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Financial Regulation in Spain.

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Financial regulation in Spain

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Abstract: This paper analyses the regulatory framework of the financial system in Spain. Particular attention is paid to the adoption of the EU directives and the way they have been transposed to Spain from 1986 to present, including the regulatory developments in the last few years from the onset of the financial crisis. The Spanish case appears particularly interesting as it has shown one of the most significant transformations during the period considered in the structure of regulation. This paper surveys the implementation of the most important EU regulations since the early 1980s to present. Overall, the implementation has been successful and has been timely. The implementation has been particularly intense and fast in what the solvency regulation is concerned. However, some other regulations, in particular those concerning capital markets, have normally required more time to be transposed or have had to be gradually implemented. The financial crisis has brought a number of significant changes beyond EU regulations for Spanish banks and it has shown that there was still substantial room for improvement in supervision and prudential regulations. The reaction has been significant as the recapitalization and restructuring process, have brought a number of regulatory changes beyond EU Directives.

Key words: Financial regulation, Spain, EU Directives, crisis, restructuring.

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1. Introduction

This paper analyse the regulatory framework for the financial system in Spain. Particular attention is paid to the adoption of the EU directives on this matter and the way they have been transposed to Spain from 1986 to present, including the regulatory developments in the last few years from the onset of the financial crisis. The Spanish case appears particularly interesting as it has shown one of the most significant transformations during the period considered in the structure of regulation. Spain joins the European Community in 1986 and a significant adaptation is then required to the European directives and regulations. This process goes in parallel to the development of a number of liberalisation movements that were initiated in Spain since the late 1970s. Although this papers covers the regulatory initiatives that were confronted from 1986 onwards, in this introduction we make a brief analysis of the grounds of financial regulation in Spain before 1986 in order to provide a broader picture of the magnitude of the regulatory challenge that the country has faced since then.

The main reference for banking regulation before the liberalization process started was the Banking Regulatory Law of 1946. This law was characterized by intervention as it set strict controls and make banks became instruments of government industrial policy. The law of 1946 gave the Ministry of Finance ample discretionary powers to grant or to deny bank charters. Entry was at the discretion of the Ministry of Finance that used its authority rather arbitrarily. The era of easy entry came to an end. A new Banking Record Office was established. Only existing banks were allowed to register and to continue in the industry. Newcomers had to demonstrate the need for banking services in a specific geographic area. The banks' capital structure, its potential earnings, its management and the convenience and needs of the community were elements the new regulators considered before approving the establishment of a new bank. Furthermore, a favourable report of the Supreme Banking Council, also under the control of the government, was needed. Branching expansion depended on the financial density of each region, the existence of unattended financial demand or well proven insufficient financial services. The concession of branches was linked to the volume of capital and reserves of each bank. The larger the bank the higher the likelihood it had to obtain authorization to open a new branch. As a result, financial concentration increased.

As noted by Aceña et al. (2010), at that time, the Ministry set maximum and minimum interest rates on deposits and on loans. It also set in preferential rates for the so-called "priority industrial sectors". All banking operations were subject to controls. As for the structure of the financial system and its supervision and regulation, the main supervisory agency for banks was the Ministry of Finance for commercial banks and the Ministry of Labour for savings banks. The General Directorate of Banks and Stock Exchange, a technical department of the Ministry of Finance, was in fact the entity in charge of all supervisory tasks. This Directorate was responsible for the Banking Record Office. Other assignments included the inspection of banks, so that they fully comply with the official regulatory norms and the credit policy dictated by the government. In 1957 the Directorate was reformed and renamed General Directorate of Banks, Stock Exchange and Investment assuming also responsibilities over insurance companies and savings banks.

In 1962, the 1946 Banking Law was replaced by a new Banking and Credit Regulatory Law. The Bank of Spain was nationalized and old and new monetary instruments were put in place. Monetary policy, however, remained in the hands of the Ministry of Finance. This ministry kept its fully comprehensive powers over the financial system.

A first timid attempt towards deregulation began in 1969. Interest rates restrictions on long-term (two years or more) loans were lifted. Barriers to entry were loosened and branching restrictions were partially removed. These more relaxed chartering and branching policies enhanced competition. After 1974, deregulation speeded up. Discrimination between banks and savings banks were eliminated. Banking operations were liberalized and the obstacles to competition among financial institutions were progressively suppressed.

The late 1970s and early 1980s saw the largest failures of the Spanish financial system in the 20th century. Because of its depth and the number of institutions affected this crisis has been included in the group of the so-called recent "Big Five Crises" (see, for example, Reinhart and Rogoff, 2008). The resolution of the banking crisis imposed significant costs on the taxpayer. The total gross fiscal costs of the rescue operation were approximately 4-5% of GDP. Deregulation and competitive pressures were other causes of the banking crisis. The number of banks increased slightly after the partial liberalization of the 1962 law, reversing the steady decline of the previous period. Moreover, there was a rapid expansion in the number of branches at existing commercial banks following the liberalization of the authorization to establish branches.

The interventions on banks took place from 1977 to 1983. To provide limited guarantee to depositors and to have a quick and adequate mechanism to intervene banks a Deposit Guarantee Fund was established in November 1977.

In 1980 the Law of Governing Bodies of the Bank of Spain, transferred all responsibilities for bank supervision, discipline and sanctions to the central bank, that at the same time was given ample political autonomy. The following step came with the Autonomy of the Bank of Spain Law (Law 13/1994 of 1 June 2013), in order to comply with EU legislation.

This working paper covers the regulation from the mid-1980s to 2007, covering relevant issues such as the liberalization of capital movements (section 2), cross-border competition and permitted activities (section 3), capital requirements (section 4), supervision on a consolidated basis (section 5), supervision of financial groups and conglomerates (section 6), large exposures (section 7), investment services (section 8), deposit guarantees (section 9), crisis management schemes (section 10) and accounting (section 11). The paper ends with some conclusions (section 12).

2. Liberalisation of capital movements

The liberalization of capital movements was a fundamental change in financial regulation in Spain after the country joined the European Community in 1986. However, it took a few years for the full implementation of Directive 88/361/EEC. As noted by Dell'Ariccia et al. (2008) the liberalization of capital movements in Spain was gradual and with occasional reversals. In particular, controls on inflows abolished in February 1992 and temporarily reintroduced in 1992-93 during the European Monetary System (EMS) crisis.

Various legislative actions were undertaken to complete the liberalization. Some of them dealt with capital movements in general, as the Ministerial Order on 27/12/1990, on the liberalization of capital movements with foreign countries. Other measures specifically dealt with bank contracts and transactions such as the Bank of Spain Circular 1/92 (15/01/1992) on the bank accounts in foreign countries of country residents, the Bank of Spain Circular 2/92 (15/01/1992), on international loan and credit transaction.

3. Cross-border competition and permitted activities

Cross-border competition and permitted activities have a reference in the Second Banking Directive (89/646/EEC) which was supposed to be effectively implemented in EEC countries by no later than 1993. The implementation in Spain took place during 1994 and 1995. It started with the Law 3/1994 (14/04/1994) to adapt Spanish law in relation to credit institutions to the Second Banking Co-ordination Directive and to make other amendments in relation to the financial system. This law was fully developed within the Royal Decree 1245/1995 (14/07/1995) on the formation of banks, cross-border activity and other issues relating to the legal regime for credit institutions,

The Law 3/1994 establishes the free opening of branches in Spain to banks from other member estates of the European Union. In practical terms, an information and authorisation system by the Bank of Spain was created in coordination with supervisory bodies of other member countries. Complementarily, it also regulated the information and authorisation rules for Spanish banks to operate in other EU countries.

Royal Decree 1245/1995, modified the regulations on the formation of banks contained in Royal Decree 1144/1988. The importance attached to the suitability of shareholders with significant holdings and to the soundness of the administrative and accounting procedures of newly formed banks should be stressed. Secondly, other provisions were implemented that relate not only to banks but to all credit institutions. Thus, the rules governing the cross-border activity of both Spanish and foreign credit institutions, whether or not carried on through a branch, were specified. For European Union institutions, the so-called "Community passport" was regulated in detail. This allowed a credit institution that is authorised to operate in one Community country to operate in all the other Community countries without needing the authorisation of the authorities of the latter. There were also rules implementing the arrangements for so-called "significant holdings", already extensively regulated in the previous Law 26/1988.

Cross border activities and the formation of banks were also affected by the Investment Services Directive-ISD (93/22/EEC) that was expected to be fully adopted by member States by 1995, while in Spain it was adopted in 1998.

In accordance with the distinction made in the Investment Services Directive between regulated and non-regulated markets, a key element of the Spanish reform in 1998 was designing the operation of the Single Securities Market, the official secondary markets existing in Spain were declared to be regulated and the distinction between official and unofficial organised markets was eliminated. The reform also introduced amendments to the admission and exclusion of listed securities. In particular, the questionable pre-existing equivalence of requirements for issuing and listing has been eliminated; this equivalence generated undesirable effects when there was a slight delay between issuing and listing and the law now seeks immediate listing of securities so that they can begin trading as soon as possible.

Another fundamental aspect of the reform, which was made necessary by the ISD, was that both Spanish investment services firms and those authorised in other European Union countries qualified to become members of official secondary markets, with the capacity to trade. This meant the effective transposition of the community passport concept. It is also worth noting that the working of the market is structured in two distinct areas with the 1998 reform: registration, clearing and settlement; and trading.

4. Capital Requirements

The initial stages of the adoption of EU regulation on capital requirements by Spain refer to Directive 89/299/EEC on the own funds of credit institutions in accordance with the 1988 Basel Capital Accord, and Directive 89/647/EEC on the solvency ratio for credit institutions, also in accordance with the 1988 Basel Capital Accord. Both directives were implemented in Spain through Law 13/1992 (01/06/1992) on solvency requirements and supervision on a consolidated basis of financial institutions, Royal Decree 1343/1992 (06/11/1992) (which develops Law 13/1992) and the Bank of Spain Circular 5/1993 (26/03/1993), on the determination and monitoring of financial institutions' own funds. Combining the three regulatory developments and organizing them in different areas of solvency regulation, these were the major changes made:

Basic solvency regulation for consolidatable credit institution groups is established in Law 13/1992 on own funds and consolidated supervision of financial institutions. This law was in part a redrafting of Law 13/1985, which had already introduced own funds requirements sensitive to the level of risk of assets and memorandum accounts in anticipation of what would subsequently become the new international practices.

