Adieu to ceiling mortgage

Representatives of many industries involved in real estate investments will undoubtedly be pleased with the changes that are to take effect as a consequence of a statute that was passed into law this past summer – Act Amending the Act on Land and Mortgage Registers and Other Statutes of 26 January 2009 (hereinafter referred to as the "Amending Act").

The Amending Act introduced many important systemic solutions with respect to mortgage as security for debt, which will lead to a certain revolution in mortgage regulations that have been in force for over a quarter of a century.

Because of the very broad scope of the amends, which will have significant bearing on many participants of legal trade, the Amending Act will come into force 18 months as of it being passed into law, thus as on 20 February 2011. However, it is worthwhile even now to look at the scope of the changes which the Amending Act will introduce in order to properly prepare for future financial investments.

Firstly, the amendment will do away with the differentiation of mortgages into regular and ceiling mortgages. At present, the rule is that an regular mortgage is established to secure existing debts of defined amount while a debt of unknown amount can be secured with a ceiling mortgage (Art. 68 and Art. 102 of the current statute). This usually means that a creditor has to establish two mortgages on a single piece of real estate: an ordinary mortgage to secure the principal debt and a compulsory deposit mortgage to secure the payment of interest accrued on the principal debt, enforcement costs, etc. To establish such mortgages, the petitioner must submit two mortgage applications and incur the costs of two court fees (with these costs usually incurred by the already "indebt" debtor).

Some take the view that the principal debt and future debts (e.g. interest on the principal debt) are treated jointly as one debt of undefined amount and as a consequence it may be secured by a single ceiling mortgage. Yet, this approach has been criticized by some representatives of the doctrine as well as its practitioners.

Such a divide in approach to the grounds for establishing ceiling mortgages on entire the sum of a debt (principal debt and additional benefits such as interest) should cease with the coming into force of the Amending Act. As then the effective rule will provide that a mortgage can serve as security for a monetary debt as well as future debts. Thus thereafter creditors will establish only one type of mortgage which will serve as security for the principal debt as well as interest, enforcement costs and other future debts of undefined amount arising in connection with the principal debt, as long as they are listed in the document establishing the grounds for the entry of the mortgage into the Land an Mortgage Register. Only one application will have to be submitted and only one court fee paid. As a consequence, the entire Chapter 2 "Compulsory Deposit Mortgage", in Section II of the binding statute, will be deleted.

Another change which will be introduced by the Amending Act, which undoubtedly will be of greatest interest among banks financing investments jointly with other banks, will be the option to establish one mortgage to secure all debts of all banks participating in financing. The Amending Act has a new Art. 68^2 under which it will be possible for a pre-arranged mortgage to secure several debts owed to various entities, established to finance a single investment. As a natural consequence of the implementation of such a solution, it will be necessary to appoint a mortgage administrator in such situations.

Unlike the legal systems of other European states (which for example have a platform for the functioning of credit agents), to date the Polish system had not offered a comprehensive solution for the joint financing by several entities of a single investment (e.g. building of a residential estate). In addition, in this area the Polish system is not at all cohesive. The possibility of the appointment of one administrator has to date been provided only under Act on Registered Pledge and Pledge Register. As a result, pledge administrator is a party to agreements establishing a pledge, and thus acts on own behalf though for the benefit of other creditors. Today there is no such solution in place with respect to mortgages. This highly complicates any transaction in which the creditor side counts several entities financing an investment. In reality, they can only with respect to the performance of rights under the registered pledge appoint one entity from among them to exercise to their benefit the rights of the pledgee. On the other hand, as far as mortgages are concerned, it is necessary for individual mortgages to be established to the benefit of every single creditor, which once again inflates the costs incurred by the debtor (such us the costs of preparing additional representations on the establishment of a mortgage, costs of numerous court fees and applications, costs of preparing complete sets of attachments to several applications).

Thanks to changes put forth under the Amending Act, in the event of several entities financing a single investment, it will be possible to enter into an agreement under which a mortgage administrator will be appointed (from among the creditors or a third party, though most often it will undoubtedly be one of the creditors as the Act on Registered Pledge permits only the appointment of administrators from among the creditors). Agreement to Establish a Mortgage Administrator will have to be concluded in writing and will have to define the scope of security established for individual debts of entities advancing the financing. Furthermore, it will have to disclose what investment is being jointly financed by the creditors. Following the appointment of a mortgage administrator, the Land and Mortgage Register will disclose only the administrator and not the rest of the creditors as the entity with rights under the mortgage.

To note, a mortgage established to the benefit of an administrator, even if it is a bank, must be established in the form of a notarial deed as the Amending Act excludes from this scope Art. 95 of the Bank Law. The mentioned regulation is not fully consistent, given the general goal of the authors of the Amending Act to implement regulations that will lower the costs incurred by participants of legal trade.

Another novelty is the introduction of an option to manage a vacated mortgage entry. After Art. 101 of the current Act, the Amending Act will add an entire new Chapter 5 under which the property owner will have the option to decide on the establishment of a new mortgage in place of a vacated entry or on the transfer into that entry of any mortgage entered with a different ri-

ght of priority. This means that if a piece of real estate is encumbered by several mortgages of various rights of priority, then upon the expiry of a debt which was secured by a mortgage entered, for example, as the first, and its deletion from the Land and Mortgage Register, then, as long as concurrently with the deletion of the mortgage the owner enters his rights to manage the vacated mortgage entry to the Land and Mortgage Register, the owner will have the right in the future to register a mortgage in that vacated entry, and the mortgage will have the right of top priority to the benefit of a different creditor (added under Amending Act, At. 101[4]).

Changes introduced with the Amending Act will have a much wider scope than discussed above, however it is difficult to discuss them all in such a short article. Just to mention, however, among other important changes, we should not forget about the right of claim that will be awarded to the creditor whose real estate is encumbered by a mortgage, to reduce the sum of the mortgage if the mortgage security becomes excessively large. The parties will also be able to decide whether the total of the mortgage will be expressed in the same currency as the amount of the debt. It will also be possible to split a mortgage, and furthermore to replace the debt that has been secured by a mortgage with another debt of the same creditor.

The current regulations necessitate many complicated legal measures and often fairly advanced structures relating to the financing of building project, which increases the costs of the investments. Without a doubt, only the use of the provisions of the Amending Act will in practice give us an answer to the question of whether the new regulations will fully satisfy the participants of legal trade. Yet today I myself believe that the statue can comprise a material step forward for Polish standards to becoming aligned with requirements of modern commerce.

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