The Lending and Secured Finance Review

Ninth Edition

Editor
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PREFACE

This ninth edition of *The Lending and Secured Finance Review* contains contributions from leading practitioners in 15 different countries, and I would like to thank each of the contributors for taking the time to share their expertise on the developments in the corporate lending and secured finance markets in their respective jurisdictions, and on the challenges and opportunities facing market participants. I would also like to thank our publishers without whom this review would not have been possible.

I hope that the commentary that follows will serve as a useful source for practitioners and other readers.

Azadeh Nassiri
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Chapter 13

SPAIN

Ángel Pérez López, Pedro Ravina Martín and Blanca Arlabán Gabeiras[1]

I OVERVIEW

The Spanish economy, like any other, has been exposed to significant challenges during 2022 and the first quarter of 2023 due to, among other things, pressure on energy prices, persistent inflation, strains on supply chains, the continuous rise in interest rates and, generally, increasing uncertainty. However, the overall impact of all these factors on Spain's growth outlook has not been as strong as previously anticipated. The Spanish economy grew at a rate of 5.5 per cent during 2022, mostly as a consequence of a very positive first half of the year. During the second half of the year, however, and in line with global markets, GDP growth slowed down significantly as financial conditions worsened and capital markets closed.

According to the Bank Lending Survey, in 2022 and first quarter of 2023 credit standards tightened across the board in Spain and loan demand fell. Even if the Spanish banks remain strong, with robust capital and liquidity positions, they have been less active in lending to the real economy, partially due to a lower risk tolerance and reduced appetite to lend to certain sectors.

Part of this financing gap has been closed by alternative players, with direct lending continuing to show steady growth when compared to previous years. It is particularly interesting to note that in the Spanish market it is not uncommon to see banks and direct lenders participate alongside each other in blended structures, as opposed to the super senior and senior structures observed in the UK and elsewhere.

The non-performing loans (NPL) ratio for Spanish banks, which had declined in former years, is expected to rise again. As a consequence, Spanish banks are already reactivating the sales of loan portfolios and distressed real estate assets and will likely continue to do so in the near future.

Large restructuring transactions did not play an important role during 2021 and 2022, because the legal deadline to file for insolvency was extended several times until 30 June 2022 and the banks made available state guaranteed financings, which enabled companies to overcome their liquidity difficulties. However, companies are now facing the normalisation of activity with increasing indebtedness, and debt restructuring will be necessary during the second half of 2023 (for which purposes the transposition of the Restructuring and Insolvency Directive is already being and will be key in the future, as further explained below).

As in any other jurisdiction, M&A activity significantly dropped during the second semester of 2022 and 2023 due to, among other reasons, the difficulty in raising financing.

1 Ángel Pérez López, Pedro Ravina Martín and Blanca Arlabán Gabeiras are partners at Uría Menéndez Abogados, SLP. The authors thank David López Pombo (partner) for his contributions to the tax section of this chapter.

However, despite this overall decrease in M&A activity, the high demand for companies operating in attractive markets, such as the infrastructure, renewables, TMT, tech and healthcare sectors, continued during 2022, with some of the most relevant acquisition finance deals closed in relation to these industries (such as Reintel, Lyntia, IVI RMA). Conversely, opportunistic M&A and finance deals are expected to continue in respect of those sectors badly hit by the current macro environment.

II LEGAL AND REGULATORY DEVELOPMENTS

Since the beginning of the pandemic, extensive new regulation was put in place both at the national and European level to try to mitigate the impact of the covid-19 crisis on the real economy and the financial sector, but those extraordinary measures are no longer applicable in Spain.

In particular, debtors in an insolvency situation under the Spanish Insolvency Law are again obliged to file for insolvency within two months from the date when they became aware of the insolvency situation (the insolvency moratorium that allowed debtors to disregard this duty expired on 30 June 2022). Equally, the obligation to liquidate companies subject to a situation of capital impairment (i.e., if their net worth is lower than 50 per cent of the share capital due to losses) did not apply in respect of losses generated during 2020 and 2021. Losses in respect of those two years will continue to be disregarded until the financial year starting in 2024 (included), but losses from 2022 onwards will start being computed for the liquidation rule.

It is likely that the progressive reduction of public aid to companies, increasing inflation and the removal of these extraordinary measures will trigger in Spain more distressed, restructuring or insolvency situations in the coming months.

In that context, an important reform of the Spanish Insolvency Law was approved in September 2022 that, inter alia, implements the Restructuring and Insolvency Directive and updates the Spanish out-of-court restructuring legal framework. This piece of legislation should increase flexibility and provide alternative methods to successfully restructure viable businesses. Thus, the restructuring plan can establish, inter alia, haircuts, extensions, debt-for-equity swaps, debt-for-asset deals, sales of assets, third-party releases and effects on reimbursement claims of guarantors.