Royal Decree 1343/92 reinforced and developed some of the principles in Law 13/1992 and show that the solvency ratio is reinforced by a number of provisions limiting the negative effects of risks to which credit institutions are exposed, particularly in terms of credit risk. In particular, it limited major risks with an individual or economic group representing more than 10% of the own funds of the consolidatable group. It also limtied tangible fixed assets to 70% of own funds. Additionally, it introduced penalties, via deduction from own funds, of excess qualifying holdings in nonfinancial institutions. Credit institutions were also required to control interest and liquidity risks and these controls must be verifiable by and available to the Bank of Spain. In any event, the main composition of own funds was that of Law 13/1985, which stipulated that own funds of credit institutions and consolidatable credit institutions' groups shall comprise all the items shown in Table 1.

There were some important exceptions to the required capital ratios that were established by the abovementioned Bank of Spain Circular 5/1993. In particular, lower individual ratios are set for Spanish credit institutions that form part of consolidated groups. These requirement reductions could total as much as 50% based on the group's holdings in the Spanish credit institutions affiliates.

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After Directives 89/299/EEC and 89/647/EEC, solvency regulation is further developed with Directive 93/6/EEC (Capital Adequacy Directive of CAD) on capital requirements for market risk resulting from trading in securities, derivatives and foreign exchanges. This implementation of this Directive was due by 1996 but was anticipatively adopted in Spain in 1993 by means of the Bank of Spain Circular 11/1993 (17/12/1993).

Additional changes were undertaken following Directive 98/31/EC (CAD2) on the revision of the Capital Adequacy Directive 93/6/EEC, in accordance with the amendment of the Basel Capital Accord to incorporate market risk, allowing for the use of internal models. The CAD2 was due to be implemented by 2000 and in Spain the transposition was effectively completed in 2001 with the Royal Decree 1419/2001 (17/12/2001) which partially modifies the abovementioned Royal Decree 1343/1992 (06/11/1992). In relation to the solvency of credit institutions, Royal Decree 1419/2001 made three changes:

- The scope of the rules applicable to government debt in relation to the capital ratio were widened to cover debt securities issued by local authorities;

- The definition of the securities trading book was widened to include positions in gold (which were given a similar treatment to positions in foreign currencies)

- Finally, and most importantly, Spanish credit institutions were allowed to use internal risk management models to calculate their capital requirements to cover market and foreign-exchange risks.

The 2004 Basel II Capital Accord issued by the Basel Committee on Banking Supervision on 26 June 2004 (known as Basel II) established a set of structured measures based on three mutually reinforcing pillars: the adoption of uniform rules to determine minimum capital requirements on the basis of the risks assumed (Pillar 1); supervisory review to foster improved internal risk management by institutions (Pillar 2); and market disclosure of the key features of their business profile, risk exposure and risk management practices (Pillar 3). These measures must be taken into account simultaneously so that the level of own funds held by institutions is in keeping with their overall risk profile. Basel II principles were implemented in the EU through 2006/48/EC and 2006/49/EC (Capital Requirements Directive of CRD I) implementing Basel II on credit institutions and investment firms. The transposition was expected by 2007/8 and Spain effectively did it in due time. In particular with the Royal Decree 216/2008 (15/02/2008) on the own funds of financial institutions, the Bank of Spain Circular 3/2008 (22/05/2008) on the settlement and monitoring of minimum capital requirements, and the Securities and Exchange Commission (CNMV) Circular 12/2008 (30/12/2008) on the solvency of investment services firms.

Amongst this regulation, Circular 3/2008 was the main step for full implementation. The Circular made significant changes, since it not only replaces the old system of determination of minimum own funds with a more complex one more sensitive to actual banking risks, but also, as a result of implementation of pillars 2 and 3, introduced new features in other respects, such as those relating to the function of the supervisor, whose responsibility in the process of control in this area is broadened, and to mandatory reporting by credit institutions. Outlined below in Table 2 are the main new features of the Circular 3/2008. The table compares, in summary form, the main elements of the Circular 3/2008 with their treatment in Circular 5/1993 and subsequent updates.

The minimum capital requirements for credit risk remain at 8% of risk-weighted assets, including the off-balance-sheet items that entail credit risk and have not been deducted from own funds. The main new features of the Circular arise from the implementation of Royal Decree 216/2008. In particular, to calculate credit risk, institutions may choose between the standardised approach or, if authorised by the Bank of Spain, the internal ratings based approach. For the standardised approach, the Circular determines the weights applicable to the various risk exposures and sets the requirements to be met by external credit assessment institutions.

Most recently, there have been two important directives related to capital regulation in the crisis environment and linked to Basel III developments. In 2009, Directive 2009/111/EC, also known as CRD II and, in 2010, Directive 2010/76/EU, also known as CRD III. As for CRD II the most important issues were related to the removal of some national options and discretions as regards prudential regimes for large exposures, inter-bank exposures, and connected clients, harmonization of eligibility criteria of hybrid capital instruments and limits to inclusion in Tier I, as well as the retention by originator or sponsor of an "economic interest" no less than 5% of the nominal value of the securitised exposures. In the case of CRD III the most relevant contents referred to the general principles applicable to remuneration policy in the financial services sector, the remuneration policies (which should aim at aligning the personal objectives of staff members with the long-term interests of the financial undertaking concerned), the assessment of performance-based components of remuneration and some amendments to capital requirements for trading book and for re-securitisations. Although some of the issues were already considered in previous regulations in Spain mentioned above, most of the contents were adopted by both the Law 6/2011 (11/04/2011) on the amendment of the law on credit institutions' own funds and on credit institution deposit guarantee funds and the Securities and Exchange Commission (CNMV) Circular 5/2011 (12/12/2011) on the amendment of solvency regulations and accounting standards for investment firms.

The purpose of the Law 6/2011 was to commence transposition of Directive 2009/111/EC. As one of the most important features this law makes it compulsory for credit institutions and investment firms to meet certain requirements to allow them to assume exposures to securitisation positions and to initiate a securitisation. Under these requirements, which are set out in Royal Decree 771/2011, a credit institution, other than when acting as an originator, a sponsor or original lender, shall be exposed tothe credit risk of a securitisation position in its trading book or non-trading book only if the originator, sponsor or original lender has explicitly disclosed to the credit institution that it will retain, on an ongoing basis, a material net economic interest. For these purposes, "retention of net economic interest" means:

a) retention of no less than 5% of the nominal value of each of the tranches sold or transferred to the investors;

b) in the case of securitisations of revolving exposures, retention of the originator's interest of no less than 5% of the nominal value of the securitised exposures;

c) retention of randomly selected exposures, equivalent to no less than 5% of the nominal amount of the securitised exposures, provided that the number of potentially securitised exposures is no less than 100 at origination; or d) retention of the first loss tranche and, if necessary, other tranches having the same or a more severe risk profile than those transferred or sold to investors and not maturing any earlier than those transferred or sold to investors, so that the retention equals in total no less than 5% of the nominal value of the securitised exposures.

The Bank of Spain may specify the conditions of application of this Law and how those institutions will communicate the retention requirement to investors. This communication must allow them ready access to all pertinent data on exposures. Also, the Bank of Spain may opt to suspend temporarily the aforementioned requirements during periods of general market liquidity crisis. As an exception to the foregoing, this Law will not apply where the securitised exposures are claims on assets unconditionally and irrevocably guaranteed by:

a) central governments or central banks;

b) regional governments, local authorities and public sector entities of Member States;

c) institutions to which a 50% risk weight or less is assigned under Royal Decree 216/2008; or

d) multilateral development banks.

In addition, the Law establishes monitoring and reporting obligations on institutions investing in securitisation instruments. Thus credit institutions shall have a comprehensive and thorough understanding of each of their individual securitisation positions and demonstrate that they have implemented therein formal policies and procedures appropriate to their trading book and non-trading book and commensurate with the risk profile of their investments. To comply with this obligation, the Bank of Spain shall determine the items which, as a minimum, have to be examined and recorded by institutions, including stress tests and how they are to be carried out. Originator and sponsor credit institutions shall apply to the exposures they intend to securitise the same

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credit standards and credit management criteria applied to the exposures they intend to hold in their portfolio, in accordance with the technical criteria on the organisation and treatment of risk stipulated by the Bank of Spain. Moreover, they shall inform investors of the level of their commitment to maintaining a net economic interest in the securitisation. Further, they shall ensure that prospective investors have readily available access to all relevant data as stipulated by the Bank of Spain.

Finally, the consequences of failing to comply with the requirements regarding securitisation positions are set out. If a credit institution does not comply with its obligation to communicate its retention requirements, the risk weight of its securitisation exposures shall be increased, the Bank of Spain determining the extent of such increase and how it is to be applied. If the due diligence conditions established by the Bank of Spain are not met, the originator credit institution may not exclude the securitised exposures in the calculation of its capital requirements.

5. Supervision on a consolidated basis

The supervision on a consolidated basis referred initially to the implementation of Directive 83/350/EEC on supervision of credit institutions on a consolidated basis in line with the 1983 Basel Concordat, which was made through Law 13/1985 (25/05/1985) on investment coefficients, own funds requirements and information disclosures rules for financial intermediaries. The developments of Law 13/1985 have been already widely commented in the previous section.

A significant change however came with the implementation of Directive 92/30/EEC 92/30/EEC on supervision of credit institution on a consolidated basis in accordance with the 1988 Basel Capital Accord.. The due implementation date was 1993 but in Spain it was transposed earlier, in 1992, through Law 13/1992 (01/06/1992) on solvency requirements and supervision on a consolidated basis of financial institutions, Royal Decree 1343/1992 (06/11/92) on the development of Law 13/1992 and the Ministerial Order of 30/12/92.

Law 13/1992 simply recognized the need of implementing the principles of Directive 92/30/EEC. The preamble of the law acknowledged the importance of being cautious and not imposing a stricter regulation on Spanish banks compared to their European counterparts. Following the Directive, Law 13/1992 pays particular attention to consolidated banking gropus defined the general type of consolidated groups although it leaves to a lower-order regulation (Royal Decree 1343/1992) the full development of the definitions and the required own funds for each group. Importantly, Law 13/1992 and Royal Decree 1343/1992 were largely modified by Law 5/2005 on supervision of financial conglomerates and Royal Decree 1332/2005, on the development of Law 5/2005. For this reason, we make a joint treatment of these regulations. In implementation of Law 5/2005 on supervision of financial conglomerates, the Royal Decree establishes the obligations of groups in which banking or securities firms coexist with insurance companies, but which do not meet the requirement of significant sectoral diversification. These groups are required to send to all Spanish relevant competent authorities the information required to verify, first, that they are not subject to the supplementary supervision regime and, second, the supplementary capital they would have to hold if they became subject to it.

