

ANNEX I

**BASIC REGULATORY STRUCTURE
OF THE
SPANISH BANKING SYSTEM**

The dispersed regulatory framework to which the activity of credit institutions (CIs) is subject can be divided into three areas: taking up of the business of credit institutions, pursuit of such business and possible corrective measures (including those applicable in the event of crisis).

Before briefly discussing each of these areas, it should be pointed out that CIs are traditionally defined as undertakings whose business is to receive deposits or other repayable funds from the public and to grant credits or undertake similar transactions for their own account (1). What distinguishes them from other financial intermediaries is that deposit-taking is their exclusive preserve (while all financial intermediaries can issue securities under securities market regulatory and disciplinary rules) (2).

Credit institutions – commonly known as banking or deposit institutions – include banks, savings banks and credit co-operatives (3) which, notwithstanding their different commercial features, operate under a practically identical regime. Specialised credit institutions (SCIs) are also considered as CIs, although their more specialised credit activity may not be funded through deposit-taking (4).

Directives 2000/28/EC and 2000/46/EC of the European Parliament and of the Council, both of 18 September 2000, have recently extended the traditional definition of credit institution to a new type of financial institution, namely electronic money institutions, whose main activity is the issuance of means of payment in the form of electronic money. These Directives are pending transposition into Spanish law (5).

I. FRAMEWORK REGULATING THE TAKING UP OF THE BUSINESS OF CREDIT INSTITUTIONS

A quick look at our more recent past shows that the first relaxation of the prohibition on setting up banks, which had been in force in Spain from 1940 (period known as the “bank-

(1) Article 1(1) of Royal Legislative Decree 1298/1986 of 28 June 1986 on the adaptation of the law regulating credit institutions to Community law, which transposes the equivalent provision laid down in article 1(1) of Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions. This Directive, hereinafter the “Banking Directive”, is a codification of several banking Directives, now repealed (73/183/EEC, 77/780/EEC, 89/299/EEC, 89/646/EEC, 89/647/EEC, 92/30/EEC, 92/121/EEC, together with their amendments).

(2) Article 28(2)(b) of Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions (LDI).

(3) The Official Credit Institute is also considered as a credit institution. However, as it is a State Finance Agency, it is regulated under a special regime.

(4) First additional provision to Law 3/1994 of 14 April 1994 and section 4 of the seventh additional provision of RDL 12/1995 of 28 December 1995.

(5) Part of the transposition is contained in the Bill on Reform of the Financial System (*Boletín del Congreso de los Diputados*, 8 March 2002).

ing *status quo*”), occurred in the 1960s, as part of the economic liberalisation that took place at that time. The first announcement of the liberalising course that was to be followed in subsequent years was Law 2/1962 of 14 April 1962 on credit and banking. Another significant step in this process was the nationalisation, in 1962, of the Banco de España (BE), which was made responsible for supervising private banks.

While the above-mentioned Credit and Banking Law distinguished between commercial and industrial banks, its subsequent implementing provisions tended to blur this distinction. This was clearly reflected in Decree 2246/1974 of 9 August 1974, the most direct antecedent of the current regulation on the establishment of banks. Under this provision, the setting up of a credit institution was subject to authorisation, but this was still granted only on a discretionary basis, applying the criterion of economic needs of the market.

Another major milestone in this liberalisation, since it fostered competition, was the entry of foreign banks into Spain in 1978, although their activity was subject to a restrictive structural and operational regime, which only began to become more flexible in 1986 when Spain joined the European Community.

Savings banks were naturally also affected by the reforms. Originally established as public or private charitable foundations, linked to the pawnbroking institutions created in Spain in the 18th century, their role as financial intermediaries was enhanced by the 1962 Credit and Banking Law and confirmed by subsequent developments. In 1971 they were placed under the supervision of the BE; in 1975 the creation of new savings banks was regulated (some of these provisions are still in force); and in 1977, they became subject to the same regulatory treatment, insofar as their operations are concerned, as banks. Moreover, regional governments gradually assumed powers over savings banks as well as over credit co-operatives, as laid down in the Spanish Constitution of 1978.

More recently, Spain’s accession to what is now known as the European Union (EU) has determined the latest legislative changes in the conditions for taking up the business of credit institutions in our country.

First, the regulations on the establishment of credit institutions were adapted to the provisions of Council Directives 73/183/EEC of 28 June 1973 and 77/780/EEC of 12 December 1977. The former required the abolition of restrictions which prevented institutions from establishing a presence or providing services in other Member States under the same conditions as national institutions. The latter directive, known as the First Banking Co-ordination Directive (IBCD), established a single definition of credit institution and harmonised conditions for authorisation (separate own funds, two persons who effectively direct the business of the credit institution and who are of sufficiently good repute and have adequate experience, a programme of operations). The granting and possible revocation of authorisation were regulated, thus preventing the application of the “economic needs” criterion (6).

Subsequently, in 1994 and 1995 (7) Spanish law was adapted to Council Directive 89/646/EEC of 15 December 1989, known as the Second Banking Co-ordination Directive (2BCD),

(6) Part of these Directives having been transposed through Royal Legislative Decree 1298/1986 of 28 June 1986, in 1987 the conditions for the taking up of the business of credit institutions were incorporated into the various regulations on the establishment of each type of entities then in force, harmonising the authorisation process for national and foreign banks. Notwithstanding, under the transitory regime provided for Spain in the Annex to the IBCD, the criterion of economic need could be applied until 31 December 1992.

(7) Law 3/1994 of 4 April 1994 adapting Spanish law on credit institutions to the 2BCD and introducing other changes in the financial system, and Royal Decree 1245/1995 of 14 July 1995 on the establishment of banks, cross-border activities and other issues relating to the legal regime of credit institutions.

which extended the harmonised conditions for authorisation (initial capital of € 5 million and suitability of shareholders that have qualifying holdings) and established the principle of a single licence or passport to operate throughout the Community. The 2BCD also regulated the taking up of the business of credit institutions through the acquisition of qualifying holdings.

The description of the regulatory process which has led to the current legislation on the taking up of the business of credit institutions shall now be followed by a short analysis of the current provisions regulating the establishment of the various types of CIs in the Spanish banking system, the control procedures applicable to shareholding changes and the regulation of cross-border activities.

1.1. Establishment of new institutions

Banks

Under the relevant provisions of Royal Decree 1245/1995 of 14 July 1995, based on article 43 of Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions (LDI) (8) the establishment of Spanish banks is subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE. The Royal Decree defines the procedure to be followed and the conditions to be complied with to obtain and retain authorisation to operate as a bank (see Box A.I.1).

Requeriments for the establishment of new credit institutions	BOX A.I.1
<p><i>Banks:</i> the establishment of new Spanish banks, as well the merger of existing ones, is subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE, under the following conditions:</p>	
<p><i>Corporate conditions</i></p> <ul style="list-style-type: none"> — Public limited company incorporated through the simultaneous formation procedure. — Initial capital: € 18 million. — Corporate purpose limited to the specific activities of credit institutions. — No special advantages or remuneration to founders. — Registered office and effective management of business within national territory. 	
<p><i>Viability of business project</i></p>	
<p><i>Administration and general management</i></p> <ul style="list-style-type: none"> — Board of Directors composed of at least five members. — Professional reputation (as specifically required). 	
<p><i>Organisation</i></p> <ul style="list-style-type: none"> — Good administrative and accounting organisation. — Adequate internal control procedures to ensure sound and prudent management. 	
<p><i>Shareholders</i></p> <ul style="list-style-type: none"> — Suitability of shareholders possessing qualifying holdings (5 % or more of capital or voting rights). 	
<p><i>Membership of Deposit Guarantee Fund</i></p>	
<p><i>Savings banks:</i> both State law and provisions issued by regional governments that have assumed powers over the establishment or merger of savings banks with registered office within their territory set out requirements similar to those listed above, with the exception of the shareholder structure (there are no shareholders in savings banks which are foundations).</p>	
<p><i>Credit co-operatives:</i> State law and regional provisions are based on substantive criteria similar to those listed above, although lower and different initial capital requirements are applied, depending on the territory within which these banks propose to operate. Power to grant authorisation is vested in the competent regional body when the credit co-operative intends to be established within the territory of the region concerned or will have its registered office there as the result of a merger.</p>	
<p><i>Specialised credit institutions:</i> substantive conditions and procedures relating to the establishment or merger of specialised credit institutions are very similar to those applicable to banks, although with lower initial capital requirements, owing to their more specialised corporate purpose.</p>	
<p>The monitoring of shareholders with qualifying holdings in a credit institution is not limited to the establishment of the institution, but extends to all the successive changes in the shareholder structure that take place over the whole life of the entity.</p>	

(8) As amended by Law 3/1994 of 14 April 1994.

Shareholder suitability is assessed on the basis of several factors, such as reputation, the possession of adequate assets to fulfil obligations, the institution's exposure to non-financial activities of the proposed shareholders, transparency of group structure, as well as the existence of any "close links" that may prevent the effective exercise of supervision (9).

European Community criteria are tightened under Spanish law inasmuch as Spanish law requires a higher number of persons to effectively direct the business, requires a higher amount of initial capital, sets a lower threshold for the level of shareholdings to be subject to monitoring, and introduces additional factors to assess suitability (adequate assets and involvement in non-financial activities).