The main legal features of the reform are as follows:

a New money privilege. Provided that the restructuring plan is judicially approved, new money or interim financing injected into the debtor will enjoy protection against clawback, equitable subordination and 50 per cent of its amount will be considered a post-insolvency claim.

b Class formation. This is an essential concept in the new framework. Secured claims form a separate class. Sub-classes within classes of secured creditors may be formed according to differences in collateral. In order to approve the restructuring plan, creditors in each class vote and, in order for the class to be deemed to have voted in favour, at least two-thirds of the creditors in the class need to have voted in favour (three-quarters in the case of secured credit class or classes). A cram-down of classes that did not support the plan is possible in certain circumstances, for instance if a majority of classes have voted in favour and at least one of the classes voting in favour is either a secured or a generally privileged class.

c Restructuring expert. This is a new role in the out-of-court restructuring practice. An expert is required for, among other things, cross-class cram-down restructuring plans. In addition to generally assisting the debtor and the creditors, the expert is responsible for preparing all required reports and valuations (e.g. best-interest test, cross-class cram-down).

d Company group restructuring. Restructuring plans can include the release of security interests and guarantees granted by other group members who are not a party to the plan in order to avoid the insolvency of both the borrower and the guarantor. Additionally, the scope of the plan can include group affiliates with a centre of main interests outside of Spain provided that certain conditions are met.

Despite this positive legal development, there are still some challenges that are jeopardising restructuring of viable businesses; for instance, when a banking loan is guaranteed by the Instituto de Crédito Oficial (ICO, a Spanish public credit institution), the approval of the Spanish public authorities is required for the bank to vote in favour of the restructuring plan. Given the very active role of ICO during the pandemic period, with multibillion guarantee programmes to facilitate liquidity to the real economy, this issue is affecting the restructuring of a large number of debtors.

In any event, the new legal framework is already being used in landmark restructuring transactions, including Telepizza and Celsa, and is expected to be used in some other distressed situations during the second semester of 2023.

In addition to the reform of the Spanish Insolvency Law, the trend of protection of vulnerable debtors under residential mortgages has continued with the approval of an update of the Code of Good Practices, which all the Spanish financial institutions have adhered to.

III TAX CONSIDERATIONS

The main corporate tax chargeable on interest and other amounts receivable under a loan by a Spanish resident corporation is corporate income tax, which applies to the entire income obtained by the taxpayer. Interest received should therefore be included with all the other worldwide income generated by a Spanish resident lender. Interest must be included within the corporate income tax base when accrued. The accrual principle for Spanish corporate income tax purposes follows Spanish General Accepted Accounting Principles (which, generally speaking, follow International Financial Reporting Standards rules). The general corporation tax rate is 25 per cent (30 per cent for, for example, banks).

Borrowing costs are normally deductible expenses for corporate income tax purposes. Borrowing costs include interest of any kind, transaction costs and other similar expenses, and may be deducted when accrued. As an exception to the rule, stamp duty levied on lenders upon the execution or amendment of mortgage loans is not deductible for Spanish corporate income tax purposes.

Nevertheless, tax deduction of interest for borrowers is contingent upon some limitations, namely, interest from participating loans in which the lender and the borrower are members of the same group of companies is not deductible.

Interest from loans in which the lender and the borrower are members of the same group of companies is not deductible if the funds borrowed are used to buy shares from a

seller who is also a member of the same group of companies, or to make equity contributions to entities who are already part of the same group of companies, unless the taxpayer proves that the transaction has valid economic reasons.

The earning stripping rule: net financial expenses that exceed the higher of 30 per cent of operating profit or €1 million is not deductible. Net financial interest means the excess of financial expenses over income derived from borrowing funds from other entities or persons. Operating profit is calculated in a similar way to earnings before interest, tax, depreciation and amortisation (EBITDA). Net financial expenses that have not been deducted can be carried forward with no time limit but are subject to the above thresholds of each fiscal year. Unutilised operating profit may be carried forward for five years. This earnings stripping limitation is not applicable to, inter alia, Spanish securitisation funds, credit institutions or insurance companies.

The deductibility of interest from loans used to acquire shares (leveraged buyout interest barrier) is generally limited to 30 per cent of the EBIDTA of the acquiring company if the entity is merged or makes a tax group with the acquired entity or other entities in the following four years. However, this limitation should not apply in the tax year in which the acquisition is executed, provided that the acquisition is financed with a maximum debt of 70 per cent of the acquisition price; and in the following years, should the loan be reduced, at least proportionally, on an annual basis within the following eight years, until the debt is 30 per cent of the acquisition price. This rule is complex, and proper analysis and monitoring must be carried out by taxpayers.

Additional limitations to the deductibility for tax purposes of certain interest expenses have recently entered into force as a result of the transposition into national law of Directive (EU) 2016/1164 as amended by Directive (EU) 2017/952 (ATAD II). Very simply stated, these limitations apply, under certain conditions, to cross-border payments that determine 'hybrid mismatches' (i.e., situations of deduction-without-inclusion, double no-inclusion or double deduction of expenses, including imported hybrid mismatches) between associated entities or in the context of a structured arrangement (e.g., an arrangement involving a hybrid mismatch where the mismatch is priced into the terms of the arrangement or an arrangement that has been designed to produce a hybrid mismatch). These rules are complex, and the Spanish tax authorities have not, to date, issued any official interpretation or criteria on the matter. Therefore, their potential application should be properly analysed on a case-by-case basis.