Royal Decree 1332/2005 also specified the criteria to be taken into account in subjecting to supplementary supervision, on one hand, those financial conglomerates that meet the aforementioned requirement of significant sectoral diversification in the second of the ways defined in the Law, i.e. by having a balance sheet total in the smallest sector of the group that exceeds Eur 6 billion, and, on the other, those regulated entities (as defined in Law 5/2005) that, not constituting a group, are investees or under notable influence of one or more physical or legal persons and have significant activity both in the banking and investment services sector and in the insurance sector. The conditions to be met under these criteria shall be decided by common agreement between the co-ordinator and the relevant competent authorities.

As for the relevant competent authorities involved in the supervision of a financial conglomerate, they are:

a) The Spanish competent authorities or those of other EU Member States responsible for consolidated supervision of the regulated entities of a financial conglomerate;

b) The co-ordinator designated pursuant to this Royal Decree, if different from the authorities referred to in the preceding point;

c) Other interested competent authorities, whenever so decided by mutual agreement of the authorities referred to in a) and b) above;

d) The Spanish competent authorities, in the case of a financial conglomerate whose foreign regulated entities do not belong to an EU State and which includes a Spanish financial institution.

As for Directive 95/26/EC on reinforced supervision of financial institutions it only required the development of some definitions for what are called in Spain as credit financial establishments and this was done in 1998 (with some delay to the supposed implementation data of 1998) with the approval of Law 37/1998 (16/11/1998), amending Law 24/1988 on the Securities Market Royal Decree Law 692/1996 (26/04/1996) on the legal regime for credit financial establishments ("establecimientos financieros de crédito").

6. Supervision of financial groups and conglomerates

The initial step in a common framework for a supervision of financial groups and conglomerates took place with Directive 2002/87/EC 2004 on rules for supplementary supervision for credit institutions, investment firms and insurance companies pertaining to a financial conglomerate. The implementation was due in 2004 and in Spain was finally done in 2005 with Law 5/2005 (22/04/2005) on the supervision of financial conglomerates, amending other financial sector legislation and the Royal 1332/2005 (11/11/2005) implementing Law 5/2005.

Part of the motivation for Law 5/2005, was the so-called Financial Services Action Plan (FSAP) set in motion by the European Commission. The FSAP set, inter alia, plan that the need to offer an adequate response to the proliferation of cross-sectoral groups, encompassing credit institutions, investment services companies and insurance companies, was addressed. This intensification of the links between traditional financial sectors had given rise to a dual problem. First of all, it favoured the emergence of new risks, or at least it potentially increased existing ones. It was therefore necessary to adopt adequate regulations proportional to these risks. Secondly, in a single financial market these new regulations had to be undertaken in a harmonised way and any inconsistencies between sectoral legislations corrected. The starting point was characterised by a variety of shortcomings. Whilst "uniform" groups of financial institutions were sufficiently covered by sectoral rules of prudential supervision that were already fully operational and working satisfactorily, "heterogeneous" groups lacked a full body of regulations, and numerous inconsistencies (not to mention loopholes) were apparent between sectoral legislations applicable to entities in such groups. The declaration of purpose of Law 13/1992 provided a set of special supervisory rules applicable to non-consolidatable mixed groups. This set of rules is structured by Law 5/2005, on the one hand, around a series of additional solvency requirements beyond those provided for in the sectoral framework (individual or consolidated) for banking, securities and insurance institutions, and also around the designation of a supervisory authority responsible for overseeing compliance and the setting up of a cooperation procedure to adopt, if applicable, the measures necessary to ensure the compliance.

The main developments of Law 5/2005 have been mentioned in the previous section and responded to the fundamental aim of providing for a specific prudential regime applicable to financial conglomerates. However, it also had a secondary aim. Namely to progress towards greater consistency between the different sectoral legislation applicable to uniform groups, and between the sectoral legislation applicable to the latter and that applicable to financial conglomerates. The full development of Law 5/2005 was made through Royal Decree 1332/2005, as described in the previous section. The Royal Decree established how a financial conglomerate shall calculate its eligible own funds and what its minimum level will be. Also, the regulated entities of financial conglomerates must inform the co-ordinator with the periodicity specified by the latter, which must be at least once a year, of any significant intra-group transaction by the regulated entities in the financial conglomerate and of any significant concentration of risk; the co-ordinator must examine the possible risk of contagion and of conflict of interest within the financial conglomerate and the risk of evasion of sectoral rules and regulations. The regulated entities of financial conglomerates must send the co-ordinator such periodic or non-periodic information as the latter may require of them to verify compliance with their obligations. Also, they must co-operate with the co-ordinator in what it asks of them and facilitate any inspections, although the competent authorities responsible for supervision of the entities of groups included in the conglomerate may approach these directly, in exercise of the powers of individual or consolidated supervision of the entities included in the conglomerate. Finally, financial conglomerates must have adequate risk management procedures and internal control mechanisms. Other regulations affected The final provisions, continuing the amendments made to Law 5/2005, revise the sectoral (banking, securities and insurance) rules of regulatory rank in order to make them consistent with each other and bring them into line with the new regime for financial conglomerates. These provisions, most of them included for the sake of fine-tuning, include most notably the definition of the scope of consolidation for supervision purposes and the changes made to the calculation of eligible own funds. Most important among the latter are, on the deductions side, the need to subtract the amount of participating interests in insurance and reinsurance companies and in entities engaged primarily in holding investments in insurance companies, whenever the participating interest exceeds 20% of the capital of the investee, and, on the eligible components side, the admissibility of including the accounting balance of the general allowance/provision for credit losses attributable to the customer, up to a limit of 1.25% of risk-weighted assets, and the gains recognised in the assets of the company in application of the fair value criterion, although the Bank of Spain may reduce the gross amount by two thirds, depending on the volatility of the different types of assets.

As for the implementation of Directive 2007/44/EC, which tightens supervision on M&A in the financial sector, it was transposed in 2009, the due year through Law 5/2009 (29/06/2009) on the regime for the acquisition of significant holdings. This law reformed the regime for qualifying holdings in the financial sector, clarifying the procedures and evaluation criteria applicable for the prudential assessment of acquisitions and increases of such holdings. The aim was to enhance both the legal certainty and the practical effectiveness of the regime, making it more consistent with the ultimate aim, which is to ensure the stability of the financial institutions and of the markets in which they operate. To this end, the Law envisages that a qualifying holding is held if it amounts to 10% (up from 5% previously) or more of the capital or voting rights of the institution acquired, or if there is a possibility of exerting notable influence in the institution (deemed to exist when there is a possibility of appointing or dismissing a Board member). Moreover, all holdings of 5% or more of the capital or voting rights, even if they are not considered qualifying holdings, must be notified to the supervisor.

Law 5//2009 also outlined a new assessment procedure that is clearer and more transparent and has shorter time limits, and establishes the criteria on which financial supervisors should base their opposition to any acquisitions proposed (the standing and solvency of the acquirer, the standing of the future administrators of the institution and the capability and solvency of the institution). It also reinforces the collaboration between the supervisor of the acquiring institution and that of the institution acquired throughout the assessment process, and simplifies the limits determining the need to notify any increases or reductions in qualifying holdings, which are set at 20%, 30% and 50% of the capital or voting rights.

Royal Decree 1817/2009 complemented the Law 5/2009, implementing its more technical aspects. Thus, the Bank of Spain will compile and publish a list specifying the information to be provided by a potential acquirer, on itself and on the reasons for the acquisition, for assessment of the transaction. Should the acquisition signify takeover of the institution, the information to be provided must also include matters connected with possible changes in the institution's structure and in its corporate governance, with the procedures envisaged relating to internal control and prevention of money laundering, and with the new business and strategic development plan.

7. Large exposures

Directive 92/121/EEC on the monitoring and control of large exposures of credit institutions set a transposition deadline by 1994. In Spain, it was implemented in 1993 with to circulars of the Bank of Spain: Circular 5/1993 (26/03/1993) on the determination and monitoring of financial institutions' own funds and Circular 12/1993 (17/12/1993) which modifies Circular 5/1993.

Circulars 5/1993 and 12/1993 set four important rules regarding large exposures:

- They consider "large risks" as those positions with a face value larger than 10% of the own funds of the financial institution.
- The value of all the risk positions of an institution with the same subject or economic agent could not exceed 25% of its own funds.
- If the risks were maintained with non-consolidated institutions within the same economic group, the limit was 20% of the own funds.

- The sum of all the large exposures of a bank will be lower than eight times the own funds of the financial institution.

Directives 2006/48/EC and 2006/49/EC (CRD) Capital Requirements Directive implementing Basel II (credit institutions and investment firms) also incorporated various principles regarding large exposures. The due implementation data was 2007/8 and that was the date met by Spanish regulators. The principles were mainly transposed through Law 36/2007 (16/11/2007) which modifies Law 13/1985 (25/05/1985) on investment coefficients, own funds requirements and information disclosures rules for financial intermediaries, Royal Decree 216/2008 (15/02/2008) on the own funds of financial institutions, Bank of Spain Circular 3/2008 (22/05/2008) on the settlement and monitoring of minimum capital requirements, and the Securities and Exchange Commission (CNMV) and Circular 12/2008 (30/12/2008) on the solvency of investment services firms.

The two circulars of the Bank of Spain contained the main changes regarding large exposures. As for Circular 3/2008, it maintains the definitions previously mentioned for Circular 5/1993. In particular, it defined a large exposure as one whose value exceeds 10% of a credit institution's own funds. The value of all the exposures of a credit institution to a

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third-party person or economic group may not exceed 25% of its own funds. Where the exposures are to non-consolidated entities of a credit institution's economic group, this limit shall be reduced to 20%. Finally, the total large exposures may not exceed eight times a credit institution's own funds.