When a new bank is to be controlled by a natural or legal person authorised in another EU Member State, before issuing its opinion the BE shall consult the supervisory authorities concerned. When it is to be controlled by a natural or legal person established or authorised outside the EU, the applicant may be required to provide additional guarantees and authorisation may be suspended, refused or limited if EU credit institutions are not granted comparable treatment in respect of competitive opportunities or effective market access in the applicant's home country.

In order to reinforce the initial stability of new banks, Spanish law, unlike Community law, lays down certain periods during which their activities are subject to restrictions. Specifically, during the first three years they shall not distribute dividends and during the first five years they shall not extend credit to shareholders, directors or senior officials (or related companies), nor shall any non-financial corporation (or group) hold, directly or indirectly, more than 20 % of the capital or a controlling interest in the bank.

Finally, mergers between banks are also subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE (10).

Savings banks

The establishment of savings banks is regulated by RD 1838/1975 of 3 July 1975, subsequently adapted to reflect Community law, with the exception of conditions applicable to the shareholder structure, since savings banks have no shareholders. The provisions laid down in the aforementioned Royal Decree are similar to those for banks in respect of initial capital, programme of operations, management and effective direction of business within the national territory, etc. Both establishment and merger are subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE.

Nevertheless, having regard to the distribution of powers laid down in the Spanish Constitution, to Law 31/1985 of 2 August 1985 on the regulation of the basic rules relating to the governing bodies of savings banks, and to the construction criteria of the Constitutional Court (11), regional governments have assumed extensive powers over savings banks established within their territory. Under these powers, which are laid down in their respective statutes of autonomy, regional governments have issued a wide range of provisions. Specifically, the establishment or merger of savings banks that have or propose to have their head office within their territory are subject to authorisation by the regional Department of Economy or similar authority.

(9) This last criterion was laid down in Directive 95/26/EC (known as the "Post-BCCI Directive"), amending the IBCD, and was incorporated into Spanish law through the first additional provision to Royal Decree 692/1996 of 26 April 1996.

(10) Article 45(c) of the Banking Law of 31 December 1946.

(11) In particular, judgments of the Constitutional Court 48 and 49/1988 of 22 March 1988.

As a result, a complete description of the conditions for the establishment or merger of savings banks would need to take into account the detail of the above-mentioned regional provisions, which goes beyond the objective of this report. However, it should be noted that, whatever the competent authority may be, the Constitutional Court has resolved that authorisation shall in all cases require a prior opinion from the BE (12).

Credit co-operatives

At the State level, the legal regime for this type of credit institution, including establishment or merger conditions, is regulated by Law 13/1989 of 26 May 1989, implemented by RD 84/1993 of 22 January 1993. To these provisions should be added those that may be issued by regional governments that have assumed powers in this field, as well as the general law on co-operatives (13), which is applicable when higher-level sectoral regulations do not apply.

This regulation incorporates the conditions for the taking up of the business and the reasons for refusing authorisation, which are similar to those applicable to banks, with the exception of a number of features derived from their corporate regime. Specifically, credit co-operatives are subject to lower initial capital requirements which, within the limits established by Community law, differ according to the territory within which they intend to operate and to the total number of inhabitants of the municipalities included in such territory.

Regional governments have also assumed powers over credit co-operatives within the framework of State law, although to a lesser extent than with savings banks. However, the establishment or merger of credit co-operatives is subject to authorisation by the Minister of Economy, except when the proposed establishment or merger is limited to the regional territory (14).

Specialised credit institutions

Legally provided for since 1994, and successors to the former *entidades de crédito de ámbito operativo limitado*, specialised credit institutions are regulated by RD 692/1996 of 26 April 1996 as far as their establishment and merger are concerned.

The above-mentioned Royal Decree lays down substantive conditions and procedures on the taking up of business, which are very similar to those applicable to banks, including consultation of the supervisory authority of the home country when the institution is to be controlled by legal or natural persons established in another EU Member State. However, these companies are subject to lower initial capital requirements, owing to their more specialised corporate purpose (which is limited to the performance of several types of credit operations, the management or issuance of credit cards and the provision of guarantees) and to the fact that they are not allowed to receive deposits from the public.

1.2. Qualifying holdings

As mentioned above, the suitability of shareholders is not only assessed at the time of the establishment of a credit institution but also whenever any change is made in the shareholder

(12) Judgments of the Constitutional Court 1/1982 and 48/1988.

(13) Law 27/1999 of 16 July 1999 on co-operative banks and relevant regional provisions.

(14) Judgments of the Constitutional Court 134/1992 of 5 October 1992 and 275/2000 of 16 November 2000 on the distribution of powers.

structure of already authorised entities. Although there were legal precedents for the monitoring of suitability, the provisions now in force, which date back to 1994 and are laid down in Title VI of the LDI and article 18 of RD 1245/1995 of 14 July 1995, are in line with Community law.

These provisions are based on the definition of qualifying holding, i.e. a direct or indirect holding in an undertaking which represents 5 % or more of the capital or of the voting rights (quantitative criterion) or which, even if falling below this proportion, makes it possible to exercise a significant influence over the undertaking (qualitative criterion). It is assumed that a significant influence is exercised when the holding allows for the appointment or removal of a member of the credit institution's board of directors.

Any natural or legal person who proposes to acquire a qualifying holding or to increase the proportion of an existing holding shall be required to inform the BE, in particular if, as a result of the acquisition, the institution would become subject to the control of the acquirer.

The BE shall have a maximum of three months from the date of the notification to oppose such a plan, if it is not satisfied as to the suitability of the acquirer assessed in the light of the conditions described in section 1.1 above. If as a result of the acquisition the credit institution would become subject to the control of a legal or natural person authorised in another EU Member State, prior consultation with the supervisory authorities of the home Member State is required. If control would be exercised by a legal or natural person established outside the EU, the acquisition could be subject to limitations, suspension or refusal.

Failure to comply with the obligation to provide prior information, or the acquisition of holdings before the BE has taken a decision or despite its opposition, may result in sanctions and the suspension of the exercise of the voting rights attaching to the improperly acquired shares.

Credit institutions shall inform the BE on becoming aware of any transfers of holdings in their capital that exceed 1 % of the same. They shall also report their shareholder structure to the BE on a regular basis.

1.3. Cross-border activities

Cross-border activities covering both foreign credit institutions operating in Spain and Spanish credit institutions operating abroad are regulated in Chapters I and II, Title V, of LDI, implemented by Title II of RD 1245/1995 of 14 July 1995.

1.3.1. Activities of foreign credit institutions in Spain

Credit institutions authorised in another EU Member State

Under Community law, the authorities of an EU Member State may not prevent credit institutions authorised in another Member State from operating within their territory. This principle of single license, or Community passport, is based on the existence of harmonised conditions required to obtain authorisation and pursue the business of credit institutions (basically relating to the supervision of their solvency on a consolidated basis by the authorities of the home country).

The activities subject to mutual recognition are listed in Box A.1.2 and constitute the core banking business which corresponds to the principle of universal banking. The sole significant exception is that CIs are not allowed to engage directly in insurance activities.

Activities subject to mutual recognition

- Acceptance of repayable funds from the public.
- Lending.
- Factoring and financial leasing.
- Payment transactions, payment services and transfers.
- Issuing and administering means of payment (e.g. credit cards, travellers' cheques and bankers' drafts).
- Guarantees and similar commitments.
- Intermediation on interbank markets.
- Trading for own account or for account of customers in transferable securities and financial instruments.
- Participation in securities issues and intermediation for own account or for account of the issuer in the placement and underwriting of such issues.
- Advice and services to undertakings on capital structure, industrial strategy, mergers and acquisitions and related matters.
- Portfolio management and advice.
- Safekeeping of securities evidenced by physical documents and administration of securities evidenced by book entries.
- Credit reference services.
- Safe custody services.

On receipt by the BE of a communication from the supervisory authority of the home Member State with the relevant information, EU credit institutions may commence the above-mentioned activities in Spain.

Credit institutions not authorised in another EU Member State

As these CIs do not benefit from Community harmonisation, the establishment of branches of such institutions in Spain is subject to authorisation according to the same procedure as that applicable to the establishment of new Spanish banks, with certain differences derived from the fact that the branches do not have an independent legal status. In this case, authorisation may be refused not only as a result of failure to comply with the prescribed conditions but also on the basis of the principle of reciprocity.

Representative offices

This category, which is not regulated under Community law, includes representative offices of foreign credit institutions, whatever their nationality, operating in Spain. Their activities are restricted to the provision of information and to marketing in the banking, financial or economic areas and their establishment is subject to authorisation by the BE.

1.3.2. Activities of Spanish credit institutions abroad***Activities in another EU Member State***

In accordance with the single licence principle, whenever the BE is notified that a Spanish credit institution proposes to establish a branch or to exercise the freedom to provide services

within the territory of another EU Member State, the BE shall communicate that information to the supervisory authority of the host Member State.

This notwithstanding, the BE may oppose the establishment of the proposed branch if the programme of operations presented includes activities that the credit institution is not authorised to undertake or if the BE has reason to doubt the adequacy of the administrative structure or the financial situation of the credit institution, taking into account the activities envisaged.

