GLOBAL FINANCE NEWSLETTER

RENEGOTIATION OF MORTGAGE LOANS:

THE NEW PROVISIONS INTRODUCED BY DECREE N. 138/2011

On 5 May 2011 the Italian government approved the law-decree n. 138 containing urgent measures regarding economy (the "**Development Decree**"), which has not yet been published on the Official Gazette. The Development Decree has introduced, *inter alia*, new provisions concerning the renegotiation of the mortgage loans.

These new provisions (article 8, paragraph 8, of the Development Decree) would become a part of those measures which grant suspension of loan instalments in favour of families (*Piano Famiglie*) and small and medium enterprises (*Avviso Comune*), in order to help borrowers in financial distress.

1. RENEGOTIATION OF MORTGAGE LOANS

Article 8, paragraph 8, of the Development Decree introduces the right for the borrowers to renegotiate their mortgage loans: specifically, upon their request, the relevant lender will be obliged to renegotiate the mortgage loan, provided that the requirements established by the Development Decree are satisfied.

More specifically, pursuant to article 8, paragraph 8, of the Development Decree, borrowers who, before the entry into force of such new provisions, have executed or assumpted a mortgage loan agreement, also after splitting up of the loan, have the right to renegotiate the terms of their mortgage loan with the relevant lender, provided that:

(i) the relevant mortgage loan agreement has been entered into for purchasing or rebuilding a residential property;

(ii) the original amount of the relevant mortgage loan is not higher than Euro 150,000;

(iii) the relevant mortgage loan accrues interest at a floating rate and provides for payment of variable instalments for the whole duration;

(iv) the relevant borrower submits, together with the request of the renegotiation, the certificate of the relevant ISEE (*Indicatore della Situazione Economica Equivalente*), which should not exceed the amount of Euro 30,000;

(v) no late payments have been made with respect to the relevant mortgage loan.

1.1. EFFECT OF THE RENEGOTIATION

<u>Replacement of the floating interest rate with a fixed interest rate</u>

The renegotiation of a mortgage loan involves the change from a floating rate to a fixed nominal annual interest rate which must not be higher than the interest rate obtained by applying (i) the lower between the 10-year Euro IRS and the IRS in Euro applicable to a duration equal to the residual life of the mortgage loan or, if not available, the quotation of the IRS related to the immediately preceding duration, as it appears on Reuters ISDAFIX 2 page at the renegotiation date, <u>plus</u> (ii) a spread equal to the one indicated in the relevant loan agreement, for the purpose of determining the applicable interest rate.

<u>The effect on the existing mortgages</u>

The renegotiation of a mortgage loan does not involve the novation on the mortgage securities originally created to secure the loan. In particular, the Development Decree provides that the mortgage securities originally created with respect to a loan which is being renegotiated, shall continue to secure the debt over the original expiry date of the loan, without the need of any additional formality or annotation.

1.2. EXTENSION OF THE AMORTISATION PLAN

The borrower and the lender will be entitled to agree that the renegotiations will extend the amortisation plan of the mortgage loans for a maximum period of five years, provided that the residual life of the relevant mortgage loan, following the date of such renegotiation, does not exceed twenty-five years. The possibility to extend the amortisation plan of the mortgage loans has been introduced to reduce the possible increase of the instalment amount upon change from the floating rate to the fixed rate becoming effective.

2. Renegotiation of securitised mortgage loans

The Development Decree explicitly refers to renegotiation of securitised mortgage loans.

In this respect, article 8, paragraph 8, items (d) and (e), provides that:

(i) the provision relating to the remaining in force of the mortgage securities originally created to secure the mortgage loan which is being renegotiated (see paragraph 1.1 above), also applies to the loan granted by the lender to the borrower, as assigned debtor, in the context of a securitisation transaction or issuance of covered bonds, in order to permit the loan repayment in accordance with the applicable amortisation plan at the time of the renegotiation. In these cases, the lender will be subrogated in the relevant mortgage securities, without the need of any additional formality or annotation, but such subrogation will be not effective until the claims of the assignee (i.e. special purpose vehicle for securitisation transactions "**SPV**"), deriving from mortgage loans which have been transferred in the context of a securitisation transaction or issuance of covered bonds (article 8, paragraph d), Development Decree) are fully satisfied;