Additionally, Circular 3/2008 made some changes to the measures in place to return to compliance with solvency regulations. Thus it equates a shortfall of 20% of minimum own funds with a shortfall of 50% in tier 1 capital, so that where a credit institution or group or sub-group of credit institutions has a regulatory capital shortfall exceeding 20% of the minimum requirement, or its tier 1 capital falls below 50% of that minimum requirement, the individual institution or each and every institution in the group or sub-group must allocate its net profit or surplus in full to reserves. However, as a new feature, and as required by Royal Decree 216/2008, the Bank of Spain is empowered to authorise other action in the event that the programme submitted by the institution for restoring compliance with capital requirements is approved. If the capital shortfall is 20% or less of the minimum requirement, the individual institution or each and every institution in the group or sub-group shall submit a proposed distribution of its profits, and of those of each of the institutions in the group or sub-group, to the Bank of Spain for authorisation. The Bank of Spain will set the minimum percentage to be allocated to reserves, taking into account the programme submitted to restore the required levels. In this case, the limit of 50% which the previous circular set on the profi ts allocated to reserves no longer applies. The limitations on the distribution of dividends do not apply to the subsidiaries in which consolidated group entities hold at least 80% (previously 90%) of the voting rights and of the capital, provided that, in the case of credit institutions, they individually meet the general own funds requirements.

As for Circular 12/2008 the limits on large exposures (those exceeding 10% of a credit instituion's own funds) do not undergo any significant changes. The amount of all the exposures of a credit instituion to a single third-party client or economic group may not exceed 25% of its own funds; if the risk exposure is to unconsolidated institutions of the reporting institution's own economic group, this limit shall be 20%. Again, the overall large exposures may not exceed eight times its own funds. However, for the purposes of calculating these limits, the exceptions envisaged by the Circular include a wide variety of exposures. To implement the so-called Pillar 2 of the Basel Accord (internal capital adequacy assessment and supervisory review process), the Circular includes a wide range of measures designed to improve the internal management of institutions and, in particular, of their risks. Thus credit institutions and consolidable groups and sub-groups of credit institutions should have a clear organisational structure with well-defined, transparent and consistent reporting lines. They should also have adequate internal control mechanisms and appropriate processes to prevent conflicts of interest and to identify, manage, monitor and report risks (including interest rate risk). These procedures should be reviewed regularly. Additionally, both credit institutions and consolidable groups of credit institutions should carry out an internal capital adequacy assessment process. This process should enable institutions to assess and maintain on an ongoing basis the amounts, types and distribution of internal capital and of own funds they consider adequate to cover all risks, depending on their nature and level, to which they are or may be exposed. In order to measure them, institutions may use their own methodologies or, alternatively, the criteria provided for this purpose by the Bank of Spain in its guidelines for this purpose. These strategies and procedures shall be summarised in a yearly internal capital adequacy assessment report to be sent on a confidential basis to the Bank of Spain for review in accordance with the provisions of Law 13/1985.

A related key fundamental instrument of control for large exposures is the Bank of Spain's Central Credit Register (CCR). The CCR holds the credit records of natural and legal persons in order to facilitate institutions in their credit risk analysis. Generally speaking, reporting institutions (credit institutions and others) are obliged to report on direct risks with residents for sums of 6,000 euro and over for the whole of their businesses in Spain or of 60,000 euro or more in any other country. Non-residents however are obliged to report amounts of 300,000 euro or more. The main regulations concerning the Spanish CCR are shown in Table 3.

The reported information allows the Bank of Spain to know the total lending granted, which enables it to perform its banking supervision obligations. For their part, the institutions that report their risks to the CCR of the Bank of Spain receive monthly aggregate information on the risk contracted by the natural and legal persons that they have reported ("account holders"). Nevertheless, any institution may request specific information about an account holder if the account holder applies for a risk operation (such as a loan) or appears as liable for payment or as a guarantor in negotiable or credit documents which the institution has been requested to acquire or trade.

As shown by Trucharte (2004) the main developments on the Spanish CCR took place as a consequence of the implementation of Basel II. With Basel II certain changes had to be made on the CCR, basically in the information required, to optimise its employment as an instrument for the banking supervisor. The CCR data structure distinguishes between credits to firms and those to individuals. Among the latter it is possible to identify those engaging in business activities (individual businesspersons). The CCR includes information on the characteristics of each loan, including the following: type of instrument (trade credit, financial credit, lease, etc), currency denomination, maturity, existence or not of guarantees or collateral, type of guarantor (government or credit institution), the cover age of the guarantee, the amount drawn and undrawn of a credit commitment and, finally but very importantly, whether the loan is current or past due (distinguishing between delinquency and default status). The CCR also includes information relating to the characteristics of borrowers: province of residence and, for firms and businesspersons, the industry in which they operate. All credit institutions supply monthly information to the CCR on any changes in the status of their outstanding credits (for example, whether the borrower has changed to delinquent or default status) and information on the new loans granted during the period. In exchange, they receive information on defaulted obligors in the system and can obtain data at any time on the total bank debt of any of their customers.

Therefore, before granting a loan to a potential customer, any bank can consult the CCR to see whether that customer fulfils its credit obligations to other banks. The CCR also enables the bank to know the amount of that customer's total debt to other credit institutions. The CCR does not include information on borrowers' financial characteristics. New entrants in the credit market can consult the CCR under the same conditions as can insider banks. Moreover, the information provided by the CCR is supplied to institutions at no cost.

The CCR is used both to support on-site inspections and to carry out off-site monitoring of credit and concentration risk. The information held in the CCR also permits off-site monitoring. The obligation of all credit institutions to report defaulted obligors works as a disciplinary element that helps to maintain the quality of the information received and is a basic input for accurately assessing the risk incurred by each bank.

8. Investment services

The Investment Services Directive (ISD 93/22/EEC) was a fundamental change for financial services in Europe. Its due date implementation was 1995 while in Spain it was not fully transposed until 1998. The main reason is that Spain did a complete reform of its Securities Market Law (by that time Law 24/1988 on Securities Markets). Hence, the implementation of the ISD was made through Law 37/1998 (16/11/1998), amending Law 24/1988 on the Securities Market.

Law 37/1998 introduced several changes on Law 24/1988. Firstly, as a result of the wide range of financial instruments included under the scope of the new market regulations, which go beyond the category of transferable securities, all financial instruments became subject to the discipline applicable to transferable securities, in order to adapt the new financial reality (e.g. swaps, FRAs, options, futures, etc.) in Spain's markets. Another significant aspect is the abolition of the monopoly on keeping book entry records for transferable securities not traded in official secondary markets, which was previously held by Broker-dealers and Brokers. There were also significant changes in the the regime of the National Securities Market Commission (CNMV) Advisory Committee (Comité Consultivo). Firstly, its composition was amended to enable the admission of representatives of all of Spain's official secondary markets. Secondly, the Committee's powers have been accommodated to the new provisions of the law regarding market subjects and the markets themselves.

Important new features in the regulation of the official secondary securities markets are also introduced. In addition to incorporating the provisions of the Investment Services Directive into Spanish law, it also incorporates market regulations such as those concerning derivatives, which had not been implemented within the Spanish financial system in 1988.

The classification of market transactions in accordance with the decentralising principles which guide the regulation within the Investment Services Division is particularly noteworthy. It resulted in a basic distinction between market transactions and non-market transactions. Market transactions are those which result in a transfer, by purchase and sale or otherwise for a consideration, within the market. A distinction is also made between ordinary and extraordinary market transactions. Ordinary market transactions are subject to the basic market functioning rules (in particular, participation of members and the routing of transactions via ordinary trading systems).

Another fundamental aspect of the reform, which was made necessary by the Investment Services Directive, was that both Spanish investment services firms and those authorised in other European Union countries qualify to become members of official secondary markets, with the capacity to trade.

Focusing on market-specific regulations, in the stock markets, the execution of transactions in the stock exchanges and in the electronic market (SIBE) was made subject to current regulations; therefore, the free access envisaged in the Directive is achieved by acquiring membership of a stock exchange management company. For this reason, some amendments had to be made to the rules regarding the acquisition of holdings in these management companies.

Several highly significant new elements were introduced in the Public Debt Market represented by book entries. Firstly, securities listed in the Central Book-Entry Office can now be traded in parallel in any other official secondary market, thus offering a wider scope for trading and interrelation between markets.

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Secondly, the fundamental market regulatory standard was called the "Market Regulation" (Reglamento del Mercado). In addition, the existing Market Advisory Commission (Comisión Asesora del Mercado) will include representatives of market members and of the Autonomous Regional Governments.

The working of the market is structured in two distinct areas: registration, clearing and settlement; and trading. Therefore, this opens several categories depending on the vocation of each market subject. Derivatives market, already developed in the Spanish financial system, has been placed on a firm legal footing.

A specific treatment was made to "Investment Services Firms", in accordance with the statutory equivalence of investment services firms and credit institutions as defined in the Investment Services Directive. Previously, investment services firms were defined by their financial institution status and by offering professional investment services to third parties. In accordance with the ISD, the activity status of investment services firms is categorised with regard to the investment services and ancillary services offered in connection with financial instruments, which, in the final instance, determine their implementation under the community passport. In compliance with the new objective and subjective regulation of financial market operators, the Law confers the status of investment services firm, in its strict sense, on Broker-dealers and Brokers, and on Portfolio Management Companies.

Importantly, Law 37/1998 incorporated regulation of a new mechanism in the Spanish securities markets, the "Investor Compensation Scheme" (Fondo de Garantía de Inversiones). This regulation transposes Directive 97/9/EC into Spanish law. The regulation of this fund also responds to one of the requirements of the Investment Services Directive and, like Deposit protection schemes for credit institutions, it compensates investors in the event of insolvency or bankruptcy of investment services firms where the cash or securities entrusted by an investor are no longer available; however, in no way does the fund cover credit risks or any losses to the value of a market investment.

The reform made by Law 37/1998 also included more comprehensive regulation on preference shares, particularly non-voting shares. The aim of the legislation is to enable financing via markets (taking into account the practical circumstances of corporate control) with sufficient guarantees to investors, using formulae to allow investment in capital without involvement (through voting rights) in the running of the company. The reform distinguishes between listed and unlisted companies, providing more flexibility to the former due to the greater transparency requirements imposed in the securities markets.

9. Deposit guarantee

Deposit guarantee schemes are a cornerstone of financial architecture and they have suffered several regulatory developments in Spain over the last three decades. Directive 94/19/EC on deposit guarantee schemes was transposed to Spain in 1996, one year after the EU official transposition date by Royal Decree 12/1995 (28/12/1995) on urgent matters on budgetary, fiscal and financial issues (seventh additional measure: Deposit Guarantee Fund).