The Spanish tax authorities have challenged the deductibility of financial expenses derived from financing incurred in order to, for example, distribute a dividend or share premium (dividend recaps) or acquire treasury stock for its redemption. While in a particular case, *Cupire Padesa*, the position of the Spanish tax authorities was ruled out, at least three more cases have been brought to the Supreme Court relating to the deductibility of financial expenses incurred in this sort of indebtedness. Therefore, proper monitoring should be made in this vein.

Interest paid is generally subject to withholding tax at a rate of 19 per cent.

Withholding taxes applied on interest payments to taxpayers who are corporations resident in Spain are refundable from the corporate income tax payable by the recipient. Specific interest payments to Spanish resident corporations are exempt from withholding tax, such as:

a interest paid to entities that are exempt from corporation tax (e.g., Spain, its political subdivisions and its administrative agencies, the Bank of Spain);

b interest paid to Spanish resident banks and some other credit institutions, provided that the credit does not qualify as bonds or securities included in the trading portfolio of the corresponding credit institution;

c interest paid to Spanish securitisation funds; and

d interest paid between entities belonging to the same Spanish tax consolidation group.

On the contrary, the 19 per cent withholding tax levied on the payment of interest to taxpayers who are not resident in Spain is not refundable (it is a final tax), but there are specific exemptions from withholding tax or reduced withholding tax rates:

a interest paid to residents in the EU or European Economic Area (EEA) (in this latter case with an effective exchange of tax information agreement with Spain, such as those of Norway and Iceland) should be exempt, provided that the EU or EEA resident is:
- the beneficial owner of the interest (as interpreted by the European Court of Justice in the joined cases *N Luxembourg 1*,[2] *X Denmark*[3] and *C Danmark 1*[4] and the *Z Denmark* case;[5] the *Interest BO Danish* cases, which were adopted by the Spanish Central Economic-Administrative Court in its resolution of 8 October 2019); and
- does not act through a tax haven or non-cooperative jurisdiction or territory for Spanish purposes, nor through a permanent establishment located in Spain or in a country or territory that is not an EU or EEA Member State; and

b interest paid to non-EU or non-EEA residents who are resident in a double tax convention jurisdiction may, under the applicable convention, benefit from withholding tax reductions or exemptions if they are the beneficial owner of the interest.

In these cases, the non-Spanish resident lender must evidence to the Spanish tax authorities or the withholding tax agent (generally, the debtor) the application of this exemption and its status as, for example, tax-resident in an EU or EEA Member State by means of a certificate of tax residency duly issued by the corresponding EU or EEA Member State tax authorities. These certificates are generally valid for a one-year period.

The granting and negotiating of loans and credits as part of the credit activity of the lender is a supply of services subject to but exempt from value added tax.

Mortgages are subject to stamp duties generally ranging between 0.5 and 2 per cent (depending on the Spanish region where the mortgaged asset is located) on the total amount (principal, interest, default interest, penalties, etc.) secured by the mortgage.

The assignment of loans or credits secured by a mortgage is generally subject to stamp duty unless made in a private agreement (i.e., a document not having access to the Land Registry). Transfer tax (normally at a rate of 1 per cent of the total guarantee) may apply to specific guarantees.

In 2013, the United States and Spain entered into an intergovernmental agreement to provide for the implementation of the US Foreign Account Tax Compliance Act (FATCA). FATCA requires financial institutions (FFIs) outside the United States to report certain

2 C-115/16.
3 C-118/16.
4 C-119/16.
5 C-299/16.

information on US account holders to the US tax authorities. If those FFIs fail to report the required information (non-participating FFIs), a punitive 30 per cent tax may be withheld on, inter alia, their US source income.

The Loan Market Association (LMA) published and subsequently amended a template investment-grade facility agreement, including FATCA provisions that are generally used in cross-border transactions and by Spanish lenders and borrowers. In summary, the FATCA provisions include the following:

a FATCA-defined terms;

b the obligation of providing FATCA information (that is, mainly, whether the parties are exempt from FATCA, which means that they are not non-participating FFIs); and

c FATCA gross-up clauses.

The gross-up obligation varies depending on who should be protected from FATCA withholding. However, it is market practice that borrowers do not make additional payments in the event of FATCA withholding because it only arises when the lender is a non-participating FFI; therefore, the risk of FATCA withholding is essentially one that can be mitigated by the lender. In addition, when the transaction requires a paying agent, it is common to include provisions requiring the resignation of the agent if the agent becomes a non-participating FFI, because of the risk of FATCA withholding being required. Therefore, the practice in Spain does not differ substantially from that followed in other jurisdictions.

IV CREDIT SUPPORT AND SUBORDINATION

Financing transactions governed by Spanish law are frequently secured by security interests and guaranteed by personal guarantees that will generally only be enforced by the security agent (to avoid partial foreclosures by any creditor). As the legal concept of the security trust does not exist under Spanish law, the agent will need to prove that it has been duly and expressly empowered[6] to carry out this enforcement.

i Security

Pledges

Pledges are created over movable assets, and possession over the collateral must be transferred to the pledgee.

