII LEASES OF BUSINESS PREMISES

Freedom of contract governs lease agreements for business premises, with the exception of matters regarding lease bonds (the tenant has to provide a bond equal to two months' rent) and court jurisdiction (claims must be filed before the first-instance court within the city where the property is located except if the parties have agreed to submit claims to arbitration), which cannot be waived or agreed upon differently by the parties. Any matter not contemplated by the parties in the lease agreement will be governed by the provisions of the Spanish Lease Act and the Spanish Civil Code.

i Initial lease term

The lease term can be freely agreed by the parties and the average term depends on the type of property being leased. For instance, lease agreements in a shopping centre or retail park would usually be agreed for five-year term (subject to renewals) while a lease of a single tenant office building will most likely be agreed for larger terms (10 to 15 years) and even above 15 years in sale and lease-back transactions.

ii Renewals

There is no statutory right of renewal and the parties may either expressly exclude or include the possibility of renewal in the lease agreement. In this regard, it is market practice to foresee that any lease renewals be subject to a market rent review. If there is no express provision and the tenant continues to lease the premises with the landlord's consent for 15 days after the lease has expired, the Civil Code will allow the tenant to renew the lease for a term equal to the periodicity of the rent term (i.e., monthly if the rent was paid monthly).

iii Rent review

The Spanish Lease Act does not regulate rent reviews and parties generally agree annual reviews according to the Spanish Consumer Price Index, which is published monthly by the National Statistics Institute. As previously mentioned, market rent reviews are usually agreed as a condition to renew the lease and are even found in long-term leases (e.g., on a 15-year term lease, the rent will be reviewed to market in year seven).

iv Service charges

There are no legal restrictions that may impair the ability of the landlord to recover service charges from tenants and the amount of service charges to be recovered will very much depend on the tenant's bargaining power. The tenant's contribution to service charges is usually calculated based on the surface area occupied by the tenant's premises. Anchor tenants may benefit from caps to service charge contributions or even be able to agree a fixed monthly contribution. Triple-net leases are not uncommon in Spanish commercial lease practice and are usually required by investors' sale and lease-back transactions. Recoverability of real estate tax is usually an important issue when negotiating leases, as it represents a big cost for the owner. Town councils all over Spain have anticipated significant tax revenues in their respective municipalities.

v Lease bond

As previously mentioned, upon execution of the lease agreement the tenant has to provide a bond equal to two months' rent. The lease bond cannot not be reviewed (upwards or downwards) during the first five years of the lease. From the sixth year onwards, the lease bond will be reviewed in accordance with the terms of the lease contract. Failing that, it will be reviewed in the same form provided for in the contract for reviewing the rent in order for the lease bond to be always equal to two months' rent.

vi Assignment and sub-letting

Unless otherwise agreed by the parties, tenants may sub-let or assign the premises to any third party without the landlord's consent. Except as otherwise agreed by the parties, the landlord may increase the rent by 10 per cent for partial sub-lets, and 20 per cent for total sub-lets or assignments.

vii Maintenance and repair

Even though the Spanish Lease Act contains provisions on maintenance and repair duties, it is commercial practice to replace such legal provisions (based on the freedom of contract principle) by contractual provisions that are more landlord-friendly. Typically, the parties will agree that the tenant must repair any damage to the premises and that it should perform any actions necessary to keep the premises in good state of maintenance and repair, and that the landlord would carry out any such works affecting the structure and façade of the premises. The tenant is not entitled to carry out any repairs that may affect the structure of the premises, unless it has obtained written consent from the landlord.

viii Insolvency

The Spanish Insolvency Act provides for the continuation of the lease agreement in the event of the tenant's insolvency as it expressly states that the declaration of insolvency does not affect any existing agreement that provides for reciprocal obligations that both parties have yet to perform.

Any outstanding payment obligations under the lease agreement will be payable to the landlord directly against the insolvency estate, as these credits will not be subject to the moratorium or reduction rules laid down in the insolvency proceedings. An insolvent tenant may reinstate the lease agreement and stop eviction proceedings exercised by the landlord before the declaration of insolvency at any time before the eviction takes place by paying all amounts due, including the landlord's court costs up to such time. This right to reinstate the lease is allowed only once.

VIII OUTLOOK AND CONCLUSIONS

2012 will be the year of structural changes in Spain that will be fuelled, mainly, by the long-awaited reform of the financing system that was initiated in 2011 when Royal Decree 2/2011 requested that financial institutions have a core capital higher than those required under Basel III.

The measures that banks will have to take pursuant to the Reform will ultimately result in the stronger banks stepping in to absorb the weaker ones. As a result of (or as condition to) such reorganisation process, banks that are highly exposed to real estate will be forced to discard reposed assets and underperforming or non-performing loans.

Loan portfolios or troubled assets whose works have been terminated may be sold to investors directly, while land and unfinished properties could be channelled into an SPV, where investors would contribute cash and know-how for their development and sale.

It is likely that distressed transactions will keep the attention of investors (both with respect to real estate and loan portfolios). Given that these types of transactions are characterised by the high discounts applied to the purchase price (particularly if the property is owned by a bank that has to make an additional provision on the value of the property as indicated above), sellers will not be willing to give any representations and indemnities. Due diligence will then be key and will have to be detailed enough to provide the investor with an accurate picture of the situation of the property it is acquiring in order to be able to ascertain whether or not the price paid outweighs the risks (if any) it is assuming.

Appendix 1

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DIEGO ARMERO

Uría Menéndez

Diego Armero is a partner in the Madrid office of Uría Menéndez. He joined the firm in 1999 and became a partner in 2006. Mr Armero advises on all types of real estate transactions and, particularly, on sale and purchase of companies operating in the real estate sector, asset deals, sale and lease back transactions, loan portfolios and real estate finance.

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Rodrigo Peruyero is an associate in the Madrid office of Uría Menéndez. He joined the firm on July 2009 and previously worked at Linklaters (Madrid office) and DLA Piper (New York office). Mr Peruyero has extensive experience in corporate and commercial law and focuses on all sort of commercial real estate transactions. He is admitted to practise in Madrid and in New York.

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