Royal Decree-Law 12/1995 introduced the first important novelties such as obligatory membership of a Deposit Guarantee Fund for Spanish credit institutions, the conditions for exemption from this duty, together with the reasons for expulsion. However, the main principles of the reformed deposit guarantee regulation were introduced by Royal Decree 2606/1996. The decree established the legal regime covering Deposit Guarantee Funds for Banking Institutions, Savings Banks, and Credit Cooperative Banks. A new feature was the definition of the system of contributions to the Funds and the mechanisms for the reduction and suspension of contributions, such that each of the Funds is fed via the annual contributions of its member credit institutions and, exceptionally, by contributions from the Bank of Spain, the amount of which must be set by Law.

The most novel features were the following:

- Voting is required as the means of electing members of the bodies governing the Funds, i.e. this is to be the means whereby associations representing credit institutions elect their representatives on the respective Deposit Guarantee Fund's Management Committee.
- The concept of the representatives of the associations is established according to two criteria: They must represent more than 80 per cent of the member institutions of the

corresponding Fund and more than 90% of the deposits held by these institutions. If these percentages are not reached the appointment of representatives shall be carried out by means of a direct vote held by all the member institutions of the Fund.

- The definition of the guaranteed deposits involves a delimitation which is as much positive as negative, in accordance with the guidelines foreseen in the Directive that it implements. Deposits not guaranteed on account of their nature and which, therefore, are not included in the calculation of the contributions, are distinguished from those which, although covered in principle, and so included in the calculation, may be excluded from the obligation to pay under certain circumstances. On the other hand, the maximum guaranteed amount in relation to deposits is limited to the equivalent in pesetas of 20,000 Euros, although up until 31st December 1999 this limit remained set at 15,000 Euros.

- The adoption of the so-called "principle of guarantee by the country of origin" which implies obligatory coverage by Deposit Guarantee Funds in the country of origin in the case of Spanish branch offices of credit institutions based in other countries of the European Union.

- The system of membership of the Banking Institution Deposit Guarantee Fund for foreign branch offices of credit institutions is also defined, and an essential distinction is drawn. Institutions based in other Member States of the European Community are permitted voluntary membership so that they may offer their depositors a complementary guarantee in addition to their own.

- The regulation of procedural aspects relating to the causes or circumstances that give rise to the liability for payment and those governing payment itself stand out. A traditional purpose of Spanish Deposits Guarantee Funds has been to ensure the stability of the financial system, avoiding a crisis afflicting one credit institution affecting the rest of the institutions operating in the market. A noteworthy feature of the new regulations was the so-called "Action Plan", which may include both preventive measures and measures for the reorganization of the institution. These measures may entail a range of actions intended to restructure the institution's assets, in particular subscription of capital increases by the Fund, and various types of financial assistance and management measures.

In 2009, Directive 2009/14/29 on (Deposit Guarantee Schemes was issued. This was implemented in Spain by Royal Decree 628/2010 (14/05/2010) on the amendment of legislation on depositor and investor guarantee scheme. The Royal Decree maintains the level of protection remains at Eur 100,000 in DGFs and those guarantees continue to apply per depositor or investor, whether a natural or a legal person, regardless of the number and type of cash, securities or financial instrument deposits in the holder's name at the same institution.

With the Royal Decree 628/2010, credit institutions have to make available to customers information on the functioning of the DGFs of which they are members, specifying the amount and scope of the cover offered. Also, they must inform about the conditions and the formalities which must be completed to obtain compensation payouts. The surplus held by DGFs in excess of the amount needed to fulfil their objectives shall remain in their assets and may not be distributed or returned to member institutions. DGFs have to conduct regular operational tests to assess their ability to cope with a possible crisis at an institution. Lastly, it is expressly specified that the investor coverage schemes (ICS) will not cover investors holding a securities account with an institution not covered by the ICS, even if that institution had in turn deposited the securities in an account at one covered by the ICS.

Most recently, Royal Decree 771/2011 also introduced some changes by amending Royal Decree 2606/1996 by introducing a new regime for additional contributions to these funds based on the remuneration of the deposits in them. Specifically, the amounts of the deposits whose agreed remuneration exceeds the limits specified below shall be weighted at 500% (i.e. 400% more than the weight they would have if they were included in that base) for the purpose of calculating the contributions of the credit institutions belonging to the related deposit guarantee funds. The limits above which the new weights will be applied are as follows: 1) sight deposits whose annual interest paid in the periodic settlement of the account is more than 100 basis points higher than average 1-month Euribor; 2) time deposits (or similar instruments) up to three months whose agreed annual interest is more than 150 basis points higher than average 3-month Euribor; 3) time deposits (or similar instruments) between three months and one year whose agreed annual interest is more than 150 basis points higher than average 6-month Euribor; and 4) time deposits (or similar instruments) with a term of one year or more whose agreed remuneration is more than 100 basis points higher than average 12-month Euribor.

The Royal Decree 771/2011 was implemented through the Bank of Spain Circular CBE 3/2011 (30/06/2011) on additional contributions to deposit guarantee funds sets out technical provisions implementing the new precepts introduced by Royal Decree 771/2011. The Circular contained two types of rules: those for identifying what is understood as deposit remuneration in different practical cases, and those regulating ad hoc tools for calculating the additional contribution. Deposit remuneration shall comprise any explicit or implicit compensation or payment, in cash or in kind, for maintaining a deposit. Thus the value of remuneration in kind shall be that applicable under tax legislation, including any tax prepayments to be made for the remuneration when they are borne by the institution. In variable-rate time deposits, the remuneration shall be that which results from applying the reference index at the deposit placement date over the whole of the agreed time period, disregarding possible future modifications. In time deposits in which the interest rates change before maturity, the interest rate taken shall be the average of the rates, weighting each by the time it is to be applied. In hybrid financial instruments in which the embedded derivative does not share similar characteristics and risks with the host contract, the interest rate used to determine their remuneration shall be the maximum annual percent remuneration receivable by the depositor on the amount deposited, if it is higher than the effective annual interest rate corresponding to the host contract after the embedded derivative has been stripped out; in the absence of the former, only the latter shall be taken. In any event, any additional remuneration envisaged in the contract, be it in cash or in kind, has to be included.

10. Crisis management schemes

The full implementation in Spain of the Directive on reorganisation and winding-up of credit institutions (2001/24/EC) which was due by 2004, was actually undertaken in 2005 with Law 6/2005 (22/04/2005) on the clean-up and liquidation of credit institutions. In line with its cross-border focus, this Law 6/2005 was applicable to credit institutions authorised in Spain which have at least one branch or provide services without a permanent establishment in another Member State of the European Union; to credit institutions authorised in another Member State which also have at least one branch or provide services without a permanent establishment in Spain; and to the branches in Spain of foreign credit institutions not authorised in an EU Member State, when such credit institutions have at least one branch in another Member State. The reorganisation measures referred to by this Law do not include those actions that, with the same name (preventive and reorganisation measures), can be adopted by credit institution deposit guarantee funds in accordance with Royal Decree 2606/1996 of 20 December 1996. Rather, they only include those adopted by the administrative or judicial authorities of an EU Member State that are intended to preserve or restore the financial situation of a credit institution. For its part, the initiation of the insolvency proceedings regulated by Law 22/2003 of 9 July 2003 on insolvency shall be deemed to be a reorganisation measure; notwithstanding this, should the winding-up phase be ordered, from that time the winding-up rules envisaged in Law 6/2005 shall be applied. In any event, upon initiation of the winding-up phase, the credit institution's authorisation shall be cancelled. Law 6/2005 is based on the principles of "competence" and "law" of the Member State in which the credit institution has been authorised. Accordingly, the Spanish judicial authorities shall be solely responsible for determining the application to a credit institution authorised in Spain, including its branches in other Member States of the European Union, of a reorganisation measure or winding-up proceeding. Such authorities shall, without delay, advise the competent supervisory authorities of the various host Member States, through the Bank of Spain, of their decision and its repercussions. They may also request that the decision be made public in the public registries. Symmetrically, if the Spanish judicial authorities consider it necessary for some reorganisation measure to be applied to the branches of credit institutions authorised in another Member State, they shall be obliged to advise the competent supervisory authorities of the home Member State of that fact through the Bank of Spain. In any event, the adoption of a reorganisation measure or winding-up proceeding in respect of a credit institution authorised in another Member State that has a branch in Spain shall be fully effective in Spain as soon as it is fully effective in the Member State in which that measure or proceeding was adopted.

Since 2009, the Spanish banking sector has undergone some of the most ambitious and intense reforms since the financial liberalization of the 1970s and 1980s. The first important milestone in the bank restructuring process in Spain took place in June 2009, with the approval of the Royal Decree-Law 9/2009 (26/06/200), which created the so-called Fund for the Orderly Restructuring of the Banking Sector (FROB). The FROB is one of the main pillars of the banking reform in Spain. The Royal Decree 9/2009 included a set of measures to address some of the weaknesses shown by Spanish banks at that time. The text of the decree provided the following rationale for reform implementation: "the situation of the Spanish banking sector cannot be described as normal, although given their size, those individual institutions likely to encounter difficulties are not systemic." Nonetheless, "if we consider their viability problems overall, a potential systemic risk could be created. The potential risk justifies the provision of early instruments and public resources in the event that circumstances make their use necessary... and the sector would find hard to sustain such losses through reliance on the three Deposit Guarantee schemes."

As for the functioning of the Royal Decree 9/2009, three different scenarios were considered:

(i) The search for a private solution by the troubled bank itself (basically taking the form of mergers with one or more institutions);

(ii) Actions to tackle weaknesses that may affect the viability of the bank and that could be covered with the existing Deposit Guarantee Fund;

(iii) An orderly restructuring process with the involvement of the FROB. The FROB could also participate as part of a financial viability plan in the event of a merger.

In practical terms, this Decree forced all Spanish banks to present viability plans to identify if they were in need of any of the solutions considered. The Bank of Spain itself released stated that FROB was a "painstaking process because of the variety and significance of the regulatory adjustments required and because of the complex decisions and negotiations entailed (…) the restructuring of the savings banks sector was unavoidable… since the sector had several structural limitations associated with its legal nature, such as the legal restrictions on raising high quality capital other than via retained earnings and a complex and rigid system of governance not conducive to best corporate governance practices." Reform emphasis from that moment onwards was placed on savings banks. However, as it has been shown by the most recent developments in the Spanish banking sector, the solvency problems were not exclusive to the savings banks. In fact, most Spanish banks are currently affected by restructuring processes on some level.

