

## TRADE ALERT

June 2017, Issue 42



## SPAIN

**BANCO POPULAR ESPANOL SA ("Popular")** reported gross non-performing assets of **EUR 37.4bn in FY2016** and was noted as having the highest NPL burden in Europe. On 6

June 2017, the European Central Bank ("ECB") determined that Spain's sixth largest lender, **was failing or likely to fail**<sup>1</sup>.

This statement from the ECB resulted in the [Single Resolution Board](#) ("SRB") placing Popular under resolution and approving the measures to be implemented by the FROB (Spain's national resolution authority).

**RESOLUTION, WRITE-DOWN AND CONVERSION**

Firstly, Popular's share capital valued at **EUR 2,098,429,046** was written down to zero euros (€0).

Secondly, the power to execute the conversion and subsequent write down was applied to the **EUR 1.35bn of Additional Tier 1 capital instruments**, by converting them into shares of EUR 1.00 each then writing them down to zero euros (€0) and establishing a non-distributable voluntary reserve. Simultaneously, the **EUR 684,024,000 Tier 2 capital instruments** were converted into newly issued Banco Popular shares of EUR 1.00 par value each, which were subsequently sold on 7 June 2017 to **BANCO SANTANDER SA ("Santander")** for a total of EUR 1.00.

**LITIGATION CLAIMS**

Under Article 86 of Regulation (EU) No 806/2014, **proceedings** may be brought before the **European Union's Court of Justice** contesting the resolution scheme **within two months** of publication of the resolution. There is a filing deadline of **one month** for an appeal for a reversal of the implementation of the SRB resolution by the FROB<sup>2</sup>.

For more information on the write down and conversion: [click here](#) for [Q&A](#) from the SRB and [click here](#) for the Resolution of the FROB Governing Committee implementing the SRB decision.

A secondary market has already arisen in trading the claims related to the resolution measures, which Bloomberg refers to as a "[lottery ticket for traders](#)". There are various potential litigation options being considered, including potential claims against the SRB or the FROB in relation to the resolution measures themselves, as well as potential claims against Banco Popular's directors, auditors and sellers of bonds.

The various litigation options are still under review however, and buyers should be careful to confirm when purchasing rights to a claim that such rights are transferable, as the holder on 7 June 2017 is the party with legal standing to bring a claim and that

[Contacts](#)**LMA UPDATED TERMS AND CONDITIONS****"GO LIVE" 27 June 2017****SALE OF BANCO POPULAR:****IMPACT ON CREDIT DERIVATIVES MARKET**

The acquisition of Banco Popular has also had an impact on the credit derivatives market. The **effect of the SRM's intervention under credit default swap transactions ("CDS")** will depend on whether the relevant trade is documented under the **2003 or 2014 ISDA Credit Derivatives Definitions**; only the latter reflects fully the new regularity intervention powers with respect to European financial intuitions – including a **new Credit Event for government bail-ins** and **revised deliverable obligation provisions to provide for 'asset package' delivery**.

On **9 June 2017**, the International Swaps and Derivatives Association, Inc. ("**ISDA**") announced that its EMEA Credit Derivatives Determinations Committee ("**EMEA DC**") [had resolved as follows](#):

1. for the purposes of the 2003 ISDA Credit Derivatives Definitions, **a Restructuring Credit Event has occurred** with respect to Banco Popular (in respect of senior transactions and subordinated transactions); and
2. for the purposes of the 2014 ISDA Credit Derivatives Definitions, **a Governmental Intervention Credit Event has occurred** (in respect of subordinated transactions).

The **date of the Restructuring Credit Event and the Governmental Intervention Credit Event** with respect to Banco Popular, in each case, was determined to be **7 June 2017**. The EMEA DC also decided to hold auctions to settle relevant transactions, though it is not yet clear which obligations will be deliverable in the auction. **Trades under the 2003 ISDA**

may be lost on an assignment.

Depending on the relevant claim, it may also be necessary to confirm when the seller purchased the bonds and what information it relied upon at that time.