Standard pledges include pledges over shares and pledges over credit rights (e.g., those arising from the balances in bank accounts, operational agreements, insurance policies or hedging agreements).

Real estate mortgages

Real estate mortgages are created over any real estate property and must be executed in a public deed before a notary public and registered with the land registry where the asset is located. Real estate mortgages generate significant costs and taxes.[7]

6 Powers of attorney for this purpose will need to be notarised and, where appropriate, apostilled or legalised.

7 These costs include stamp duty (described in Section III), notarial fees and land registrar fees. The calculation base for these costs is the total amount secured by the mortgage.

Spanish law provides for the possibility of creating a floating mortgage, which is a security interest created over a specific real estate asset to secure an indefinite number of liabilities up to a maximum cap. Floating mortgages can only be granted in favour of financial institutions and public authorities (and in the latter case, exclusively to guarantee tax or social security receivables) and, therefore, this constitutes an implicit restriction for trading the loans secured with floating mortgages (see Section VI). The floating mortgage deed must include a description of the actual or potential secured liabilities, the maximum mortgage liability (which will cover all the obligations without allocating mortgage liability to each of them), the term of the mortgage, and the method of calculating the final secured amount and balance payable.

Chattel mortgages and pledges without displacement

Chattel mortgages can only be created over:

a business premises;
b cars, trains and other motor vehicles;
c aircraft;
d machinery and equipment; and
e intellectual and industrial property.

Powers of attorney for this purpose will need to be notarised and, where appropriate, apostilled or legalised.

These costs include stamp duty (described in Section III), notarial fees and land registrar fees. The calculation base for these costs is the total amount secured by the mortgage.

There is a specific type of mortgage for ships (naval mortgage). A chattel mortgage must be executed in a public deed before a notary public and registered with the Movable Assets Registry.

Pledges without displacement can only be created over:

a harvests;
b animals on plots;
c harvesting machinery;
d raw materials in warehouses;
e merchandise in warehouses;
f art collections; and
g credit rights held by the beneficiaries of administrative contracts, licences, awards or subsidies, provided that this is permitted by law or the corresponding granting title, and over receivables (including future receivables) not represented by securities or qualified as financial instruments.

Pledges without displacement must be executed in a public deed or public policy before a notary public, and registered with the Movable Assets Registry.

Except for pledges without displacement over credit rights and inventories, these security interests are rarely used in Spain, mainly because:

a the pledgor or the mortgagor would not be able to sell the relevant assets without the pledgees' or the mortgagees' consent, respectively;
b most of the assets that can be mortgaged with a chattel mortgage (mainly those that are not movable) can be covered by a real estate mortgage if expressly agreed to by the parties in the real estate mortgage deed; and

c in most cases, those assets that cannot be covered by a real estate mortgage are not valuable enough to warrant the cost of creating the chattel mortgage.

Financial collateral

Financial collateral is a security interest that secures the fulfilment of principal financial obligations. Although not unanimous, the most common construction is that obligations pursuant to almost any financing document can be secured by financial collateral. Financial collateral can consist of cash or securities and other financial instruments, and certain types of credit rights held by credit institutions. Therefore, financial collateral could be made up of shares issued by public limited liability companies – although some scholars question whether it can include shares in non-listed companies – and credit rights arising from the balances in bank accounts.

This type of security interest may benefit from a separate enforcement procedure if the debtor becomes insolvent and, as regards pledges over shares, can be foreclosed by a private sale (not in a public auction, as is the general rule under Spanish law) conducted by the depository of the shares or by the pledgee's direct appropriation of the shares, breaching the general Spanish law principle that prohibits any form of foreclosure of a security agreement that enables the holder of the security interest to directly and immediately acquire the secured asset. A Spanish financial collateral security interest offers reasonably quick and safe enforcement that can compete with other security structures such as double Luxcos.

ii Guarantees and other forms of credit support

Normally, the borrower's shareholders and each of its subsidiaries provide, to the extent permitted by law (specifically, the financial assistance prohibition and conflict of interest restrictions), first demand guarantees or other types of personal guarantees in respect of the fulfilment of the obligations assumed by the borrower under the financing documents.

A personal guarantee may be created by agreement between the creditor and the guarantor, or by operation of law. To facilitate the enforcement of a personal guarantee against a Spanish company, a settlement clause establishing the method of calculating the outstanding debt is usually included.

A guarantor cannot be obliged to pay the beneficiary of the guarantee until all the debtor's assets have been realised. This benefit for the guarantor does not apply in the following cases:

a if the guarantor has waived the benefit;
b if the guarantee is joint and several;
c if the debtor is declared insolvent; or
d when the debtor cannot be sued in Spain.

Additionally, a guarantor may raise against the creditor all the exceptions and defences corresponding to the debtor that are inherent to the debt.