In any event, the implicit focus made on savings banks by was reinforced by a new law in 2010 that was explicitly oriented to savings banks, the Royal Decree-Law 11/2010 (9/07/2010). Prior to this law, savings banks relied mostly on retained profits to increase their solvency ratios. Given that one of the main regulatory responses to the crisis has been requiring more bank capital (i.e. Basel III requirements) the limitations of savings banks to access market financing had to be removed. The Royal Decree-Law 11/2010 addressed these limitations in two main ways: first, it increased the flexibility of rules governing existing core capital instruments, cuotas participativas (capital certificates) to allow for these instruments to carry voting rights. However, reliance on this type of financing since 2010 has been very limited. Second, and most important, it allowed for alternative ways for a savings bank to transfer all its banking activities to a bank (a public limited company) and remain as a holding institution or even an ordinary foundation, dedicated to the promotion of social works. This was a critical step during the Spanish bank restructuring process, as far as savings banks were concerned, for two main reasons:

- Savings banks were able to maintain their foundational nature and, therefore, the institutional diversity of the Spanish banking sector was legally guaranteed.

- The decree enhanced the development of larger savings bank groups, with a core financial centre that took the form of a commercial bank. This permitted the new banking groups to have better access to capital markets and liquidity, while the regional scope and relationship banking nature of the savings banks' model was maintained within the banking group.

A third important regulatory event that comprised the Spanish bank reforms was the Royal Decree-Law 2/2011 on the strengthening of the Spanish financial system. The aim of the recapitalisation of the banking sector was that all Spanish banks should have a core capital ratio of at least 8% (10% if they were not a listed company and, hence, had difficulty accessing to equity markets, as experienced by some of the savings banks). Those that did not meet the new minimum requirements had until September 30th, 2011, to increase their capital, either through reliance on private investors or through the FROB.

Even if the banking sector experienced a significant restructuring and consolidation following the regulatory initiatives undertaken from 2009 to 2011, the main outstanding challenge for Spanish banks remained the asset impairment problem linked to their real estate market exposure. Towards the end of 2011, the debate on the likely impact of a potential clean-up of assets in the Spanish banking sector was very intense. In February 2012, the government approved the Royal Decree-Law 2/2012 (3/02/2012). The rationale states that the measures were "designed to clean up institutions' problematic exposures to construction and real estate developers in Spain - particularly land – from their balance sheets… as well as to consider potential migrations of assets from normal to problematic portfolios."

Most of the reform was directed at introducing new provisions and fostering further sector consolidation. Through this approach, the government was giving priority to private sector based solutions before imposing additional costs on taxpayers. The new provisioning scheme seems simple but there are several exceptions and specific features with very relevant implications.

Importantly, the new provisions are applied to the stock of legacy assets as of 31.12.2011 and not to new loans or assets. The reference framework to estimate the impact of the new provisions are the accounting statements of banks as of June 2011. The total

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exposure to risk (construction and development) of Spanish banks was estimated at Eur 323 billion (Eur 175 billion were considered to be non-performing or substandard).

A bulk of new provisions was requested for land and housing under development. Only considering specific provisions, the coverage ratio of land was projected to increase from 31% to 60% and that of housing under development from 27% to 46%. There were also other specific provisioning requirements. In particular, in the case of repossessed finished housing and other real estate developer collateral, the value of the provisioning coefficients was increased in relation to the time that the asset has been held on the bank's balance sheet: 10% (1st year); 20% (2nd year) and 30% (3rd year) to 25% (1st year); 30% (2nd year); 40% (3rd year) and 50% (4th year). Similarly, provisions for doubtful loans on finished housing were set at 25% and for substandard loans at 20%. In the case of foreclosed housing from households, the provisioning coefficients are now set at: 10% (1st year); 20% (2nd year); 30% (3rd year) and 40% (4th year). For other loans with personal guarantees classified as substandard, the minimum provisioning coefficient increases from 10% to 24%.

As for the new general provisions, the idea was to prevent a macroeconomic deterioration from turning currently performing loans into non-performing ones. Importantly, this is only for outstanding loans as of December 2011 and it is not applicable to new loans. It is also worth noting that this is not a reform of the current Spanish dynamic provisioning scheme but a one-off measure (and does not enter into the definition of regulatory capital).

The new banking reform gave preferential treatment to institutions that present merger plans. In order to facilitate these processes, the FROB was allowed to buy shares of the institutions. These shares must be sold through a competitive procedure within a maximum period of 3 years. Importantly, the FROB was also allowed to provide funds to facilitate the processes through CoCos (convertible into shares within 5 years).

On June 9th, 2012, the Eurogroup published a statement in which they set up contingent financial aid for the recapitalization of Spanish banks for 100 billion euros. The aid was defined as a "loan amount" that "must cover estimated capital requirements with an additional margin of safety". Importantly, following the formal request for aid by the Spanish authorities –effectively made last June 25th - an assessment needs to be provided by the European Commission, the European Central Bank, the European Banking Authority and the International Monetary Fund. The conditionality is embedded in a Memorandum of Understanding (MoU). As specified in the Eurogroup statement, the financial assistance is expected to be provided by the European Financial Stability Facility (EFSF) or the European Stability Mechanism (ESM). Importantly, the Spanish government was expected to retain the full responsibility of the financial assistance. Additionally, the Eurogroup considers that the policy conditionality of the financial assistance should be "focused on specific reforms targeting the financial sector, including restructuring plans in line with EU state-aid rules and horizontal structural reforms of the domestic financial sector."

On August 31, 2012, the Spanish government approved the Royal Decree-Law 24/2012 on "a new framework for the restructuring and resolution of financial institutions". The title is quite illustrative on the aim of getting from restructuring measures to a final resolution setting for the banking crisis in Spain The Royal-Decree 24/2012 constitutes the first main step of the compliance with the MoU requirements. In particular, the new decree aims to meet, as a minimum, the following conditions of the MoU:

- "Introduce legislation to ensure the effectiveness of SLEs, (by End-August 2012).
- Upgrade of the bank resolution framework, i.e. strengthen the resolution powers of the FROB and the Deposit Guarantee Fund (DGF) (by End-August 2012).
- Prepare a comprehensive blueprint and legislative framework for the establishment and functioning of the Asset Management Company or "bad bank" (by End-August 2012).

Given the timeframe established by these MoU conditions, it is not surprising that the new decree was approved exactly on August 31, 2012, in time to comply with these time constraints. The Royal Decree-Law 24/2012 even includes pre-emptive action measures, as it shows some progress on commitments agreed to be implemented before the end of 2012, such as the strengthening of retail investor protection and the transfer of responsibilities for sanctioning and licensing of new banks from the Ministry of Economy and Competitiveness to the Bank of Spain.

Importantly, even if the MoU agenda was quite specific and clear in both its content and progress, the Royal Decree 24/2012 acknowledges that the implementation of the MoU is taking place within an environment of significant foreseeable regulatory changes in Europe that may force Spain to adopt some of these ongoing measures to a new EU legal framework, in particular where the provision of EU funds and the functioning of the available funding mechanisms (the EFSF and/or the ESM) are concerned. Specifically, in the motivation of the Royal Decree it is said that "as soon as the EU agrees on a legal text for a Directive on bailout and resolution mechanisms for banks, this decree will be adapted to that Directive".

The Royal Decree-Law 24/2012 included measures on six main subjects:

a) A new and strengthened framework for crisis management of financial institutions that allows for effective restructuring and orderly resolution if necessary.

b) Reinforcement of the FROB's intervention tools at all stages of crisis management.

c) Strengthening of the protection of retail investors.

d) Establishment of an Asset Management Company (AMC).

e) Burden sharing between the public and private sector of the cost of restructuring resulting from the restructuring of entities.

f) Other aspects, such as the strengthening of capital requirements, new limits on executive compensation and transfer of competences to the Bank of Spain.

As for the strengthened framework for crisis management of financial institutions, early intervention of a bank would take place in any of the following situations:

- Solvency requirements are not being met or there is a reasonable expectation that they will not be met.
- Liabilities of the bank are (or are expected to be) larger than the assets.
- Banks cannot (or are expected not to be able to) meet their financial commitments.

The decree provides the Bank of Spain with the power to directly remove the board of directors and other executive representatives of a bank. The Bank of Spain may also force the Board of Directors to set a board meeting and may force the board to negotiate a program of debt restructuring with the debtors of the institution. The orderly resolution of an institution might also take the form of partial business sales or an asset and liability sale to a bridge-bank (a bank where the assets are transferred and managed by the FROB) or to an asset management company.

As mentioned above, a troubled bank may be required to make asset sales and/or to transfer assets to the AMC. Additionally, the FROB may require the transfer of all assets to a so-called bridge-bank that would be controlled and managed by the FROB itself. The FROB should dispose of its capital shares in the bridge-bank in 5 years.

The FROB could also decide to provide financial aid to the acquirers of troubled banks to help in the restructuring of the bank without taking control of it. This way the FROB could eventually minimize the public funds used.

In the cases where the FROB decides to inject funds in a bank as part of a restructuring process or to support the acquirers of a troubled institution, the funds could be provided as ordinary shares or as CoCos (convertible bonds). As far as CoCos are concerned, the FROB can convert them into capital in the 6 months following the fifth year of their subscription. The six months deadline can be increased to 2 years depending on the entity's situation. As for the ordinary shares –as in the case of the bridge bank- the FROB should dispose them in 5 years.

The decree reinforced the FROB's powers, sharing some important supervision and discipline powers with the Bank of Spain. The decree highlights that "the FROB will be in charge of managing the restructuring and resolution processes in the Spanish banking sector". As described earlier, the FROB –in coordination with the Bank of Spain- may determine and monitor a number of early intervention actions and the current decree gives the FROB full rights to take control of financial firms and effectively manage them if necessary.