For more information on selling or purchasing Banco Popular claims, contact:



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## THE SPANISH NPL MARKET

In the wake of the resolution of Banco Popular, Spain continues to be a focus for the EU Council's Financial Services Committee which recently published a [report](#) on the status of non-performing loans ("NPLs") across different Member States. It highlights the success of some of the measures implemented by Spain, including the Spanish asset management company ("SAREB"), the "bad bank" to which **EUR 51bn** (net book value) of exposures have been transferred.

Various reforms to reduce the stock of NPLs have been implemented since 2012 by way of executive legislation (Royal Decree-laws). Such measures provide liquidity and support to banks, change provisioning requirements and amend the supervisory and regulatory architecture.

Deloitte reports however, that Spain is lagging behind the UK and Ireland in deleveraging, with local banks currently holding around **EUR 120bn of NPLs** (excluding REOs<sup>3</sup>). Further sales activity is expected in 2017 with a more diverse asset class, including secured SME and corporate exposures, against the backdrop of an improving real estate market and positive economic outlook.

This month's trade alert considers some of the key legal issues for loan investors in Spain.

### REGULATION AND BANKING LICENCE REQUIREMENTS

There is **no licensing requirement** for lending in Spain. However, certain banking activities (such as taking deposits) may require authorisation from the **Bank of Spain** ("BoS"), the **National Securities Market Commission** ("CNMV") or the **Spanish Economy Minister**.

Provided they are registered with the BoS, credit institutions authorised to lend in another Member State are entitled to lend in Spain in accordance with **European Union passporting rules**.

**Credit Derivatives Definitions do not have an "asset package delivery" option** - which **may distort the valuations** where Santander's bonds (Santander being the successor of Banco Popular) get delivered.

For further information on the sale of Banco Popular and how this has impacted the CDS market, please contact [Assia Damianova](#).

### ENGLISH COURT OF APPEAL CONFIRMS PRIMACY OF CHOICE OF GOVERNING LAW IN ISDA MASTER AGREEMENTS

On **15 June 2017** the English Court of Appeal handed down a significant judgment in ***Dexia Crediop S.p.A v Comune di Prato*** (*Dexia Crediop SPA v Comune Di Prato* [2017] EWCA Civ 428 (15 June 2017)). The court's unanimous judgment confirmed that the nature of an agreement made pursuant to an ISDA Agreement will be sufficiently international in character to prevent the application of any mandatory rules of local law.

[Click here](#) for the Cadwalader Clients & Friends Memo.

### BANKIA MERGES WITH BANCO MARE NOSTRUM

On **27 June 2017**, **Bankia S.A.** agreed to acquire **Banco Mare Nostrum** ("BMN") by way of an all-stock "merger by absorption".

As part of the deal, Bankia will issue **205.6m new shares to the shareholders of BMN**, equivalent to **6.7% of its post-merger capital**. The offer values unlisted BMN at 0.41 times its book value ([EUR 825mn](#)).

Both banks are **majority state-owned**, having been bailed out at the height of the financial crisis. Bankia received **EUR 22bn** of state aid, while BMN received **EUR 1.65bn**. Spain's bank rescue fund is expected to hold [around 67% of the resulting entity](#). The FROB gave the go-ahead for the deal back in March, concluding that the tie-up was "[the best strategy to optimise the recovery of State aid](#)".

According to a [report on the merger produced by Bankia](#), the transaction will reinforce Bankia's position as **Spain's fourth largest lender**, leaving it with total assets worth [EUR 223bn](#). The integration of BMN sees Bankia's **gross loans increase by 20% and deposits increase by 28%**.

The merger forms part of a [wider consolidation trend](#) within the Spanish

## METHODS OF TRANSFERRING LOANS

In Spain, **loans are typically transferred by way of assignment**. The transfer is normally effected using a Spanish law assignment agreement which transfers the assignor's rights and obligations in the loan to the assignee. Notably, **transfer by novation is usually avoided in Spain**.

**Novation will result** in the original agreement being extinguished and a **new contract being formed**. A transfer by novation therefore carries a risk of **releasing existing security** or guarantees.

**Participation agreements are valid in Spain**. These are typically private agreements between the grantor and the participant where the grantor remains the lender of record. However, **Spanish syndicated loan facilities** will often **restrict the ability of lenders to transfer a loan via sub-participation**.