First-demand guarantees, which are not regulated by law, are abstract and independent from the main obligation, creating a primary liability on the guarantor, and are not subject to the debtor's assets being realised. Lenders usually request that all personal guarantees created under the finance documents be first-demand guarantees.

iii Priorities and subordination

Priorities

Security interests are governed by the principle that security created earlier has priority over that created later. With respect to real estate mortgages, chattel mortgages and pledges without displacement, priority is determined by the date (and time) on which they are registered with the public registry, which is deemed to be the date (and time) on which the relevant document was submitted for registration. With regard to ordinary pledges, which are not registered in any public registry, priority is determined by the date (and time) on which possession is transferred. However, Spanish law allows creditors to agree on the priority of pledges and real estate mortgages. Therefore, creditors can agree that all the credits have the same priority, or a creditor can decide to assign its priority to another.

Pursuant to the Spanish Insolvency Act, in the context of bankruptcy proceedings, credit rights secured by security interests will benefit from a special privilege up to the value of the collateral. The creditor is generally considered an ordinary creditor in respect of the excess.[8]

Subordination

Notwithstanding this, classifying a bankruptcy credit as subordinated credit would entail extinguishing any security granted in favour of the creditor (and, as a result, any special privilege to which the creditor may be entitled). Under Spanish law, subordination can be triggered by operation of law or from a contract.

Contractual subordination in Spain is in line with international practice. The contractual provisions in this regard are similar to those of other jurisdictions.

Spanish insolvency law refers to a category of subordinated claims, that entails the subordination, by operation of law, of certain claims to the prior payment by the insolvent debtor of all ordinary claims. These subordinated claims include, among others, the following:

a claims that are not notified by the creditors to the insolvency trustee in a timely manner;
b claims that are contractually subordinated to all remaining claims of the debtor;
c claims for interest; and
d most importantly, all rights against the debtor held by legal or natural persons who qualify as 'specially related' to the debtor. This category includes shareholders holding a stake of 10 per cent or more in the insolvent entity (or 5 per cent if the insolvent entity is a listed company) when their credit right arose, formal directors, or shadow directors, and companies of the insolvent entity's group. Note, however, that, as an

8 In the context of bankruptcy proceedings affecting Spanish companies, creditors will be divided into two categories: bankruptcy creditors and creditors against the insolvency estate. The list of creditors against the insolvency estate is closed and includes expenses incurred in the proceedings and essential basic expenses for the debtor to continue in business (e.g., salaries, utilities), and these creditors will be paid before any uncharged assets are distributed to the bankruptcy creditors. The claims of bankruptcy creditors may be classified as privileged, ordinary and subordinated. Privileged claims may, in turn, be deemed specially or generally privileged.

However, as indicated in Section II, for the purposes of voting for a restructuring plan, credit rights must be grouped into distinct classes if there is a 'sufficient commonality of interest amongst creditors making up one class, according to objective criteria'. Claims that have the same payment priority are deemed to have a commonality of interest. In turn, claims with the same payment priority can also be separated into different classes based on justified sub-classification criteria.

exception, shareholders' credit rights that do not arise from loans or facilities (i.e., supply or other commercial agreements) are not subordinated. In addition, according to the new Insolvency Law, credit rights arising from interim financing granted by shareholders shall not be subject to clawback if the rest of the affected credits in a bankruptcy scenario exceed 60 per cent of the total liabilities.

There is also a rebuttable presumption that any person who acquired a credit against the insolvent debtor from any of those related parties within two years of the commencement of the bankruptcy proceedings (i.e., judicial declaration of bankruptcy) is also a related party for insolvency law purposes.

V LEGAL RESERVATIONS AND OPINIONS PRACTICE

Standards applicable to the issuance of legal opinions in Spain are not very different from those applicable in other jurisdictions. In pure lending transactions, legal opinions are usually issued by counsel to the lenders or arrangers, except when capacity opinions are requested from counsel to the borrowers. This also applies in plain vanilla bond issuances. On the other hand, in high-yield bond transactions it is usual that legal opinions are issued by counsel to the arrangers or initial purchasers and by counsel to the issuer. Limitations apply to disclosing legal opinions to third parties other than the initial addressees. Disclosure without reliance may be permitted in some cases (e.g., if required by law or a court order, or to auditors or rating agencies on a need-to-know basis). Exceptionally, disclosure with reliance is permitted during the syndication of the loan, but this is normally restricted to a very short time frame and is subject to limitations and restrictions (including a requirement for the disclosing entity to notify the opinion provider of such disclosure).

Below is a description of the main issues and most frequent legal reservations in practice in Spain.

i Corporate benefit

Directors of Spanish companies have a general duty to act loyally and diligently in compliance with the applicable law and in the best interests of the company.

It is not always easy to prove that providing security or guarantees in the context of a group financing is in the best interests of a company. Any analysis of this circumstance is ultimately factual.

Accordingly, corporate benefits should be analysed on a case-by-case basis considering, among other things, the structure of the group, the nature and amount of the guarantees provided, the purposes of the financing and the direct and indirect consideration received by the relevant guarantor. With regard to downstream guarantees, corporate benefit may be easier to prove. However, courts have always been more suspicious about upstream or cross-stream guarantees.

ii Clawback

According to the Spanish Insolvency Act, any action taken or agreement reached in the two years preceding the declaration of insolvency of a company can be rescinded by the court if the receiver can prove that the action or agreement was 'detrimental to the insolvency estate'.