Whenever a Spanish credit institution intends to establish a subsidiary or acquire a qualifying holding or a controlling interest in an EU entity, the host Member State shall apply the relevant harmonised provisions, which are equivalent to those laid down in Spanish regulations, after consulting the BE in its capacity as home supervisory authority.

Activities in a non-EU Member State

Without prejudice to the requirements to be fulfilled in the host country, the establishment of branches is subject to authorisation by the BE under the same conditions as discussed above. The BE may oppose such plan if it considers that the branch shall not be subject to effective control by the supervisory authority of the host country or if there are legal or other impediments preventing or hindering its supervision. As regards freedom to provide services, credit institutions are only required to inform the BE of their intention.

The creation of a subsidiary or the acquisition of a holding in an existing credit institution are subject to authorisation by the BE. Such authorisation may be refused if it is considered that, in the light of the financial situation of the institution or its management capacity, the plan may adversely affect the credit institution, the effective supervision of the group may not be ensured or the activity of the controlled institution is not subject to effective control by the national supervisory authority.

2. REQUIREMENTS FOR THE PURSUIT OF THE BUSINESS OF CREDIT INSTITUTIONS

2.1. Reserve requirements

Until 31 December 1998 the definition and implementation of monetary policy fell within the competence of the BE. This task included the possibility of requiring CIs to hold minimum reserves calculated as a percentage of reimbursable funds, which could vary in scope and amount and was called the cash ratio.

Since 1 January 1999, the date on which Spain adopted the single currency in Stage Three of Economic and Monetary Union, this function has been assumed by the European System of Central Banks (ESCB), as provided for in the Treaty establishing the European Community (15) and the Statute of the ESCB and of the European Central Bank (ECB) (16).

The regulations concerning the minimum reserve system now in force were issued pursuant to article 19 of the Statute. Under these regulations, CIs are required to hold minimum

(15) Articles 105 and following of the consolidated version of the Treaty establishing the European Community.

(16) Protocol annexed to the Treaty on European Union.

reserves in reserve accounts with the national central banks of the countries where they are established. Therefore, the required percentage of funds accepted by CIs in each Member State shall be held in accounts with the respective national central banks.

Council Regulation (EC) No 2531/98 of 23 November 1998 (17) established the basis for minimum reserves (which mainly include liabilities of the institution resulting from the acceptance of funds and from off-balance-sheet items), the reserve ratios (which shall not exceed 10 %, though different reserve ratios may be set for specific categories of liabilities) and the sanctions which may be imposed in cases of non-compliance with reserve requirements (18).

Regulation (EC) No 2818/98 of the European Central Bank of 1 December 1998 specified the institutions subject to reserve requirements, the liabilities included in the reserve base (deposits, debt securities issued by the institution and money market paper), the reserve ratio (0 % for specified transactions with maturity over two years and 2 % for all other liabilities included in the reserve base), the allowance to be deducted from the amount of each institution's reserve requirements (€ 100,000), the maintenance period and the remuneration on such holdings. The Regulation permitted, under certain conditions, the indirect holding of minimum reserves through an intermediary also subject to the same requirements.

2.2. Solvency ratio

2.2.1. Historical background and current regulations

The first Spanish regulations in this field, issued in 1962, established the so-called “guarantee ratio”, whereby individual institutions were required to maintain own funds in excess of a given percentage of their borrowed funds. However, the concept of own funds was rather imprecise, and different definitions applied to different institutions. Moreover, the ratio did not cover the whole amount and range of risks incurred and it ignored the existence of financial groups.

Substantial progress was achieved with Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting requirements for financial intermediaries, and its implementing provisions, which embodied the main lines of the regulations in force. These provisions extended the definition of own funds to include subordinated debt (19), introduced a risk weighting system with differing ratios according to the various types of assets and commitments, and imposed the same requirements on all CIs, which were also required to ensure compliance on a consolidated basis.

The following step was the full adaptation of regulations to the Community solvency Directives adopted since 1989 (20), which set out the basic common standards to be transposed to national legislation, although more stringent provisions than those laid down in these Directives may be applied to national CIs.

(17) Recently amended by Council Regulation (EC) No 134/2002 of 22 January 2002, which extended to two months the period for the ECB Governing Council to take a decision on the review procedure for the imposition of sanctions.

(18) The infringement procedure is described in section 3.1 of this Annex.

(19) From a legal viewpoint, subordinated debt ranks after unsecured credits in the assignment of loans on a priority basis [article 20(1)(g) of Royal Decree 1343/1992 of 6 November 1992].

(20) Council Directive 89/299/EEC of 17 April 1989 on the own funds of credit institutions, Council Directive 89/647/EEC of 18 December 1989 on a solvency ratio for credit institutions, Council Directive 92/30/EEC of 6 April 1992 on the supervision of credit institutions on a consolidated basis, Council Directive 92/121/EEC of 21 December 1992 on the monitoring and control of large exposures of credit institutions (incorporated into the Banking Directive) and Council Directive 93/6/EEC of 15 March 1993 on the capital adequacy of investment firms and credit institutions.

The current regulatory framework is based on Law 13/1992 of 1 June 1992 on the own funds and the supervision of financial institutions on a consolidated basis, which amended Law 13/1985 in respect of CIs and also dealt with the parallel regime applicable to securities firms, insurance companies and groups incorporating both. As far as CIs are concerned, the Law was implemented by lower-level provisions (21) down to the level of detail established by the Banco de España Circular CBE 5/1993 of 26 March 1993 on the calculation and control of minimum own funds, issued pursuant to the powers conferred on the BE under higher-level comprehensive regulations.

2.2.2. Scope of application. Consolidated institutions and consolidated groups of credit institutions

The regulations apply to consolidated groups and subgroups of CIs, as well as to individual institutions not included in a group. The provisions do not apply to the Spanish branches of credit institutions authorised by other EU Member States since prudential supervision is entrusted to the home country. The regulations do apply to Spanish branches of non-EU credit institutions, although they may be exempted if they fulfil specific requirements.

In order to ensure the adequate distribution of risks within the group, Spanish regulations incorporate individual capital requirements for subsidiaries included in a consolidated group or subgroup. However, these requirements may be less stringent than the consolidated ones, depending on the parent company's participating interest.

The regulations address the scope of consolidation (22) from a two-fold perspective: activity and degree of control. With respect to activity, all types of intermediaries usually undertaking financial activities (with the exception of insurance companies), as well as special purpose vehicles, whose activity is an extension of the business of a financial institution or consists of providing ancillary services to the group, are eligible for consolidation. As regards control, the regulations refer to article 4 of Law 24/1988 of 28 July 1988 on the Securities Market (LSM), which established the principle of the management unit determining the origin of consolidation, it being understood that these circumstances occur when the prerequisites set out in mercantile regulations (23) are fulfilled or when the majority of the directors of the controlled institution are senior managers of the controlling institution or of other entities controlled by the latter.

As for the structure of consolidated groups and subgroups of credit institutions (CGs), Spanish law, in line with Community law, refers to vertical consolidation (where the group parent company is a Spanish credit institution or a Spanish company holding shares or other equity in CIs), though it goes further than this, dealing also with cases in which the parent company is a Spanish non-financial holding company and other cases of "horizontal" consolidation (groups with a non-consolidated parent company).

Although only rules applicable to CGs or to individual CIs are discussed herein, it should be pointed out that these CIs may be incorporated into groups whose parent company is an investment firm or a holding company basically oriented towards securities (in which case there will be a consolidated group of investment firms) or into groups which include non-credit financial institutions (called other consolidated groups of financial institutions). All these cases

(21) Royal Decree 1343/1992 of 6 November 1992 and Ministerial Order of 30 December 1992.

(22) The consolidation procedures are described in detail in provisions 18 to 22 of CBE 4/1991 of 14 June 1991 on CI accounting.

(23) Article 42(1) of the Commercial Code.

are subject to specific more stringent rules, which encompass not only the solvency requirements applicable to the CIs included in the group but also the specific requirements imposed upon the other financial institutions of the group.

Finally, both Community and Spanish law exclude the consolidation of insurance companies with CIs or investment firms. However, under Spanish law, groups including such companies – non-consolidated mixed groups of financial institutions – are required to apply a net aggregation system to the own funds and solvency requirements of the institutions or consolidated groups included in the aforementioned groups, in accordance with the requirements laid down in their own regulations, subject to certain adjustments (24).

2.2.3. Own funds

Broadly in line with Community law, Spanish regulations distinguish between two types of funds, tier 1 and tier 2 funds, according to the extent to which they fulfil the typical functions of capital (capacity to absorb losses and indefinite availability to the institution). A series of items are deducted from these funds in order to ensure that they are used within the scope of the above-mentioned functions, to avoid double counting of own funds and to reduce the risk of contagion from other non-financial activities.

Box A.1.3. enumerates the eligible own funds for the calculation of the solvency ratio of an individual credit institution, as well as the main deductions applicable.

In a CG, consolidation reserves and paid-up minority interests in subsidiaries are also included, while consolidated goodwill is deducted. Moreover, special eligibility conditions are set for preference shares and subordinated debt issued by foreign subsidiaries.