In Spain syndicated loan facilities typically require that an assignment does **not result in any costs (including withholding tax) being incurred by the borrower**. Funds may choose to acquire debt via an EU based special purpose vehicle ("**SPV**") in order to mitigate possible adverse tax consequences.

## FORMALITIES AND CONSENT

There is **no legal requirement to notify the borrower** (or guarantor) that a loan has been transferred **in order for the transfer to be effective as between the transferor and transferee**. However, **where a borrower has not been notified** of the transfer, any **payments made to the transferor** by the borrower will be deemed valid for the purpose of satisfying its obligations under the applicable loan agreement. Once a borrower has been notified of the transfer, payments made to the previous lender (rather than the transferee) will not be deemed to fulfill borrower obligations under the credit agreement.

Where there are **multiple debtors** under a credit agreement, the following notification rules apply: (i) in the case of "joint" debtors each debtor must be notified separately; and (ii) where debtors are "joint and several", any of the debtors may be notified in order for valid notice to have been given.

Other than as may be expressly provided in the loan documentation, there are **no additional borrower consent requirements under Spanish law**.

## SECURITY AND TRUSTS

**Trusts are not a recognised legal concept** in Spain. In addition, **Spain is a civil law jurisdiction** which **does not recognise**, in general terms, a difference between **legal and beneficial ownership**.

In Spain, **security interests are generally granted in favour of all lenders and not only to the security agent**. Security is **accessory to the debt** in Spain. Prospective lenders acquiring a loan by way of assignment will therefore take the **benefit of any existing security arrangements** (and guarantees) by operation of the law.

Unlike some common law jurisdictions, the **security agent will not be able to act on behalf of all lenders as a trustee**. Although the market is exploring alternative solutions, **lenders**

banking sector, with the market now dominated by Spain's four major banks: **Santander, BBVA, Caixabank and Bankia**.

## REALIA

On 27 April 2017, **Realia Business S.A., the Spanish real estate company controlled by Mexican business magnate Carlos Slim, refinanced a syndicated loan** worth [EUR 678mn](#) that was due to mature on 27 April 2017. Realia's Q1 [financial results](#) published on 8 May 2017 include information regarding the execution of the **new 7 year term loan** in the amount of **EUR 582mn**.

## ITALY

### INTESA SANPAOLO RESCUES BPVI AND VENETO BANCA

On **23 June 2017** the **ECB** named **Banca Popolare di Vicenza ("BPVI")** and **Veneto Banca** as *failing or likely to fail*.

Unlike in Spain, where the SRB intervened, the ECB determined that resolution action by the SRB **was not warranted in the circumstances**. As a result, **Italian authorities were required to wind down the bank using national insolvency laws**.

The **European Commission** has now [approved Italian measures](#) to facilitate a sale of some of the banks' businesses to Italy's largest retail bank, **Intesa Sanpaolo ("Intesa")**.

BPVI and Veneto Banca will be **wound up and exit the market**, while selected assets and liabilities (excluding NPLs, subordinated bonds and shareholdings) are to be transferred to Intesa. The plan sees junior creditors (with debts amounting to around EUR 1.2bn) and shareholders (EUR 4bn) wiped out whilst senior bondholders [are protected](#) from losses.

The deal has [caused controversy](#), not least because of the large amount of taxpayer's money needed to implement it – amounting to nearly **EUR 17bn**. As part of the Commission-approved deal, the Italian State has agreed to provide the following:

- (i) cash injections of about [EUR 4.785bn](#) for **Intesa**;
- (ii) [EUR 400mn](#) in guarantees in respect of Intesa acquired loans which may 'turn bad'; and
- (iii) additional guarantees of up to [EUR](#)

**under a syndicated loan will need to accept the security interest before a Spanish notary** in order to take the benefit of such security.

Lenders should be aware that **where existing security is registered** (as is the case for mortgages and non-possessory pledges) the assignment of any security arrangements will also need to be registered in order for the new lender to enforce the security directly. **Where security has not been re-registered**, enforcement may **only be available via the security agent**, which can be problematic in Spain.

If acceptance of the security by all lenders is not possible, **alternatives are available**, including **granting the security to the security agent for the benefit of and on behalf of all the lenders**. However, whether such drafting is sufficient remains to be seen. **Parallel debt structures** are also being explored as a possible alternative in Spain.