'Detrimental' is not defined and has been construed rather broadly by the courts. The Spanish Insolvency Act also provides for certain circumstances in which a detriment to the insolvency estate is presumed to exist. Among other things, unless proven otherwise, the granting of security in respect of pre-existing or refinanced debt is presumed to be detrimental to the insolvency estate. Moreover, debt prepayments (with some exceptions in secured loans), gifts and other benefits for no consideration are automatically presumed to be detrimental.

However, the Spanish Insolvency Act provides some safe harbours for the refinancing of existing debt, which is protected from clawback risk subject to compliance with specific formalities and majority thresholds, which differ depending on whether the refinancing agreement has been subject to court sanction.

iii Financial assistance

Companies are generally prohibited from providing financial assistance in respect of acquisitions. Breaching this prohibition could entail both liability for directors and the nullity of the transaction in which the financial assistance was provided.

Acquisition finance transactions have been structured to comply with the restrictions on financial assistance (other than creating separate debt tranches) by implementing a debt push-down through a forward merger. From 2009 onwards, however, a specific regulation applies to forward mergers whereby if two or more companies merge and any of them has received financing within the three years prior to the acquisition of a controlling stake in, or essential assets of, any of the companies that are part of the merger, some protective measures apply. Among other things, directors must issue a report justifying the merger, and an independent expert must issue a fairness opinion confirming that the transaction is reasonable and that there has been no financial assistance. This provision has been subject to much debate, especially in relation to the scope and effects of the report issued by the independent expert.

iv Security trustee and parallel debt

Spanish law does not recognise the concept of a security trustee who is the legal holder and enforces the security package on behalf of the lenders from time to time. Thus, legal title over a security interest must be held by the creditor of the secured obligation.

Furthermore, the validity and enforceability of any parallel debt governed by Spanish law is uncertain, because under Spanish law, contracts and obligations are only valid and enforceable if they are based on a valid and legitimate reason (*causa*, which is the Spanish version of the English law concept of consideration).

In view of the above, lenders will need to provide a notarised and (in the case of foreign lenders) apostilled power of attorney in favour of the security agent to enable it to lead a coordinated enforcement process on behalf of all the lenders.

v Acceleration

In the Spanish market, the decision to accelerate loans and enforce security is usually an act of last resort once all other alternatives such as debt restructuring have failed. However, courts have traditionally been reluctant to uphold loan acceleration and subsequent enforcement of security if the default is not deemed material.

The recent Real Estate Credit Agreements Law includes a detailed and mandatory regulation for acceleration clauses if there is a payment default of a mortgage loan by consumers.

Thus, to accelerate the mortgage loan, the following requirements must be met:

a the borrower is in default;

b the lender requests the payment from the borrower and grants him or her a minimum term of one month to make the relevant payment; and

c the instalments amount to at least 3 per cent of the principal or 12 monthly instalments if the payment default occurs in the first half of the mortgage loan; or 7 per cent of the principal or 15 monthly instalments if the payment default occurs in the second half of the mortgage loan.

These rules also apply to mortgage loan agreements signed prior to the entry into force of the Real Estate Credit Agreements Law that include an acceleration clause, unless the borrower claims that applying the relevant acceleration clause is more favourable or the relevant acceleration clause was triggered prior to the entry into force of the Real Estate Credit Agreements Law (regardless of whether, as a result, enforcement proceedings were initiated, or whether the proceedings are suspended).

VI LOAN TRADING

The assignment of a lender's participation under a facility agreement governed by Spanish law may be carried out by:

a assigning the credit rights, which would result in transferring to the assignee the credit rights held by the assignor against the borrower (but not the contractual obligations assumed by the assignor towards the borrower); or

b assigning the contractual position under the agreement to any third party, and thus the relevant rights and obligations.

Hence, assigning the contractual position under an agreement would be relatively similar to a novation under English law, as it entails the transfer of both rights and obligations, and the subrogation of the assignee to the contractual position of the assignor. However, the previous contractual relationship does not need to be terminated. This is really unusual in the Spanish market, as loan acquirers usually cannot comply with the information, reporting, management and other obligations applicable to the loan as financial entities do, and therefore the usual structure is the acquisition of the credit rights arising from the loan that is previously accelerated. This transfer of credit rights can be made through a direct sale or, for mortgage loans, through the issuance of a Spanish regulated type of loan certificates, which are becoming more popular for the transfer of big mortgage loan portfolios.

