

Alert | Banking & Financial Services



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A Sigh of Relief for NPE Investors: Italian Supreme Court Passes Ruling on Land Loan Agreements (*Mutui Fondiari*)

The Supreme Court confirms that land loan agreements and relevant mortgages are valid even if the 80% LTV drawdown is exceeded.

On 16 November 2022, in Decision No. 33719, the Italian Supreme Court appear to have ended the nearly decade-long case law dispute on the consequences of a breach of the 80% financeability threshold of land loan agreements entered pursuant to Article 38 of Italian Consolidated Banking Law (TUB)¹.

This decision is of material importance to both banks and investors in the NPE (non-performing exposure) market who envisaged their “secured” investment being considered null and void and therefore fully unsecured.

In short, *mutui fondiari* are mortgage loans where both lender and borrower benefit from certain specific rights (e.g., shorter clawback, rights on enforcement, limitations on termination). Bank of Italy regulations provide that a *mutuo fondiario* must have on drawdown a loan-to-value ratio (LTV) not

¹ Art. 38 co. 2. TUB: “The Bank of Italy, in accordance with the resolutions of the CICR, shall determine the maximum amount of financing, identifying it in relation to the value of the mortgaged property or the cost of the works to be performed on the same, as well as the cases in which the presence of previous mortgage registrations does not prevent the granting of financing.”

exceeding 80%; the issue the Supreme Court considered related to this specific point. The borrower in the case claimed that because the LTV had been exceeded, the loan (and the mortgage) was null and void.

Indeed, the Supreme Court has stated (hopefully) once and for all **that exceeding the financeability limit pursuant to Article 38(2) TUB:**

- 1. does not invalidate the validity of the land loan agreement,**
- 2. does not allow the court to re-qualify *ex officio* the land loan agreement into an ordinary loan agreement,**
- 3. affects neither the validity nor the enforceability of the mortgage securing the loan agreement.**

In particular, the Italian Supreme Court has deemed that:

“with regard to land loan agreements, the financeability limit set forth in Article 38, paragraph 2, of Legislative Decree No. 385 of 1993, shall not be considered an essential element of the agreement, as it is not a provision that defines the content of the agreement itself nor ensures its validity, but a merely specific or supplementary element; the provision is not a mandatory rule - such as the provision through which the Italian law maker has empowered the Bank of Italy to set the financeability limit as part of ‘prudential supervision’ (see Articles 51 et seq. and 53 of the Consolidated Banking Act) - the breach of which, if set as a basis for the nullity (and invalidity) of the agreement (in this case, of the loan already disbursed, which should also entail the loss of the mortgage guarantee), would lead to the result of undermining the very interest that the rule was intended to protect, which is that of the bank's capital stability and the containment of risks in the credit activity”;

*“where the parties have intended to enter into a land loan agreement fulfilling the legal standards (i.e. medium or long-term financing granted by a bank secured by a first degree mortgage on real estate assets), given that their common intention to that effect is undisputed (or, if disputed, ascertained by the judge), the court is not entitled to re-qualify the agreement *ex officio*, for the purpose of neutralizing the legal effects of the type or sub-type of agreement legitimately chosen by the parties in order to bring it back to the general type to which it belongs (ordinary loan) or to different types of agreement, even in the presence of a challenge to its validity in terms of the exceeding of the limit of financeability, which implicitly assumes the correct qualification of the agreement in terms of a land loan agreement”.*

The Supreme Court’s decision may provide comfort to investors in the market willing to invest in non-performing loans originating from land loan agreements, the validity of which—as well as the validity of the related mortgage guarantee—is no longer being disputed, thus allowing operators to pursue their investments with a greater level of certainty.

Authors

This GT Alert was prepared by:

- **Corrado Angelelli** | + (39) 02.771971 | Corrado.Angelelli@gtlaw.com
- **Dante Campiverdi** | + (39) 02.771971 | Dante.Campiverdi@gtlaw.com
- **Rodrigo Francisco Santini** | + (39) 02.7719771 | Francisco.Santini@gtlaw.com

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