The **safest approach** for lenders is therefore to ensure they have a **direct contractual right to the benefit of any security granted by the borrower(s)**.

In addition, it should be noted that funds cannot benefit from **floating mortgages** in Spain, and particular care needs to be taken in the review of **mortgage backed loans**.

#### **ENFORCEMENT OF SECURITY**

In order to enforce on behalf of a lender, the security agent will need to show that it has been **duly empowered** to do so. This requirement is usually satisfied by lenders providing the security agent with a **notarised and apostilled power of attorney ("POA")** which expressly authorises such enforcement.

**Spanish law prohibits creditors from having an automatic right to keep property given as security or collateral if the debtor fails to pay**, except in certain specific cases (i.e. when the collateral is cash, or other liquid instrument). As a result, **foreclosure** must take place **through a public sale** of the secured property, normally through a **formal auction procedure**.

It remains unclear whether funds can benefit from the **expedited enforcement process** available under the **Financial Collateral Directive (Royal Decree 5/2005)**. If courts decide that funds are unable to take advantage of this quicker enforcement process, funds will need to enforce under the ordinary enforcement procedure.

#### **WITHHOLDING TAX**

Interest paid to a **non-resident lender** is generally subject to a **19% withholding tax** unless (i) the rate is reduced by virtue of a **tax treaty** between Spain and the jurisdiction of the non-resident lender or (ii) the interest is paid to a **resident in another EU Member State**, provided that such non-resident lender, being the beneficial owner of the interest, does not operate in Spain through a permanent establishment and is **not resident in a "tax haven"** (for the purpose of Royal Decree 1080/1991 of 5th July).

#### **STAMP DUTY, TRANSFER TAX AND VAT**

The transfer of a loan is **not generally subject to stamp duty where the transfer is not a registrable transaction**.

[12bn](#) to cover potential losses from the two banks' bad loans.

Whilst the deal was structured in accordance with **rules on state aid for banks**, many are now calling for **further reform**. In Germany, the government has called for measures to prevent states **circumventing creditor bail-in rules** when giving state aid to a bank.

[Italy's financial sector is plagued by a surfeit of bad loans](#). The **total stock of NPLs** held by Italian banks is estimated to be [roughly EUR 331bn](#).

#### **CADWALADER ARTICLE ON ROUST RESTRUCTURING**

The **Roust Corporation** successfully completed its **USD 1.1bn** restructuring in February 2017.

It is particularly noteworthy due to the contribution of **significant new value in kind**, which was achieved through the **merger of a distinct business entity owned by Roust's controlling shareholder into the reorganised Roust Corporation**. In exchange for their contribution of a strategic and highly valuable asset, Russian Standard Vodka and all related intellectual property, certain Roust affiliates received 57% of the equity in reorganised Roust.

[This article](#) provides additional information regarding the USD 1.1bn reorganisation of Roust Corporation in the United States Bankruptcy Court for the Southern District of New York. **Cadwalader acted as transatlantic adviser to the Ad Hoc Committee of Convertible Noteholders**. Please contact [Richard Nevins](#) or [Cort Malmberg](#) for additional information.

#### **LOAN MARKET ASSOCIATION UPDATES**

On **13 June 2017**, the **Loan Market Association ("LMA")** published revised versions of the **Standard Terms and Conditions and User Guide** on the pending page of the [LMA website](#).

The LMA revisions remove the Pricing Panel mechanism for resolving disputes over the reasonableness of the Buy-in/Sell-out ("**BISO**") purchase price. Instead, the Terms and Conditions will require the party entering into the substitute transaction to do so on arm's length terms and in good faith. In addition, the purchase price for the substitute transaction must be reasonable in the circumstances.

However, where the **security for the loan is real estate** (or any other type of security that is registered with a Spanish public registry) **stamp duty will be applicable on the notarial deed formalising the transfer.**

The **tax base** is the maximum guaranteed amount of the loan outstanding. The tax rate may **vary across different regions** in Spain **between 0.5% and 2.5%**, depending on the region.

In general, save in instances where loans are transferred between individuals, loans transfers are **subject to VAT rather than any transfer tax.** However, loan trading is typically treated as **exempt from VAT** under Act 37/1992 of 18th December.