No specific formalities need to be complied with for an ordinary transfer to be effective between the parties. However, under Spanish law, the transfer date must be certain and unambiguous for it to be fully effective against third parties. Therefore, it is very common to formalise the assignment agreement in a public document before a Spanish notary public. Furthermore, a notice must be served to the debtor to guarantee the assignee that any payment made by the debtor to the assignor will not release the former from its obligations as regards the assignee (as well as, if applicable, to comply with the data protection regulations). Following certain amendments to legislation in the autonomous regions of Catalonia, Navarre, Comunidad Valenciana and Andalusia, a notice must be served to the debtor (and, if applicable, to the relevant mortgagor) to inform it of the assignment and of the main terms and conditions of the assignment, including, in particular, the price paid by the

assignee to the assignor. Other amendments introduced to the legislation of the autonomous regions of Castilla La-Mancha and Comunidad Valenciana in 2019, and in Andalusia in 2020, respectively, require that a notice must be served if the relevant credit is assigned to a securitisation fund within a securitisation (i.e., not if the credit is transferred to the assignee through a direct assignment but through loan certificates). In the case of Castilla La-Mancha, the drafting of these amendments is rather obscure, and the consequences of not serving these notices are unclear. A similar piece of legislation was also in place in the autonomous region of Extremadura; however, in its resolution 72/2021 of 18 March 2021, the plenum of the Spanish Supreme Court declared void the precepts of the law upon which the serving of these notices became mandatory. It is still unclear the effect that this might have on the remaining autonomous legislation and whether we could be seeing a series of analogue resolutions, although for the moment it is most likely that we will not see any material change in this regard in the foreseeable future.

Spanish notarial documents are essentially public deeds that must be used for, among other things, any transaction that requires registration with a land registry, and public policies, which can only be used to formalise contracts of a commercial and financial nature corresponding to the ordinary course of business of at least one of the parties.

Although the creation and assignment of mortgages must be documented in a public deed, other types of security interests are usually documented in a notarial policy. The creation or assignment of a mortgage, when documented in a public deed, triggers stamp duty,[9] which must be paid and the mortgage registered for it to be able benefit from the advantages established under Spanish law (particularly, an expedited enforcement process). For the transfer of credit rights through loan certificates, the issuing bank remains as lender of record and no stamp duty is levied.

In turn, pledges without displacement, which must be registered with the Movable Assets Registry, may be documented in notarial policies (and thus no stamp duty accrues).

Moreover, some Spanish security interests cannot be assigned to every type of creditor. Floating mortgages can only be assigned to financial institutions and public authorities (and in the latter case, exclusively to guarantee tax or social security receivables), and financial security interests can only be assigned to:

a credit entities;
b investment services companies;
c insurance companies;
d collective investment in transferable securities;
e mortgage securitisation funds, asset securitisation funds and their managing entities;
f pension funds; and
g financing institutions.

In practice, this constitutes an additional restriction to the Spanish debt trading market.

Syndicated facility agreements governed by Spanish law usually provide for a specific form of assignment agreement, which is used by lenders when carrying out any assignment

9 See Section III. The Spanish tax authorities have recently issued two binding resolutions stating that the total amount secured should be understood as the outstanding amount of the facility as at the effective date of the assignment and not as its mortgage liability, as was the case beforehand. This may have an impact on transactions in which mortgage-secured facilities have been partially repaid by the debtors and on past transactions (the assignees may consider requesting a refund of any excess stamp duty paid).

of their participation in the loan. They also set out the conditions under which an assignment may be carried out without the debtor's consent. Although the lenders' aim is to make the above-mentioned conditions more flexible, the borrower usually wishes to limit the concept of permitted assignee or permitted assignment for the financing to remain under the control of its banks, namely the banks with which it has a special relationship and is familiar. It is not unusual for creditors to close the terms and conditions of the assignment pursuant to LMA trade forms, but executing trade confirmations is generally supplemented by executing the form set out in the facility agreement or any other assignment agreement governed by Spanish law that is subsequently formalised in a public deed. This requirement is particularly important for evidencing title to claim the assigned indebtedness and to enforce the security interests and personal guarantees. This is especially relevant for movable or immovable mortgages and pledges without displacement, where the creditor must be a registered creditor.

Spanish financial institutions are among the European leaders in deleveraging, launching to the market every year several competitive processes to transfer single names when they are not confident about a particular economic sector or about the debtor's ability to recover financially. Likewise, credit rights are often grouped together (according to the type of security attached to them or the nature of the debtors) to launch to the market big non-performing assets portfolios that attract investors from all around Europe, converting Spain into of the main European markets for NPAs, and also facilitating the development of an ancillary industry (servicers, notary publics, lawyers, etc.) with a strong specialisation in the recovery process and asset management.

Spanish banks had made a great effort to reduce the volume of non-performing loans (NPLs) during the past decade, and default ratios are at minimum levels. However, the recent increase in interest rates, together with the impact of the covid-19 crisis, is increasing the doubtful debt in banks' balance sheets, not with debt that is actually unpaid, but that is unlikely to pay (UTP). Thus, banks are reactivating the deal flow of NPL portfolios and are starting to sell UTP portfolios, which require a more intensive involvement of the selling bank as lender of record of the UTP loans. The sale of unsecured NPL portfolios (both of individuals and small and medium-sized enterprise (SME) portfolios) remains as a healthy pattern for banks to regularly clean their balance sheets, and sales of small and mid-size real estate owned portfolios are increasing. The pipeline of secured NPL portfolios is being reactivated, in several cases with transfers through loan certificates and securitisation structures (remaining the bank as lender of record).