(ii) if the lender, in order to carry out the renegotiation, repurchases the claim previously transferred in the context of a securitisation transaction or issuance of covered bonds, the relevant assignee shall give notice of such repurchase through the publication in the Italian Official Gazette, even by mean of a single notice relating to all of the claims repurchased by the lender/assignor. Any security interest, lien or encumbrance created in favour of the lender/assignor, shall continue to be in force and effect and shall have the same ranking, without the need of any additional formality or annotation (article 8, paragraph 8, item e), Development Decree).

3. Some Considerations

(i) <u>Scope of the provisions</u>

Listed here below, some considerations regarding the scope of application of the provisions on the renegotiation of the mortgage loans:

Specifically:

(a) the provision according to which borrowers, in order to be allowed to renegotiate, must have entered into a mortgage loan for purchasing or rebuilding a residential property, might raise doubts, due to the very specific purpose that each loan shall have, with regard to the applicability of the Development Decree to the mortgage loans granted in order to carry out the subrogation under article 8 of Legislative Decree n. 7/07 (*Decreto Bersani*), and article 120-*quater* of the Italian consolidated banking act (*Testo Unico Bancario*). In this respect, it has to be noted that the purpose of such loans seems to be a refinancing purpose rather than a purchasing or rebuilding one.

(b) The provision according to which, in order to be allowed to renegotiate the mortgage loans, it is necessary that the relevant mortgage loan accrues interest at a floating rate and provides for payment of variable instalments for the whole duration, might raise doubts, due to the fact that it is unclear whether such provision refers solely to the residual life of the mortgage loan (or to its original duration as well), regarding the applicability of the Development Decree's provisions with respect to the mortgage loans which do not have a floating rate and variable instalments at the date of disbursement (but did become floating rate and variable instalments mortgage loans as a result of a previous renegotiation).

(c) Moreover, the provision according to which, only mortgage loans in respect to which no late payments have been made at the date of the request of renegotiation could be renegotiated, may raise doubts, considering that, as textually drafted, such provision seems specifically to exclude loans in respect of which late payments have been made in the past but are in line with payments at the date of request of renegotiation.

(ii) <u>Effects of the securitisation</u>

With reference to the renegotiation of mortgage loans which claims have been securitised, according to the provisions of article 8, paragraph 8, item a), d) and e) of the Development Decree, and specifically taking into consideration the following:

(a) the provision of article 8, paragraph 8, items a) and c) explicitly provides that any borrower has the right to enter into renegotiations with the "lender" (not making any reference to different entities, such as the possible assignees);

(b) the provisions in which reference is made to mortgage loans object of securitisation transactions (article 8, paragraph 8, item d) and e)) expressly indicate the following actions that might be carried out with respect to such securitised claims:

    (1) an additional loan that might be granted to the borrower/assigned debtor in order to allow such borrower/assigned debtor to renegotiate its mortgage loan; and

    (2) the repurchase of the securitised claims by the lender in order to carry out such renegotiation.

It seems reasonably to argue that (also in compliance with the recent measures granting the suspension of loan instalments in favour of families (*Decreto Milleproroghe*[1]) and small and medium enterprises

[1] As a matter of fact, such rules have held the SPV harmless from the negative consequences deriving from the facilitations granted to the borrower, providing that the relevant charges shall be borne by the lenders.

(*Avviso Comune*), that the aims of the Development Decree in this respect are the following:

(i) to have the SPV not involved in the renegotiation activity pursuant to the Development Decree nor bearing the consequences deriving from the renegotiation (i.e. the payments received from the SPV shall not be affected by the renegotiation);

(ii) without prejudice to (i) to procure that the lenders (assignors) are obliged to ensure that the borrowers whose mortgage loans have been securitised are granted the same rights of renegotiation as the borrowers whose mortgage loans have not been securitised . To this purpose the lenders have been granted with relevant instruments to achieve this goal (i.e. the survival of the original mortgage in case of refinancing or repurchase – and relevant renegotiation - of the securitised mortgage loans).

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