For the final calculation of eligible own funds, the following two relative limits, aimed at ensuring the quality of CI or CG own funds, shall be applied: tier 2 capital shall not exceed tier 1 capital, and lower quality subordinated debt shall not exceed one half of tier 1 capital.

2.2.4. Capital requirements

Pursuant to the general principle of solvency regulations, institutions are required to hold a sufficient amount of eligible own funds to cover the sum of the requirements arising from each type of risk incurred in the pursuit of their business. Broadly in line with Community law, the risks to be covered, as well as their measurement method and minimum coverage requirements are as follows:

Credit risk

Credit risk is the risk that the counterparty will fail to fulfil its obligations to the institution in due time and form. As a general rule, credit institutions are required permanently to maintain at 8 % the ratio of capital to assets and off-balance-sheet items to which weightings have been allocated according to their risk level. Three basic types of weightings are applied:

(24) In addition to individual credit institutions, the BE has supervisory powers over consolidated groups and subgroups of credit institutions, consolidated groups of financial institutions and non-consolidated mixed groups when the parent company is a credit institution or when supervisory powers are attributed to the BE by the Minister of Economy.

Banking solvency regulations

In line with international, and in particular EU, practices and regulations, the basic principle of Spanish banking solvency regulations issued since 1985 has been that CGs and individual CIs which do not belong to a group should permanently hold sufficient own funds to cover risks incurred in the pursuit of their business.

Eligible own funds for the coverage of risks and deductions applicable to individual CIs are listed below. A number of items (e.g. consolidation reserves, minority interests in subsidiaries, etc.) should be added in the case of CGs.

Tier 1 capital

- Paid-up capital, participating interests in savings banks and endowment capital of branches of non-EU foreign institutions.
- Disclosed reserves (self-generating, share premia, reserve fund for participating interests). Profit for the financial year brought forward.
- Fund for general banking risks.

Deductions

- Losses of the previous and current financial years. Intangible assets.
- Own shares and transactions or commitments on such shares.
- Claims on third parties for the purchase of own shares and on corporate staff when individually in excess of € 30,000.
- Shares held by non-consolidated subsidiaries up to the amount of financing received from the parent company or guaranteed by the latter.

Tier 2 capital

- Asset revaluation reserves and reserves arising from mergers.
- Welfare funds in the form of real estate (only savings banks and credit co-operatives).
- Non-voting shares.
- Subordinated debt of indeterminate duration, whose principal is used to absorb losses, leaving the CI in a position to continue trading.
- Other subordinated debt with a maturity of at least five years.

Other deductions

- Qualifying holdings in CIs or financial institutions and other venture capital issued by these institutions.
- Other holdings or venture capital in financial institutions, when they exceed 10 % of the own funds of the holding company.
- Excess qualifying holdings in non-financial corporations.
- Shortfall in specific provisions.
- Other risk assets that the institution may decide to deduct.

Moreover, for the final calculation of eligible own funds, the two following relative limits shall be applied: tier 2 capital shall not exceed tier 1 capital, and lower quality subordinated debt shall not exceed one half of tier 1 capital. Likewise, tier 1 capital shall predominantly be made up of capital and reserves, which limits the eligibility of preference shares.

Risks which should be covered are basically the following:

- Credit risk on asset and off-balance-sheet items or commitments and derivatives, defined as the risk that the counterparty will not fulfil its obligations to the institution in due time and form.
- Foreign-exchange risk on foreign-exchange positions, i.e. the possibility of losses arising from movements in exchange rates.
- Market risk on the trading book (the most recently included), i.e. the possibility of losses in securities and other positions taken by institutions with the intention of benefiting in the short term from interest rate or price movements.

As a general rule, credit institutions are required to maintain permanently a ratio of 8 % of risk-weighted items, according to weighting rules established by law.

If this requirement is not satisfied, apart from the disciplinary actions which may be taken and from the obligation to prepare and implement a programme ensuring return to compliance, the distribution of profits to shareholders will be restricted or prohibited, depending on the shortfall in coverage.

Furthermore, there are certain limits on risks relating, on the one hand, to tangible assets and positions in a single currency (neither being envisaged in Community law) and, on the other, to qualifying holdings in non-financial corporations and large exposures, the latter in order to avoid undesirable concentrations in a single institution or group in excess of 25 % of own funds (20 % in the case of exposure to the institution's own group).

- a) Asset items are risk-weighted taking into account the nature of the debtor according, inter alia, to the economic sector to which it belongs and to the collateral securing the assets.

In relation to economic sector, debtors are divided into three main groups: central government (zero weighting), CIs (20 % weighting) and private sector (100 % weighting). As far as collateral is concerned, asset items carrying explicit guarantees are subject to the weighting attributed to the ultimate obligor or guarantor, if this is more favourable than the weighting attributed to the direct obligor. As for other guarantees, which are described in detail in the regulations, differing weightings are applied according to the type of collateral provided (asset items secured by collateral in the form of securities are subject to, with slight differences, the weighting assigned to the issuer, whereas a 50 % weighting is applied to loans secured by mortgages on residential property).

RD 1419/2001 of 17 December 2001 extended to securities issued by local authorities the regime applying to government debt in respect of the solvency ratio level (zero weighting) and large exposures.

- b) Off-balance-sheet items and commitments incorporate credit risk to the extent that they may give rise to a cash disbursement by the institution. This risk is measured in two steps: first, the item is multiplied by a reducing ratio (0 %, 20 %, 50 % or no reduction) measuring the probability that this disbursement may take place; second, the value obtained is weighted according to the weighting allocated to the counterparty, as set out for asset items.

Both off-balance-sheet and asset items are calculated at book value net of specific provisions.

- c) Specific criteria are established for transactions that do not incur direct credit risk but do give rise to the risk that the counterparty may not meet the terms of contracts that would yield profits to the institution. This may occur with transactions on interest rates or exchange rates (swaps, options, etc.), with the exception of those traded on organised markets, under certain conditions. Here again, the risk is measured in two steps: first, the principal amount is multiplied by a percentage measuring the current and future replacement cost of the transaction; second, the value obtained is multiplied by the weighting allocated to the counterparty, the maximum weighting being 50 %, even for the non-financial private sector.

Foreign-exchange risk on positions in currencies

Credit institutions are required to hedge with own funds 8 % of their overall net position in currencies to cover possible losses arising from exchange rate movements in their open positions in each currency. The net position in a currency is the difference between assets (including accrued income and purchase commitments) and liabilities (including accrued costs and sale commitments). The net overall position in currencies is the higher of the total equivalent value in national currency of net long positions and of net short positions.

Market risk in the trading book

CIs and CGs with a trading book are required to hold capital against market risk, the latest risk to be included in solvency regulations (25). According to the definition set out in

(25) As laid down in Directive 93/6/EEC. Although transposition was not required until 31 December 1995, the content of this Directive was incorporated into Spanish law in 1993 in respect of investment firms and in 1994 in respect of CIs and CGs.

accounting regulations (26), the trading book includes, as a rule, debt instruments and equities and derivatives which are held or taken on by the institution with the intention of benefiting in the short term from price or interest rate movements.

Market risk and its capital coverage are determined, according to the standardised approach laid down in Community law, on the basis of the calculations and weightings applicable to price risk on positions in the various instruments, settlement/delivery risk, credit risk and counterparty risk arising from the trading book.

Recently, RD 1419/2001 of 17 December 2001 (27) extended the definition of trading book to include positions in gold, treated in a similar fashion to foreign-exchange positions, and allowed institutions to develop their own risk-management internal models for the calculation of capital requirements for market risk and foreign-exchange risk, subject to authorisation by the BE. The implementing Banco de España Circular has not yet been issued.

2.2.5. Limits on exposures

There are four prudential limits on exposures of which the first two are not included in Community law:

- Limit on net tangible fixed assets, which may not exceed 70 % of own funds.
- Limit on positions in a foreign currency, which may not exceed 5 % of own funds, unless authorised by the BE. This limit is applicable at the individual unconsolidated level.
- Limits on qualifying holdings in non-financial corporations, in line with Community law. A qualifying holding is a holding which represents 10 % or more of the capital or which makes it possible to exercise a significant influence over the management of the undertaking. The higher of the two following amounts shall be deducted from own funds: the total amount of qualifying holdings in excess of 60 % of own funds or the individual amount of each qualifying holding in a single undertaking or group in excess of 15 % of own funds.
- Limits on large exposures, also in line with Community law (28). A large exposure is an exposure incurred to a single client or group of connected clients (including the credit institution's own group in respect of the unconsolidated portion) the value of which exceeds 10 % of own funds. Subject to full or partial exemptions for given risks, two limits are set: individual exposure to a single client or group of connected clients shall not exceed 25 % of own funds (20 % for exposures to the credit institution's own non-consolidated group) and total large exposures shall not exceed 800 % of own funds.

2.2.6. Consequences of non-compliance with solvency regulations

In addition to the obligation to inform the BE of any non-compliance, and present a specific programme ensuring return to compliance, and regardless of possible sanctions, credit

(26) Rule 8 of Banco de España Circular 4/1991 of 1 June 1991.

(27) Transposition of Directive 98/31/EC of 22 June 1998 amending Directive 93/6/EEC of 15 March 1993.