Documentation of the NPLs has been a crucial negotiation point, because purchasers need notarial copies of the loans with enforcement effects to accede to an expedited enforcement process. Some years ago, it was unclear whether notaries were able to issue second copies with enforcement effects when the previous copies were unavailable or had been lost by the assignors. Assignors were reluctant to assume strong commitments regarding the delivery of original documentation, and the risk of not having all the copies with enforcement effects, particularly for mortgage portfolios that were not enforced, could lead to a decrease of the price paid by the assignee. However, the General Directorate of Registries and Notaries has recently clarified that the assignee of a mortgage loan has the right to request the issuance of a new copy with enforcement effects of the loan, provided that the relevant assignee, among other things, has not previously requested this type of copy for the same loan. This clarification has been welcomed and will significantly facilitate one of the key negotiation points in this type of transaction.

Pursuant to Article 1,535 of the Spanish Civil Code, a debtor would be entitled to extinguish a loan that is assigned to a third party if the relevant loan is deemed a disputed claim by paying to the assignee an amount equal to:

a the purchase price (thus benefiting from any agreed discount); plus

b any legal costs that the assignee may have incurred; plus

c any interests accrued on the price as from the date on which the purchase price was paid to the assignor.

The Spanish Supreme Court has clarified that this right shall be construed restrictively and shall not apply to sales of a portfolio of NPLs, and any discrepancies related to certain clauses of the loans (e.g., floor clauses, abusive clauses) shall not cause the relevant loan to be deemed a disputed claim for the purposes of Article 1,535 of the Spanish Civil Code. These clarifications will significantly help the management of large portfolios of NPLs by investors, as one of the main strategies implemented by debtors was precisely to claim the exercise of this right, even if the legal requirements to do so were not met.

Finally, Law 5/2019 on real estate credit agreements establishes that real estate lenders are those entities (other than banks) that are engaged in the activity of regularly granting (or intermediating in the origination of) mortgage loans over residential assets or real estate-related loans to consumers, and these real estate lenders should register with the Bank of Spain. The Bank of Spain published a Q&A document that included an expansive interpretation of the concept of real estate lenders, which could potentially include the acquirers of secured NPL portfolios. This interpretation could trigger land registries to reject the registration of mortgages in favour of NPL acquirers that are not registered as real estate lenders with the Bank of Spain. Directive 2021/2167 on NPL servicers (not yet implemented in Spanish law, but the implementation term ends in December 2023) establishes that NPL purchasers cannot be subject to authorisation or registration, unless required by national consumer protection regulations. Hopefully the implementation of this Directive may provide a clear pattern to avoid the registration of secured NPL purchasers with the Bank of Spain (establishing that the servicer registration in the relevant public registry will suffice) and reduce the discussions with land registries. Having said that, the majority of the land registries are currently taking the position that, for the transfer of the mortgage loans to be registered in favour of the acquirer, either:

a the servicer in charge of the enforcement of the NPL must be recorded at the registry of companies involved in the mortgage loan market created by Law 2/2009 or at the real estate lenders registry created by Law 5/2019; or

b the judicial enforcement of the NPL has already commenced.

VII OTHER ISSUES

There are no other issues of note at present.

VIII OUTLOOK AND CONCLUSIONS

The ongoing conflict in Ukraine and its negative consequences (including the increase in commodity prices, inflation rates and disruption in supply lines), alongside the tightening of financial markets and the increase in interest rates, are expected to continue impacting growth prospects. Spanish GDP is projected to grow by 1.6 per cent in 2023 (versus the 5.5 per cent growth rate experienced during 2022).

The anticipated change in the monetary policy stance in advanced economies to curb the rise in the inflation rate may have a positive effect on bank profitability. However, Spanish financial institutions, as well as other EU financial institutions, are still facing other historical challenges owing to, among other things, regulatory pressure, the need to adapt to a growing digital environment and the existence of other sources of financing (including alternative lenders and fintech companies), which are becoming real competitors to traditional bank lending, not only for large multinational Spanish companies but also for SMEs. Banks will have to monitor very closely the effects that these challenges may have on their businesses and activities and manage their response to innovation and new competition simultaneously with the completion of their own reorganisation processes, focusing on their traditional business and continuing with the divestment of their non-core assets.

The extent of the economic crisis and the way that Spanish banks handle the current challenges will determine lending and secured finance volumes for 2023. Banks will need to anticipate and manage potential risks and identify new opportunities that may arise in the near future. Liquidity needs arising from the current economic situation are still expected to grow. Likewise, as the insolvency moratorium is lifted, volumes of restructuring transactions are expected to increase. If traditional banks are not able to close the funding gap by themselves, an opportunity may arise for alternative and opportunistic lenders to enter into rescue financing, restructuring and leveraged deals.

Conversely, some sectors such as energy, telecoms, infrastructure, IT and digital businesses will continue to thrive. Deals related to these core sectors are expected to continue during 2023 (albeit perhaps at a slower rate than in previous years).