### **INSOLVENCY LAW AND RISKS FOR INVESTORS**

Key changes were made to the Spanish insolvency Act ("SIA") in 2014 and 2015. The aim of the reforms was to **increase the efficiency and legal certainty in insolvency procedures** in addition to ensuring a swift resolution for viable and non-viable debts.

The reforms aimed to strike a proper balance between creditors and debtors and focused on the following:

- (i) **enhancing out-of-court agreements;** and
- (ii) **the simplification of in-court insolvency procedures.**

Investors should be aware of the following insolvency risks when trading in Spain:

**Clawback Regime:** Under section 71 of the SIA, **certain acts and contracts can be rescinded where entered into two years before the declaration of insolvency.** Rescission may apply where the acts or contracts are **detrimental to the insolvency estate.** There is a presumption that certain acts will be deemed harmful to the insolvency estate, including in cases where security is created in favour of 'related parties' or where non-matured secured debt is pre-paid.

**Equitable Subordination:** If a creditor is a 'related party' of the debtor, its **claims may be subordinated** under the SIA. Related parties include family members, directors and shadow directors, shareholders holding at least 5% (if the insolvent company is listed) or at least 10% (if the insolvent company is not listed) of the share capital of the insolvent company and companies belonging the same group.

**Contentious Credits:** Where a **debt is the subject of litigation**, and the claim against the debtor is sold to a third party, the debtor may have a **right to cancel the debt by paying the purchase price for which the claim has been sold**, along with any litigation costs incurred by the purchaser and any interest payable in respect of the purchase price.

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#### **Special Note**

*Special thanks to **Miguel Lamo de Espinosa Abarca** and **Álvaro Sáinz Ruiz** of [GÓMEZ-ACEBO & POMBO Abogados, S.L.P.](#) in Spain, who assisted us with this Trade Alert.*

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The updated documents and redlines showing changes are available to LMA members on the [website](#) and "went live" as of **27 June 2017**; therefore, any trades concluded on or after this date will be subject to the **new Standard Terms and Conditions.**

### **ICELANDIC UPDATE**

#### **GLITNIR HOLDCO EHF**

##### ***Optional Cash Redemption Notice – 1 June 2017 and Temporary halt of transfers from 17 May 2017 to 1 June 2017***

Glitnir Holdco ehf. effected an optional redemption of the Amortising Zero-Coupon Convertible Notes due 2030 (the "**Notes**") in part on 1 June 2017 in accordance with Condition 6.3(A)(ii). The aggregate principal amount of each Noteholder's interest in the Notes was reduced accordingly as a result of such redemption. Noteholders who wish to confirm the principal amount outstanding in respect of their holding of Notes can do so through the Glitnir secured website.

For a more in depth review of Glitnir's updates, please [click here](#).

#### **LBI EHF.**

On 2 June 2017 LBI ehf. issued a notice of a scheduled payment to be applied in partial redemption of the Notes on the Payment Date of 15 June 2017. The final amount of Euro Equivalent Available Cash that was paid on 15 June 2017 was EUR 43,615,742. Convertible Notes previously returned to LBI due to the final rejection of claims for EUR 1,934,784 were cancelled before the scheduled payment. The aggregate principal amount of the Convertible Notes outstanding immediately following the Payment is EUR 962,798,981.

For further updates, please [click here](#).

#### ***Landsbankinn Fully Repays Remaining Bond Owed to LBI***

On 22 June 2017, Landsbankinn fully prepaid the outstanding balance under Bond Series 2024 of USD 160mn and has thereby fully repaid all outstanding Bonds owed to LBI. The prepayment totals USD 161.33mn, including accrued and unpaid interest (EUR 144.7mn).

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- <sup>1</sup> Under the circumstances described under Article 18.4(c) of Regulation (EU) no 806/2014, determining that the entity is, or will, in the near future, be unable to pay its debts or other liabilities as they fall due.
  - <sup>2</sup> Under Articles 123 et seq of Law 39/2015 of 1 October on the Common Administrative Procedure of Public Administrations, giving one month from the day after the Resolution is published.
  - <sup>3</sup> Real Estate Owned properties on the books of the bank following foreclosures.