(28) Article 49 of the Banking Directive. In line with Commission Recommendation 87/62/EEC, Spanish law had established earlier a 40 % limit on own funds for exposures to a single client or group of connected clients. This limit remained effective until 31 December 1993.

institutions' freedom is automatically restricted in two aspects: profit distribution is affected insofar as, if the shortfall in eligible own funds exceeds 20 % of minimum requirements, individual or consolidated credit institutions shall be required to assign total profits or net surplus to reserves. If the shortfall falls below the above-mentioned percentage, at least 50 % (or more, if required by the BE) shall be allocated to reserves (29). Furthermore, the establishment of new offices shall be subject to authorisation by the BE or, where appropriate, by the regional government, on the basis of an opinion from the BE.

2.3. Accounting

In Spain, the power to establish accounting standards and rules and financial statement formats for CIs and CGs is vested in the Ministry of Economy and Finance, which has delegated this responsibility to the BE (30). The accounting rules laid down in the Commercial Code, the Companies Act and specific regulations applicable to CIs are implemented and adapted to CIs by BE provisions.

Specifically, CBE 4/1991 of 14 June 1991 on accounting rules and financial statement formats, updated and amended by subsequent circulars, is the accounting framework for CIs and CGs and for branches of foreign CIs operating in Spain. All matters which are not explicitly included in the aforesaid Circular shall be regulated by the General Chart of Accounts and its implementing provisions and the Regulations on the Presentation of Consolidated Annual Accounts.

CIs and CGs are required by the BE to present two types of financial statements:

- Public financial statements: with information to third parties on the economic and financial position of the institution.
- Confidential financial statements: with more detailed information to be reported to the BE. This information shall be used for supervisory purposes and for the compilation of monetary, financial or economic statistics.

Since statistical data are necessary for the fulfilment of the tasks entrusted to the ECB, in particular the conduct of monetary policy, CIs are required to provide specific financial information permitting the ECB to draw up on a regular basis an aggregated balance sheet for euro area financial intermediaries as a whole.

The accounting principles and rules on which CI and CG financial statements are based have traditionally been aimed not only at providing information to third parties, like the statements of any other firm, but also at supplying the BE with extensive information on their financial position and at restricting transactions which may increase solvency or liquidity risk. For this reason, the principle of prudence shall prevail in the event of conflict between specific regulations or of lack of such regulations.

Finally, CI financial statements shall be drawn up on a consistent basis so that monetary authorities may obtain aggregate data allowing the adequate conduct of monetary policy and the compilation of statistics.

(29) In the case of savings banks, which are always required to assign 50 % of profits to reserves, the allocation of this or a higher percentage is subject to possible investments or charitable activities that may be exceptionally authorised by the Minister of Economy, as laid down in article 11 of Law 13/1985 of 25 May 1985.

(30) Article 48(1) of the LDI and Ministerial Order of 31 March 1989.

In its definition of general accounting principles for CIs and CGs, the BE considers that the purpose of the balance sheet, profit and loss account, annual report and other supplementary financial statements is to provide a true and fair view of the credit institution in respect of its financial position, results and exposures.

The achievement of this objective and the application of accounting standards or rules should be based on the following *accounting principles: prudence, historic cost, accrual, consistency, recording and no on- or off-balance sheet netting.*

Given the operational peculiarities of CIs and CGs, CBE 4/1991 deals extensively with certain accounting treatments, particularly in relation to credit risk, trading book, mobilisation of financial assets and derivatives.

Credit risk is addressed both as regards solvency risk and country risk.

As far as solvency risk is concerned, three types of provisions are required depending on the condition of the debtor:

- a) A general provision amounting to 1 % of credit risks (0,5 % for certain types of risks) shall be set up.
- b) Specific provisions must be made for loans which have been classified as doubtful, with the objective of covering the potential losses arising from the transaction or the client. These provisions depend on the sector to which the debtor belongs, the length of time that the loan has been considered doubtful and existing collateral.
- c) Statistical loan loss provisions, whose amount may be estimated according to the standardised model proposed in CBE 4/1991 or to internal models developed by institutions subject to authorisation by the BE, shall be set aside to cover transactions which have not yet been specifically identified as doubtful assets but in which experience shows that this risk may exist. This type of coverage started to be applied on 1 July 2000, date of entry into force of CBE 9/1999 of 17 December 1999 under which it was established (31).

As for country risk, i.e. the risk arising from total claims on a single country other than business risk, under CBE 4/1991 countries are classified into six categories or groups to which different minimum coverage requirements are applied depending on the degree of risk.

Investment in and management of securities, whether aimed at benefiting from short-term movements or at making steady investments, are included in CBE 4/1991, which recognises four types of portfolios to which different valuation methods are applied: trading book, available for sale portfolio, held-to-maturity portfolio and permanent holdings portfolio.

Fund raising operations through the securitisation of financial assets are recognised either through the writing-off of a transferred asset, or as a liability, provided given requirements are fulfilled, in particular that all the transferor's rights are passed on to the transferee. With respect to this type of transaction, the Circular addresses the accounting treatment of financial asset transfers, rediscount of bills, asset holdings, repurchase agreements and securities lending.

CBE 4/1991 also regulates the accounting treatment of derivatives. When derivatives are considered as hedging instruments against risks arising from other transactions which have al-

(31) Subsequently, Banco de España Circular 4/2000 of 28 June 2000 clarified the definition of net endowment to the statistical provision, excluding changes in the general provision from its calculation.

ready been recognised, the recognition of profits or losses on derivatives shall match the results of the hedged items. When derivatives are considered as non-hedging financial instruments, if they are quoted on an organised market, they shall be recorded immediately; if not, they shall be valued on a monthly basis and solely resulting losses shall be recorded in the profit and loss account. Final results shall be recognised upon settlement.

CIs often create legally independent corporations whose purpose will be to engage in specific activities, such as management of investment funds, cards, etc., or to operate in different geographical areas. As a result, to fulfil the disclosure obligations laid down in the Commercial Code, as well as supervisory capital requirements, CIs are subject to overall consolidation of their financial statements with those of the financial institutions constituting with them a management unit, as defined in the LSM, excluding (as provided for in article 6 of RD 1343/1992) insurance companies, which shall be valued according to the equity method. Jointly managed financial institutions are subject to proportional consolidation. By contrast, non-financial corporations which are included in the economic group of a credit institution, as well as corporations over which, though not included in the economic group, a significant influence is exercised shall be valued according to the equity method and shall appear separately in the consolidated balance sheet under a specific heading.

Pursuant to the latest updating of CBE 4/1991, amended by CBE 5/2000 of 19 September 2000, the accounting treatment of credit institutions' staff pension schemes was adapted to RD 1588/1999 of 15 October 1999 which endorsed the Regulation on the implementation of corporate staff pension schemes in respect of employees and beneficiaries. Furthermore, CBE 4/2001 of 24 September 2001, relating to the information on holdings included in the basis for the calculation of contributions to the Deposit Guarantee Fund (DGF) and on secured amounts, stresses the need for credit institutions to assert careful control in relation to custody accounts.

2.4. Transparency of transactions and customer protection

2.4.1. Former and current regulations

Sectoral regulations aimed at improving bank customer protection were developed in parallel with the interest rate and commission fee liberalisation process, which started in 1981 and culminated in a Ministerial Order of 3 March 1987. This provision, together with its implementing BE Circulars, was the most direct predecessor of current regulations, which replaced strong interventionism with a new stance based on the general principle of freedom of prices for banking products and services supported by a wide array of consumer protection regulations.

Current regulations are based on article 48(2) of the LDI whereby, without prejudice to the principle of freedom to conclude agreements that must govern the relationship between parties, the Minister of Economy is empowered to issue regulations intended to protect the legitimate interests of credit institutions' customers, whether lenders or borrowers (32).

Accordingly, the MO of 1987 was superseded by MO of 12 December 1989, which reinforced and improved the principles established in the former, extending them to all CIs. In turn, the BE was specifically empowered to implement this Ministerial Order, thus issuing CBE 8/1990 of 7 September 1990, as successively amended, which incorporated some of the provi-

(32) Provisions issued by regional governments under the powers conferred upon them in this field shall not offer a lower customer protection level than that provided by central government regulations.

sions laid down in other general regulations (33) in order to ensure the comprehensive applicability of the Circular.

As for Community law, which is not very extensive in this field, the consumer credit Directive (34) and Commission Recommendation of 30 July 1997 concerning transactions by electronic payment instruments and in particular the relationship between issuer and holder were, to a large extent, also incorporated into CBE 8/1990.

CBE 3/2001 of 24 September 2001 amending CBE 8/1990, which will be discussed in more detail in the following sections, basically encompassed two issues. In the first place, the Circular incorporated Community provisions (35) laid down in Law 9/1999 of 2 April 1999 regulating the legal regime of transfers between EU Member States, MO of 16 November 2001 implementing the law, and other provisions relating to transfers in general. In the second place, it embodied several provisions regulating operations carried out through electronic channels, in particular the Internet.

2.4.2. Transparency and customer protection

Among the provisions aimed at ensuring that the customer may receive adequate information to adopt well-founded decisions on the banking product or service concerned, the following should be pointed out:

Effective cost or yield of transactions

The regulations incorporate a definition of effective cost or yield, allowing the comparison of prices applied by institutions offering the same financial product: the equivalent annual rate (EAR), i.e. the rate equalling on an ongoing basis the current value of amounts received and paid on all items between the parties throughout the transaction and in annualised terms. This rate must be included in various types of documents, such as contracts, settlement documents and others.