Another very relevant and controversial issue in the MoU was the burden sharing regime between the public sector and the private stakeholders. The Royal-Decree law 24/2012 defines this burden sharing as the owners of hybrid capital instruments could be forced to bear part of the losses of a troubled institution. According to the decree, "the objective is to reduce, to the maximum extent possible, the cost for taxpayers of restructuring, according to the European rules of state aids". The troubled banks themselves will be able to offer a number of possibilities to the owners of hybrid capital including haircuts on the value of the outstanding debt, the early buy back or anticipated sale of the debt instruments at discounted prices, a conversion of hybrid capital to any other form of equity capital or "any other instrument offered by the bank". Importantly if the FROB considers that the loss absorption by private owners is not enough, it will be able to impose on them specific exchange exercises. These exercises could consist of exchanges into capital instruments, direct or conditioned cash repurchases, or reduction and anticipated amortization of the nominal value of the instrument. All these actions will take into account market values, applying a haircut as established in the European rules.

Importantly, the Royal Decree Law 24/2012: a new minimum capital requirement. Specifically, the Tier 1 capital requirements of 8% and 10% at that time (8% as a general rule and 10% for entities with difficult access to capital markets and for those for which wholesale funding is predominant) became a single requirement of 9% that all the entities must comply with as of January 1st, 2013. The new regulation adapts the definition of the Tier 1 ratio to the one established in the European Banking Authority.

The approval by the European Commission of the plans for the four banks in which the Fund for the Orderly Restructuring of the Banking Sector (FROB) has a majority stake on November 28th, 2012, was a key milestone in the resolution of the banking crisis in Spain. These banks -classified as Group 1 according to the MoU criteria- were then set to receive the necessary equity funds to meet their capital requirements.

As for the effective implementation of the EU financial assistance program, the MoU text included 32 milestones to be completed over 2012 and 2013.

As previously stated, one of the latest recommendations of the MoU referred to the improvement in the decision-making and resolution powers of the Spanish supervisors. A major step in this direction was taken by the Bank of Spain in late September 2013, when the Executive Commission of the Bank of Spain approved an internal Circular of Procedures applied in the Directorate of General Banking Supervision (Internal Circular 2/2013), updating the rules that were in force at that time (Internal Circular 7/2011). The new Circular included a number of mandatory procedures that were undertaken by early 2014. In any event, the Bank of Spain acknowledged that the new procedures will very probably have to be updated once the Single Supervisory Mechanism (SSM) within the European Banking Union is in place in late 2014.

Also following the principles of the MoU- the FROB approved a "general framework for action to supplement its decision-making powers in relation to possible corporate operations". This general framework was announced in October 2013. This new framework is set to facilitate the success of corporate operations "to resolve credit institutions." The principles approved by FROB are mainly the following:

a) The main aim is to avoid problems of "fairness for the creditors or shareholders" of a bank resulting from the general rules applied.

b) A clear economic justification should be provided -and validated by an independent expert- to demonstrate the preservation of value for the FROB and the minimization of costs for taxpayers.

c) The principles set by the FROB should comply with the European rules on State aid.

Many of the principles of the MoU were effectively implemented in Spain by Law 9/2012 (14/11/2012) on restructuring and resolution of credit institutions, which raised the content of Royal Decree-Law 24/2012 and Royal Decree-Law 9/2009. Table 6 shows the main changes.

11. Accounting

Changes in accounting principles have been transversally introduced in several regulations in Spain. However, as for the transposition of the main EU principles, the first reference is Directive 86/635/EEC on annual and consolidated accounts of banks and other financial institutions. The due transposition date was 1993 but in Spain it was transposed earlier, in 1991. In particular, from 1988 to 1991 with Law 26/1988 (29/07/1988), on the

Discipline and Administration of Credit Institutions, the Bank of Spain Circular 18/89 (13/12/89) on financial repos and options, Royal Decree 1564/89 (22/12/1989) on public limited companies, Royal Decree 1643/1990 (20/12/1990) which approves the so-called "Plan General de Contabilidad" (General Accounting Rules) and, mainly, with Bank of Spain Circular 4/1991 (14/06/1991) on accounting rules and financial statement formats.

Bank of Spain Circular 4/1991 was largely modified by Bank of Spain Circular no. 4/2004 (22/12/2004) on the public and confidential bank reporting rules and financial statements formats in accordance to the transposition (due in 2004 and made by that date) of EC 1606/2002 (Regulation) and 2003/51/EC on the application of International Accounting Standards to annual and consolidated accounts of banks, financial institutions and insurance companies. The amendments of Circular 4/2004 do not alter significantly the guiding principles of on Circular 4/1991 in this area, namely to promote healthy, sound accounting and to minimise the costs and uncertainty that the coexistence of numerous accounting criteria would entail. THe accounting criteria and approaches of Circular 4/1991 of 14 June 1991 on Accounting Rules and Financial Statement Formats (hereafter, "4/91") were mostly retained in Circular 4/2004 and they were ingeneral in accordance with International Financial Reporting Standards (IFRS).

The adoption of the IFRS by the EU is part of the project to promote the formation of a European capital market, and to increase convergence with US accounting standards. However, the compatibility of Circular 4/2004 with the Community Regulation is no obstacle to its broader application with the aim of covering both accounting issues for external use and issues relating to the exercise of the powers and requirements of the Bank of Spain, especially in relation to supervision.

12. Conclusions

This paper analyses the implementation of the most important EU regulations regarding the financial system in Spain since the early 1980s to present. Overall, the implementation has been successful and has been timely. In any event, some specific observations can be made for the Spanish case:

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- The implementation process was particularly intense after 1986, when Spain joined the European Community. Spain was then going through an intense process of liberalization and some of the Directives that had to be transposed completed that process and set up the pillars of what we know today as the modern Spanish financial system.

- The implementation has been particularly intense and fast in what the solvency regulation is concerned. Some of the Directives on Capital Regulation following -Basel I and Basel II in particular- were implemented in advance in Spain.

- However, some other regulations, in particular those concerning capital markets, have normally required more time to be transposed or have had to be gradually implemented.

- Banks' supervision and prudential regulations have also been carefully implemented in Spain and some specific features not yet included in EU regulations –such as countercyclical provisions for bank losses- were already implemented in Spain since the early 2000s.

- The financial crisis has brought a number of significant changes beyond EU regulations for Spanish banks and it has shown that there was still substantial room for improvement in supervision and prudential regulations.

- The recapitalization and restructuring process and, in particular, the financial assistance program of the EU for Spanish banks, have brought a number of regulatory changes beyond EU Directives, in particular those concerning early-prompt corrective actions and bank resolution mechanisms, including burden sharing rules and other principles that will facilitate the adaptation of Spanish regulations to the forthcoming environment of the European Banking Union.

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Table 1. Composition of own funds in Spain in accordance to Basel I principles

Capital stock.
The initial fund (fondo fundacional).
Reserves
Generic banking provisions
Credit cooperative training and promotion funds
Subordinated financing and all other receivable or non-receivable items to be used to cover losses.
All losses and any assets that may reduce the effectiveness of said resources in covering losses shall be deducted from these resources.

Source: Law 13/1985.

Table 2. Transition from Basel I to Basel II in Spain: Bank of Spain Circulars 5/1993 and 3/2008.

Circular 5/1993 of 26 March 1993	Circular 3/2008 of 22 May 2008
Scope of application	
Groups and sub-groups of credit institutions, as well as individual credit institutions of Spanish nationality regardless of whether or not they form part of a group or sub-group of credit institutions	No significant changes
General minimum own funds requirements	
Institutions shall at all times hold a sufficient volume of regulatory own funds to cover certain risks (credit, foreign-exchange and gold position, trading book and commodity). They must comply with limits on risk concentration and tangible fixed assets, and comply individually with limits on foreign-exchange position risks. They must also have administrative and accounting procedures, risk management systems and internal control mechanisms appropriate to their size and to the diversity and complexity of their activities.	An institution shall at all times hold a sufficient volume of regulatory own funds to cover risks similar to those established in CBE 5/1993 (plus operational risk and dilution risk). Also, institutions must comply with the obligations relating to limits on large exposures, internal risk management, corporate governance, capital assessment, interest rate risk measurement and market disclosure.
Components of own funds	
Tier 1 capital	Tier 1 capital
Share capital of public limited companies, initial capital and non-voting equity units of savings banks, capital contributions of credit co-operatives and assigned capital of branches	No significant changes
Disclosed reserves, and funds similar to or reclassified as reserves	
Preference shares and non-voting shares not carrying cumulative dividend collection rights	Preference shares and non-voting shares ear-marked for the coverage of risks and losses in the event of general write-down, with undefined term, and which do not carry cumulative dividend collection rights. Limits are set on what can form part of tier 1 capital, unless there are clauses to ensure they can be converted into capital, and in the case of general
Tier 2 capital	Tier 2 capital
Asset regularisation, adjustment and revaluation	No significant changes

reserves The book value of the general loan loss provisions. Other non-voting shares and redeemable shares with a maturity of not less than five years	
Subordinated debt with a maturity of not less than five years	No significant changes (now known as "standard")
Subordinated debt with undefined maturity.	No significant changes
Not envisaged	Short-term subordinated debt: its original maturity must be no less than two years from the effective disbursement date and it may not contain rescue, repayment or early redemption clauses.
Not envisaged	Ancillary capital: for the coverage of position and foreign-exchange risk only
Solvency ratio	
Credit risk: the minimum capital requirements will be 8% of the result of the weightings of the various risk components.	Credit risk: The minimum capital requirements are 8% of the institution's total risk-weighted assets calculated by the standardized approach or, if authorized by the Bank of Spain, the internal ratings based (IRB) Included in credit risk is dilution risk, which arises from the possibility that an amount receivable acquired by a credit institution is reduced through credits to the obligor for reasons such as the commercial relationship between the obligor and the seller of the receivables.
Counterparty risk: the risk of counterparty default in derivatives transactions. Two valuation systems are established: at market prices and by the original exposure method.	Counterparty risk: The value of counterparty risk exposure can be calculated by various methods: original exposure method, mark-to-market method, standardized approach and internal model method.
Foreign-exchange and gold-position risk: not less than the sum of 8% of the net overall foreign-exchange position and 8% of the net gold position. However a ratio below 8% may be set in certain cases. Subject to certain requirements, institutions may use internal risk management models to determine the foreign-exchange and gold-position risk.	Foreign-exchange and gold-position risk: calculated under the standardized approach by multiplying by 8% the sum of the net overall positions in currencies, gold and reporting currencies. A minimum threshold is set equal to 2% of total regulatory own funds, below which these requirements are zero. For all or for a pool of foreign-exchange positions, this method may be replaced by internal models.
Trading book risk: in calculating capital requirements, regard shall be had to both the credit risk and the market risk on trading book business. Position risk shall be divided into a general risk and a specific risk. Thresholds shall be set below which the minimum requirement shall not apply. If certain requirements are met, internal risk management models may be used to determine the trading book and commodity position risks.	Trading book risk: the capital requirements shall be determined by the sum of the following requirements: that for price risk of fixed-income positions; that for price risk of commodities positions; that for price risk on positions in shares and other equity, including those in collective investment institutions; that for credit and counterparty risk linked to the trading book; that for clearing and delivery risk; and that for foreign exchange and gold position risks. Position risk