Subject to technical details relating to specific transactions, the items which are, as a rule, included in or excluded from the EAR are listed in Box A.I.4.

Price of foreign exchange transactions

Without prejudice to the principle of pricing freedom, credit institutions shall publish the exchange rates applied on their retail foreign currency or banknote exchange transactions (under € 3,000), as well as relevant charges and commission fees.

Price of variable interest rate transactions

Certain precautions are established with respect to the reference indices that may be used by credit institutions to set the price of transactions, when this varies over time. Objec-

(33) Specifically, Law 7/1995 of 23 March 1995 on Consumer Credit, Law 2/1994 of 30 March 1994 on the Subrogation and Modification of Mortgage Loans and MO of 5 May 1994 on the Transparency of Financial Conditions for Mortgage Loans.

(34) Council Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit, which was transposed, together with its successive amendments, into the Consumer Credit Law.

(35) Directive 97/5/EC of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers.

Items included in or excluded from the EAR*1. Items included*

- Nominal interest rate on the transaction.
- Commission fees on credit transactions (review, commitment and others) and on deposit transactions (account maintenance).
- Life insurance premia, when imposed by the institution as a condition for granting credit.

2. Items excluded

- Credit subsidies; tax allowances.
- Commission fees or charges for non-compliance with contract conditions.
- Fund transfer commission.
- Facility fee.
- Valuation charges.
- Insurance and guarantee charges, with the exception of those appearing under items included.
- Record checking, notary and registry charges.
- Withholding and other taxes.

tive prices must be applied. Thus, interest rates published or applied by the credit institution or its group may not be used as a benchmark by these institutions. Moreover, in order to provide standardised benchmarks for these transactions, the BE prepares and publishes on a monthly basis a series of indices or official benchmark rates which, though not compulsory, are widely accepted and include both long-term benchmarks (average interest rates on mortgage loans) and short-term interbank indices [Mibor (36) and Euribor].

Customer information prior to conclusion of the contract

To provide guidance to the market and the public at large, credit institutions are required to publish a number of interest rates: prime rate, overdraft rates on current accounts and credit accounts, as well as reference rates on other commonly granted financial facilities, in particular consumer credit and housing loans.

On the other hand, pricing freedom implies an obligation on credit institutions to make available at all times to customers a prospectus specifying the maximum commission fees which may be charged, the transactions for which they are payable and the conditions governing their application. The prospectus shall also set out the charges payable for transactions and services usually provided by the credit institution. The publication of the above-mentioned rates in the prospectus is considered, as a rule, a condition for their applicability. Therefore, the application of less favourable conditions or of charges for services whose rates are not specified is subject to disciplinary sanctions. For the sake of transparency, the prospectus shall be clear and readily understandable, this requirement being subject to prior approval by the BE and by the National Securities Market Commission in the case of stock market transactions.

(36) Under Order of 1 December 1999, the Mibor, which is expected to be calculated according to a new formula, is not considered as an official index for loans arranged as from 1 January 2000. These provisions were incorporated into CBE 8/1990 through CBE 1/2000 of 28 January 2000.

Under the new regulations the prospectus must include a specific section setting out the general conditions applicable to foreign transactions.

More stringent transparency conditions prior to conclusion of the transaction are applied to mortgage loans. Credit institutions are required to provide information on, inter alia: changes in the benchmark index over the previous two years (in the case of variable-rate loans), transaction costs payable by the customer, the maximum amount of the loan in relation to the appraisal value, the funds payable on account and the terms for contracting the services of third parties.

This information, including at least the points listed in Box A.1.5, shall be displayed on the notice board, in full view of the public, at all the business premises of the credit institution.

Credit institutions engaged exclusively in telephone banking shall communicate the above-mentioned information in writing to their customers, at least on a quarterly basis. When the possibility of carrying out transactions through the Internet is offered, credit institutions shall make available on their website their identification details, the information displayed on the notice board, the prospectus specifying commission fees and the valuation rules applicable.

In certain transactions credit institutions are required to present to the customer a binding offer, undertaking to maintain the conditions of the offer for a given period. This obligation extends, inter alia, to consumer credit when the customer has requested a binding offer and, in general, to mortgage loans regulated by MO of 5 May 1994. Customers may also request a written offer setting out the specific conditions applicable to credit transfers governed by Law 9/1999 of 12 April 1999.

Compulsory delivery of contracts and minimum information requirements

In certain cases, credit institutions are required to deliver a written contract to the customer, as specified in Box A.1.6.

As a rule, together with the contract the institution shall make available to the customer information on the commission fees, charges payable and valuation rules applicable to the agreed transaction. This document shall be sent by electronic means or in writing and shall fulfil the minimum information requirements set out for this purpose. The institution shall keep the customer's acknowledgement of receipt.

Without prejudice to the parties' freedom of contract, the regulation defines minimum information requirements for banking contracts (37) which, in general terms must include information on the interest rate, payment period, commission fees and charges payable, the EAR, etc., whereas the information to be included in mortgage loan contracts is set out in more detail in specific regulations.

Information subsequent to conclusion of the contract

The customer shall be informed of any changes in interest rates or commission fees in good time. As a rule (with the exception of permanent agreements), the communication shall be personally addressed in writing to the customer.

(37) Credit institutions' securities market contracts are regulated under MO of 25 October 1995.

Information to be displayed on the notice board

1. Prime rate, overdraft rates on current accounts (distinguishing between customers and others) and credit accounts. Other benchmark rates.
2. Indication of exchange rates on transactions with banknotes and foreign currencies and conversion rates for euro legacy currencies, with relevant commission fees.
3. Indication of the availability of a prospectus specifying the whole range of commission fees and valuation rules (also on the BE's website).
4. Changes in interest rates on certain transactions (permanent agreements, variable-rate securities).
5. Reference to the Complaints Service of the BE and, where appropriate, to the credit institution's ombudsman.
6. Reference to the regulations on the transparency of banking transactions and customer protection.
7. Indication of the availability of a prospectus on mortgage loans.
8. Information required under securities market transparency regulations.
9. Indication of customers' right to request binding offers, where appropriate.
10. Indication of customers' right to receive an offer with the specific conditions applicable to cross-border credit transfers within the EU.

The customer shall also receive information on the settlement of lending and borrowing transactions and services. Additionally, the requirement to provide information on the settlement of credit transfers has recently been introduced. The relevant obligations (for instance, on current account statements) and minimum information requirements in respect of settlement are laid down in CBE 8/1990.

The information subsequent to conclusion of contracts may be supplied by electronic means, if so requested by the customer or if the contract has been concluded electronically and includes this condition.

2.4.3. Other protection regulations

As an exception to the principle of pricing freedom, certain limits have been established in relation to the ordinary transactions of a wide range of customers. Thus, the maximum commission fee for prepayment or creditor subrogation on variable-rate mortgage loans shall be 1 % of the prepaid or subrogated amount, unless a lesser rate has been agreed in the contract (38). Likewise, the maximum commission fee for prepayment of loans regulated by the Consumer Credit Law shall not exceed 1.5 % of the prepaid capital under variable-rate contracts and 3 % under fixed-rate contracts. There are also limits on the interest rate applied to current account overdrafts (39).

Within this framework, under Regulation (EC) No 2560/2001 of the European Parliament and of the Council of 19 December 2001 on cross-border payments in euro, charges lev-

(38) Law 2/1994 of 30 March 1994.

(39) The upper limit set out in article 19(4) of the Consumer Credit Law is the interest rate giving rise to an EAR which does not exceed 2.5 times the legal rate of interest.

Compulsory delivery of contract

1. Opening of current and savings accounts, as well as issuance or renewal (when new conditions are established) of relevant electronic payment instruments.
2. When the contract amount is lower than € 60,000, on loans and credits, including commercial discount (excluding overdrafts on current and credit accounts, unless requested by the customer), term deposits, bank and similar commercial paper and repurchase agreements on financial instruments traded on organised markets.
3. Financial leasing transactions.
4. Non-standardised or customised transactions.
5. Transactions requiring standard contracts, as provided for under MO of 25 October 1995 (specific government debt transactions, portfolio or securities management contracts) and MO of 7 July 1989 on government debt financial accounts.
6. When the credit institution and the customer agree that services may be requested or used through phone-banking.
7. When requested by the customer.

ied by an institution in respect of electronic payment transactions and credit transfers in euro up to the amounts specified therein shall be the same whether the transaction is carried out between or within EU Member States. This Regulation shall be implemented with effect from 1 July 2002 for electronic payment transactions and 1 July 2003 for credit transfers.

For the purposes of accrued interest, the value date for transactions credited or debited to customer accounts does not normally coincide with the transaction execution date or the drawdown date. Consequently, the time lag allowed (maximum for credits and minimum for debits) is established according to the type of transaction and credit institutions are required to make every effort to credit or debit customer accounts without delay.

Advertising of transactions or services provided by CIs is subject to Law 34/1988 of 11 November 1988 on Advertising and to approval by the BE or by regional governments within their field of competence, when cost or yield is explicitly or implicitly referred to. The reason for establishing this requirement (which in no event implies recommending the product or service advertised) is to ensure that advertising reflects in a clear and precise form, and in relation to competitors, the main characteristics of the transactions, in particular the obligation to inform on the EAR.

- The function of the Complaints Service of the Banco de España, created in 1987, is to receive and process complaints related to specific transactions lodged by customers in respect of CI activities which may involve the infringement of rules of conduct and good banking practices and customs (40).

The regulations define the complaints filing, processing and resolution procedure. In this respect, it is worth noting that claimants are required to lodge the complaint in the first place

(40) Article 9 of MO of 12 December 1989 and Chapter II of CBE 8/1990. Pursuant to Order of 16 November 2000 on the regulation of certain aspects of the legal regime of currency-exchange bureaux and their agents, the field of competence of the Complaints Service has recently been extended to customer complaints against currency-exchange bureaux authorised to conduct transactions with foreign banknotes and traveller's cheques and to arrange cross-border credit transfers.

with the credit institution's ombudsman, if any, and that the Complaints Service issues a non-binding report which is notified to the parties concerned. An extensive Annual Report is made available by the Complaints Service on the BE's website.

2.5. Other banking regulations

Expansion: establishment of branches and business pursued through agents

Branches may be freely established within Spanish territory (41) subject to possible statutory restrictions and, as mentioned above, the limits which apply in the event of non-compliance with capital requirements.

Another form of expansion is to pursue business through agents, i.e. persons granted power of attorney by the institution to carry out standard banking transactions with its customers on its behalf. Among the LDI-based conditions regulating the relationship between CIs and their agents (42), the following should be highlighted: the responsibility for compliance with regulatory and disciplinary rules in respect of activities undertaken by the agent rests with the principal credit institution; under exclusive agency terms, the agent must represent a single institution or group; the agent must unequivocally identify the principal credit institution in all relationships with customers.

Incompatibilities associated with holding the position of senior official

Under the regulations applicable to each type of credit institution, members of the board, or similar body, and senior managers, or similar officials, shall not be allowed to hold similar positions in other CIs or companies (43).

As far as banks are concerned, under a regulation dating back to 1968, senior officials are prohibited, in general, from holding a similar position in other banks and from being on more than four boards of directors of public limited companies. Subject to an overall limit of eight posts, the aforementioned prohibition does not apply to positions held in family companies, as defined for these purposes; in firms in which the bank has qualifying holdings; and in "related" banks (currently to be interpreted as referring to banks within the same group). A specific restriction is applied to positions with general executive powers (managing director and senior managers) which are not compatible with any other position and require full-time commitment. Regulations applicable to savings banks and credit co-operatives set out similar restrictions for senior officials.

Central Credit Register of the BE

The Central Credit Register of the BE (CCR) was created in 1962 (44), when the BE was entrusted with the task of establishing a service dealing with credit transactions carried out by banks, savings banks and other credit institutions. Pursuant to OM of 13 February 1963, the BE

(41) Article 30 bis of the LDI.

(42) Article 30 bis of the LDI and article 22 of RD 1245/1995 of 14 April 1995. In addition to the conditions laid down in these provisions there are those applicable under securities regulations when the activities pursued by agents include transactions falling under such regulations.

(43) With respect to savings and co-operative banks, the regulations issued by regional governments within their field of competence are also applicable.

(44) Article 16 of Decree-Law 18/1962 of 7 June 1962, updated in the Bill on the Reform of the Financial System.

has been issuing the provisions regulating the operation and scope of this service, the latest being CBE 3/1995 of 25 September 1995, which sets out the current regime.

The institutions required to report exposures to the CCR on a monthly basis are Spanish CIs, in respect of their entire business (including that of their foreign branches and special purpose vehicles), and foreign CIs, in respect of their activities in Spain. The BE, the Deposit Guarantee Fund and mutual guarantee companies are also reporting institutions.

In general terms, direct exposures arising from credit, money or off-balance-sheet transactions, including debt securities, as well as indirect exposures to guarantors of direct exposure transactions, are required to be reported, where these are above a minimum amount specified under CBE 1/2001 of 30 March 2001 (45).

Each reporting institution may access CCR aggregate data on the total risk incurred in the system by the borrowers in relation to which it has reported exposures, or data on the risk incurred by borrowers which have expressly authorised access to their data. The information supplied which is, in any event, subject to professional secrecy, is intended as an instrument to help improve the analysis and monitoring of exposures, for the purpose of ensuring the solvency of credit institutions.

Finally, it should be pointed out that, under article 56 of Law 39/1988 of 28 December 1988 regulating Local Finance, the BE co-operates with the Ministry of Economy in the operation of the Central Credit Register for Local Authorities (46), which is under the responsibility of the Ministry, by providing the relevant information received by the CCR.

3. CORRECTIVE MEASURES

The supervisory framework described above is supplemented by: a regime for the imposition of sanctions to which CIs are subject; the supervisory powers conferred upon the BE, under which it is authorised to intervene in the management of institutions facing exceptionally serious problems by placing them under administration or replacing their directors; and measures aimed at the protection of depositors and investors and the management of banking crises through the action of the Deposit Guarantee Fund (DGF).

Most of the following legal provisions were urgently adopted to manage the crisis which affected the Spanish banking system between 1978 and 1984.

3.1. Regime for the imposition of sanctions

The LDI consolidated for the first time the formerly dispersed infringement provisions applicable to CIs.

The power to impose sanctions laid down in the LDI is established for cases of statutory infringements classified as very serious, serious or minor (irrespective of the concurrence of possible serious or minor offences under criminal law). Minor infringements are defined on a residual basis, i.e. as breaches which are not expressly specified. Very serious and serious in-

(45) In general, the minimum amount for which exposures are to be reported is € 6,000 in respect of the entire business in Spain and € 60,000 in any other country for direct exposures to residents, and € 300,000 for direct exposures to non-residents.

(46) Recently regulated under RD 1438/2001 of 21 December 2001.

fringement generally refer to similar situations, as set out in the regulations applicable to CI's activities, although very serious infringements are characterised by aggravating circumstances.

Liability for infringements falls on CIs, including branches of foreign CIs, their senior officials and, in certain cases, persons possessing qualifying holdings in such institutions. Additionally, any physical or legal persons, other than credit institutions, undertaking activities restricted to CI's are also liable to the extent set out in the LDI.

The procedure is governed, with certain special characteristics, by RD 2119/1993 of 3 December 1993 on the infringement procedure applicable to institutions operating on financial markets. The power to institute proceedings and to impose sanctions in respect of minor or serious infringements is vested in the BE and the resolution of very serious infringements rests with the Ministry of Economy, with the exception of revocation of authorisation to operate as a credit institution, where the power is vested, in general, in the Council of Ministers.

Depending on the seriousness of the infringement, and after applying statutory evaluation criteria, sanctions applicable to credit institutions range from private warning to fines of varying amounts and, finally, revocation of authorisation or, in the case of branches of Community institutions, a ban on the undertaking of any new operations within Spanish territory. Sanctions applicable to managers or administrators who are responsible for the infringement include warning and fines, as well as suspension from duty and disqualification for holding similar positions in the same or any other credit institution (47).

Subject to the above-mentioned procedure, savings banks and credit co-operatives in the field of competence of regional governments are also subject to the infringement procedure established at the regional level in relation to infringements in respect of which the power to impose sanctions is not reserved to the central government under article 149(1)(11) of the Spanish Constitution (48). In the case of serious or very serious infringements, the resolution proposed by the competent regional body must be approved by the BE.

Finally, as from 1 January 1999, Spanish CIs are subject to the powers of the ECB to impose sanctions in the event of non-compliance with minimum reserve requirements (49).

3.2. Administration and replacement of directors

Measures such as placing a credit institution under administration or replacing its directors, formerly set out in the extinguished RDL 5/1978 of 6 March 1978, have now been incorporated into the LDI. Both measures refer to the possibility of intervening in the ordinary management of the institution when, as laid down in the law "a credit institution faces exceptionally serious problems affecting its capital adequacy, stability, liquidity or solvency", and where it is impossible to infer the true situation of the institution from its accounts. The time limit for these measures is conditional on resolving the situation which gave rise to such remedial action. The choice of the action to be taken depends on the assessment of the specific situation, at the discretion of the BE within its technical field of competence.

(47) Certain aspects of the infringement procedure are updated in the Bill on the Reform of the Financial System.

(48) Statutory infringements related to the solvency of credit institutions, as specified in article 42 of the LDI, are reserved to the central government. See judgment of the Constitutional Court 96/1996 of 30 May 1996.

(49) See article 7 of Council Regulation (EC) No 2531/98 of 23 November 1998 relating to the sanctions and the specific procedure applicable in cases of non-compliance with minimum reserve requirements, as well as Council Regulation (EC) No 2532/98 of 23 November 1998 and European Central Bank Regulation (EC) No 2157/1999 of 23 September 1999 on the powers of the European Central Bank to impose sanctions.

The reasons for which these measures, which are of a prudential and exceptional nature and are not to be considered as sanctions, are adopted must be stated. Although these actions have frequently been associated, either simultaneously or subsequently, with insolvency proceedings or with the intervention of the DGF, they may also be applicable to a credit institution, as has already occurred in practice, where such circumstances do not concur.