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	shall be broken down into a general risk and a specific risk. Credit institutions with a significant level of activity they may use their own internal risk management models to calculate their capital requirements. The exemption thresholds for little activity have undergone only small changes.
Not envisaged	Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, and includes legal risk. The methods for calculating capital requirements for operational risk are the basic indicator approach, the standardised approach and its variant the alternative standardized approach, and the advanced measurement approaches based on each institution's own measurement systems.
Limits on large exposures: an exposure is considered to be large if its value exceeds 10% of the credit institution's own funds. The value of all the exposures of a credit institution to one individual, institution or external economic group shall not exceed 25% of its own funds. The total large exposures shall not exceed 800% of the credit institution's own funds.	No significant changes
Adoption of measures to return to compliance with solvency regulations: if a regulatory capital shortfall exceeds 20% of the minimum requirement, all net profit or surplus must be allocated in full to reserves. If the capital shortfall is 20% or less, a proposed distribution of profits shall be submitted for authorization to the Bank of Spain, which shall set the minimum percentage to be allocated to reserves, although it may never be less than 50% of profits.	Adoption of measures to return to compliance with solvency regulations: if a regulatory capital shortfall exceeds 20% of the minimum requirement or tier 1 capital falls below 50% of that minimum requirement, all net profit or surplus must be allocated in full to reserves, although the Bank of Spain is empowered to authorise other action in the event that the programme submitted by the institution for restoring compliance with capital requirements is approved. If the capital shortfall is 20% or less of the minimum requirement, a proposed distribution of profits shall be submitted for authorisation to the Bank of Spain, which shall set the minimum percentage to be allocated to reserves (the limit of 50% of profits no longer applies).
Governance, organisational structure, risk management and internal control procedures	
Institutions must have an organisational structure commensurate with the volume of the risks managed by them. In particular, they must have a risk control department or unit which is independent from the operating units, and their staff must be competent in using risk control models.	Organisational structure. Institutions must have: an organisational structure appropriate to the nature of their activities, with well defined, transparent and consistent lines of responsibility; an internal audit function which oversees the smooth working of the information and internal control systems; a unit to carry out the regulatory compliance function; and adequate internal control mechanisms, including sound administrative and accounting procedures.

Not envisaged	Assessment of on-balance-sheet interest rate risk: establishment of specific procedures to assess and manage this risk. Institutions shall, among other things, analyse the effect that interest rate risk may have on their future solvency and stability when the potential impact of that risk is negative and exceeds certain thresholds.
Not envisaged	Internal capital adequacy assessment process: institutions shall specifically have sound, effective and exhaustive strategies and procedures to assess and maintain on an ongoing basis the amounts, types and distribution of internal capital and own funds that they consider adequate to cover the nature and level of the risks to which they are or might be exposed. A yearly internal capital adequacy assessment report shall be sent to the Bank of Spain.
Not envisaged	Review and assessment by the Bank of Spain: if a supervised credit institution or group or sub-group of credit institutions does not have adequate corporate governance procedures or if its internal capital adequacy assessment process is inadequate, it has to prepare a compliance and capital adequacy programme which shall be submitted to the approval of the Bank of Spain.
Disclosure	
Not envisaged	Obligation to publish the document "Prudential information". The Circular stipulates the minimum content of this document to ensure that the disclosures made by institutions are comparable and establish the principles on which an institution's disclosure policy should be based. This document must be made public at least annually, at the same time the annual accounts are issued. However, depending on the circumstances, the Bank of Spain may require more frequent disclosure and stipulate deadlines. The institutions themselves may also increase the frequency of such public disclosures if considered appropriate in view of the characteristics of their business. The disclosures to be made in this document centre on key aspects of an institution's business profile, risk exposure and means of managing risk. In particular, disclosure should be made of risk management objectives, the institution's strategies and processes to manage those risks, the scope and nature of risk reporting and measurement systems, and the policies for hedging and mitigating risk

Source: Bank of Spain and own elaboration.

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Table 3. Spanish regulations concerning the Central Credit Register

Bank of Spain Circular 3/1995 on the Central Credit Register.
Law 44/2002 (22/11/2002) on "measures to reform the financial system)
Ministerial Order ECO/697/2004 (11/32004) on the reform of the Central Credit Register
Ministerial Order ECC/747/2013 (25/4/2013) which modifies Ministerial Order ECO/697/2004 (11/32004) on the reform of the Central Credit Register.
Bank of Spain Circular 1/2013 (24/05/2013) on the reform of the Central Credit Register.

Source: Bank of Spain and own elaboration

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Table 4. Implementation of some of the principles of the EU's Memorandum of Understanding under Law 9/2012 and changes with respect to Royal Decree/Law 9/2009.

ROYAL DECREE-LAW 9/2009 (26/06/2009)	LAW 9/2012 (14/11/2012)
Management of crises affecting credit institutions	
Not specifically envisaged	Early action measures: provided for institutions that may be viable on the basis of their own funds, but which may require exceptional, temporary assistance, through contributions to share capital, purchase of ordinary shares or instruments convertible into shares, to be repaid within two years.
Restructuring processes: two phases are envisaged. The first, with the submission of the plan of action setting out the actions planned to overcome the situation of financial weakness. When the plan of action is insufficient, the restructuring process is initiated with the intervention of the FROB. Its objective is to support integration processes or the transfer of all or part of the banking business. The FROB can provide temporary financial support to the restructuring process	Restructuring processes: envisaged for institutions displaying temporary weaknesses that may be overcome by means of public financial support, to be repaid within a five-year period, extendable by no more than two years. The restructuring instruments that the FROB may implement (individually or jointly) are two: 1) public financial support, and 2) the transfer of assets or liabilities to the Asset Management Company (AMC).
Not specifically envisaged.	Orderly resolution of institutions: applied to unviable credit institutions. The resolution instruments that may be adopted by the FROB (individually or jointly) are: 1) sale of the business or the institution; 2) transfer of assets or liabilities to a bridge bank; 3) transfer of assets or liabilities to the AMC, and 4) financial support for acquirers of the business, the bridge bank or the AMC.
Composition and powers of the FROB	
The FROB is governed by a Governing Committee with eight members: five proposed by the Banco de España and three of which correspond	The Governing Committee is made up of representatives of the Ministry of Economic Affairs and Competitiveness, the Ministry of

to the Deposit Guarantee Fund	Finance and Public Administration (five members) and the Banco de España (four members). It will have a general manager with full executive powers
It has a capital endowment financed from the State budget and the contributions of the Deposit Guarantee Fund. In addition, it may raise funds on the securities markets by issuing fixed-income securities, taking out loans, requesting the opening of credit facilities and conducting any other debt operation, although such funds may not amount to more than three times the value of the capital endowment existing from time to time. However, as from 1 January 2010, funding beyond this limit may be authorised, although external funds may in no event amount to more than ten times the capital endowment.	It has the capital endowments that may be financed from the State budget. In addition, to achieve its purposes, the FROB may raise funds by issuing fixed-income securities, taking out loans, requesting the opening of credit facilities and conducting any other debt operation. The external funds obtained must not exceed the limit established in the State budget.
The FROB basically has two functions: management of the restructuring processes (by means of financial support and management measures to improve the organisation and the procedural and internal control systems), and the strengthening of the capital of institutions with the exclusive purpose of carrying out integration processes.	The FROB manages credit institution restructuring and resolution processes with the instruments mentioned above.
Not envisaged.	In cases of restructuring or resolution of credit institutions that belong to international groups, the FROB will collaborate with the EU institutions, including the European Banking Authority, and with foreign authorities with the relevant responsibilities, and may conclude collaboration agreements and exchange information for the exercise of its powers.
Burden sharing system for the costs of institution restructuring or resolution	
Not envisaged.	The distribution of the costs of restructuring or resolution of institutions is addressed, and the mechanism

	established whereby the holders of hybrid capital instruments (preference shares, convertible bonds, subordinated bonds or any other subordinated financing obtained by the credit institution) may be obliged to assume part of the losses of an an institution in crisis.
Asset Management Company and SAREB	
	Its purpose is to concentrate those assets considered to be troubled or that may damage the balance sheet of credit institutions or that are considered to reduce their viability, in order to remove them from institutions' balance sheets and allow them to be realised separately

Source: Bank of Spain.

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THE ABSTRACT OF THE PROJECT IS:

The research programme will integrate diverse levels, methods and disciplinary traditions with the aim of developing a comprehensive policy agenda for changing the role of the financial system to help achieve a future which is sustainable in environmental, social and economic terms. The programme involves an integrated and balanced consortium involving partners from 14 countries that has unsurpassed experience of deploying diverse perspectives both within economics and across disciplines inclusive of economics. The programme is distinctively pluralistic, and aims to forge alliances across the social sciences, so as to understand how finance can better serve economic, social and environmental needs. The central issues addressed are the ways in which the growth and performance of economies in the last 30 years have been dependent on the characteristics of the processes of financialisation; how has financialisation impacted on the achievement of specific economic, social, and environmental objectives?; the nature of the relationship between financialisation and the sustainability of the financial system, economic development and the environment?; the lessons to be drawn from the crisis about the nature and impacts of financialisation? ; what are the requisites of a financial system able to support a process of sustainable development, broadly conceived?'

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THE PARTNERS IN THE CONSORTIUM ARE:

Participant Number	Participant organisation name	Country
1 (Coordinator)	University of Leeds	UK
2	University of Siena	Italy
3	School of Oriental and African Studies	UK
4	Fondation Nationale des Sciences Politiques	France
5	Pour la Solidarite, Brussels	Belgium
6	Poznan University of Economics	Poland
7	Tallin University of Technology	Estonia
8	Berlin School of Economics and Law	Germany
9	Centre for Social Studies, University of Coimbra	Portugal
10	University of Pannonia, Veszprem	Hungary
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