The decision to place a credit institution under administration or to replace its directors rests exclusively with the BE and may be adopted ex officio or at the request of the institution concerned. Notification of the reasoned decision shall be given to the Ministry of Economy. The credit institution shall be heard in both cases, except if the measure has been requested by the institution or when the delay that such hearing would imply might seriously jeopardise the effectiveness of the action or the economic interests of the parties concerned.

When a credit institution is placed under administration, the proceedings and agreements adopted by any of its bodies as from the date of publication of the administration resolution in the Official State Gazette shall not be valid and may not be executed unless they are expressly authorised by the administrators appointed in the resolution, with the sole exception of those related to actions brought or appeals lodged against the resolution or the conduct of administrators. Likewise, any powers of attorney or proxies granted before the administration resolution is made public may be revoked by the administrators.

When the directors of a credit institution are replaced, they are substituted by provisional directors who shall assume the powers of the institution's managing body and also the functions of administrators in relation to General Meeting resolutions, over which they shall therefore have the power of veto.

Finally, several regional governments are also conferred certain powers in respect of administration and replacement of directors of savings banks established within their territory.

3.3. Deposit guarantee funds

DGFs, one for each type of credit institution, were set up in the late seventies (50). Their institutional framework and basic functions have remained broadly unchanged, though their legal regime has been updated on several occasions, in particular as a result of the transposition of the relevant Community legislation.

Each DGF is run by a management committee composed of four representatives of the BE, one of whom is the chairman and has the casting vote, and four representatives of member institutions, all of whom are appointed by the Minister of Economy.

Further to the transposition of Community regulations on deposit-guarantee schemes (51), membership of DGFs, which had previously been voluntary, became compulsory

(50) The Bank Deposit Guarantee Fund was set up under RD 3048/1977 of 11 November 1977 and was afforded legal personality by RDL 4/1980 of 28 March 1980. The Savings Bank DGF was created under RD 2860/1980 of 4 December 1980 and was invested with legal personality by RDL 18/1982 of 24 September 1982, under which the Co-operative Bank DGF was also set up with legal personality and full capacity. There is no deposit guarantee fund for specialised credit institutions, since they are not allowed to take deposits.

(51) Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes, which was transposed into Spanish law, together with other changes to the regulation of these DGFs, through the seventh additional provision to RDL 12/1995 of 28 December 1995. The common implementing provisions applicable to the three DGFs were laid down in RD 2602/1996 of 20 December 1996.

for all Spanish credit institutions, as well as for branches of CIs located in countries outside the EU, when their deposits in Spain are not covered by a deposit-guarantee scheme in their home country or when the latter must be supplemented to reach the level and scope of cover offered by the Spanish one. As for branches situated within the EU, membership of Spanish DGFs is optional, depending on the harmonisation of the level of protection provided throughout the Community. When membership of the relevant DGF is compulsory, failure to join the scheme or exclusion from the same for specified reasons may entail the revocation of the authorisation to operate as a credit institution.

DGFs were initially financed jointly by the BE and member institutions. However, in 1996 it was established that the cost of financing such schemes would fall entirely on the latter, with an annual contribution of up to 0.2 % of the guaranteed deposits (currently the rate is much lower) (52). This notwithstanding, extraordinary contributions by the BE may be allowed by law.

From the outset, two basic functions have been assigned to DGFs: provision of deposit guarantee and management of banking crises, including participation in any insolvency proceedings which may affect a credit institution.

With respect to the general guarantee function of DGFs, the guarantee provided covers deposits received from each depositor by the credit institution in Spain and in the EU up to the amount of € 20,000. However, certain deposits are excluded from guarantee, such as debt securities issued by the institution and bearer certificates of deposit, as well as, as a form of sanction, deposits taken in breach of the law or subject to unusual financial conditions which have helped to aggravate the institution's financial situation.

The scope of the guarantee provided has recently been extended to investors who have entrusted securities or other financial instruments to credit institutions in connection with investment business (53), in order to cover the risk of temporary unavailability that may arise from the insolvency or suspension of payments of the intermediary in its securities and financial instruments business. Cover for each investor is provided separately from the guarantee afforded for deposits and up to the same amount.

In this respect, two regulations were issued in 2001. RD 848/2001 of 3 August 2001 on investor-compensation schemes (54) introduced partial changes into the regulatory regime of DGFs laid down in RD 2606/1996 of 20 December 1996 in order to incorporate the extended scope of the guarantee. Pursuant to the powers delegated to the BE, CBE 4/2001 of 24 September 2001 set out the valuation standards to be applied to the various types of securities and instruments included in the calculation of annual contributions to DGFs, as well as the information that member institutions are required to report on an annual basis to the BE for the calculation of such contributions.

The two cases covered by the guarantee are the declaration of insolvency and the admission of petition for suspension of payments of the institution concerned (or suspension of the

(52) Pursuant to two ministerial orders of 14 February 2002, the ratio to be applied has been set at 0.6 per thousand for banks, 0.4 per thousand for savings banks and 1 per thousand for co-operative banks.

(53) Pursuant to Directive 97/9/EC of the European Parliament and of the Council of 3 March 1997 on investor-compensation schemes, transposed into Spanish Law, in respect of investment business carried out through CIs, under the thirteenth additional provision to Law 37/1998 of 16 November 1998 on the Reform of the Securities Market, which introduced a new article 2 ter in RDL 18/1982 of 24 May 1982.

(54) This RD refers to investor-compensation schemes operating both through investment firms and CIs, for which similar broad standards are established, though in the case of CIs the guarantee is provided through the existing DGFs.

restitution of securities or financial instruments). Further to the transposition of Community legislation, other cases covered by the guarantee are those in which, even though no such judicial proceedings have been initiated, deposits have not been repaid or securities and financial instruments have not been returned and the BE determines that the institution is unable to fulfil these obligations in the near future.

With regard to their second basic function, i.e. the management of banking crises, DGFs play a markedly different role to other European bodies which are solely responsible for providing the aforementioned guarantee. Indeed, they may adopt preventive and reorganisation measures aimed at improving the institution's viability within a reasonable period of time in order to overcome the crisis situation. These measures must be adopted within the framework of an action plan agreed by the institution and formally approved by the BE, this being the only direct intervention by the BE in the management of the crisis, although their adoption may coincide with or follow the placing of the institution under administration or the replacement of its directors.

One of the technical standards to be taken into account when adopting preventive or reorganisation measures, which is expressly referred to in the above-mentioned regulations, is the evaluation of the cost of financing such assistance, compared with the potential cost to the DGFs of payment under the guarantees if these measures were not adopted.

There is an extensive list of possible measures, ranging from direct financial assistance (non-returnable, guarantee, loans under favourable conditions, purchase of non-profitable or impaired assets, etc.) to capital restructuring, including measures aimed at facilitating merger with or acquisition by other sound institutions or the transfer of the business to another institution, as well as capital increases subscribed by the DGF. In this case, holdings acquired must be sold within a year under the procedure concerned.

Finally, it should be pointed out that DGFs play a significant role when institutions are subject to insolvency proceedings and that in cases of suspension of payments two of the administrators appointed by the judge are taken from lists presented by the DGF to which the institution belongs or has belonged. The direct administration of the institution is assumed in accordance with the Law on Suspension of Payments and the administrator is the DGF itself. In the case of a declaration of insolvency, the functions of commissioner, receiver and trustees are assumed by the DGF concerned.

Where CIs are subject to insolvency proceedings with cross-border effects within the EU, Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions requires the principles of unity and universality to be applied to the credit institution, including branches located in other Member States. This means that the authorities of the home Member State shall alone be empowered to adopt reorganisation measures or open winding-up proceedings in respect of a credit institution, including branches established in other Member States in which their decisions are recognised. In turn, unless otherwise provided, these measures and proceedings shall be in compliance with the laws applicable in the home Member State.

3.4. Revocation of authorisation

Subject to the regulations issued by regional governments within their field of competence over savings banks and credit co-operatives, at the national level the entire list of grounds for revocation of authorisation to operate as a credit institution is set out in article 57 bis of the Banking Law of 31 December 1946, as successively amended.

The grounds for revoking authorisation include initial or subsequent absence of activity, obtaining the authorisation through false statements or by irregular means, failure to fulfil authorisation conditions, capital inadequacy, lack of security that obligations shall be honoured or exclusion from a DGF. The authorisation may also be revoked as a result of an infringement procedure. Foreign branches whose authorisation has been withdrawn by their home country authorities shall not be allowed to continue to operate in Spain.

The Council of Ministers is the authority responsible for deciding on revocation of authorisation, on the basis of a proposal by the Minister of Economy. However, the latter is specifically empowered to take this decision in the event of exclusion from the DGF and, in the case of branches, when the authorisation of the credit institution has been revoked in its home country.

Revocation of authorisation implies by law the winding up of the institution concerned and the opening of a liquidation period in accordance with the applicable company regulations. When winding up is not the consequence of revocation of authorisation (for instance, in the case of voluntary winding up), the Minister of Economy may decide that winding-up proceedings should be initiated if the number of persons affected or the financial situation of the institution make it advisable (55).

4. OTHER REGULATIONS APPLICABLE TO CREDIT INSTITUTIONS

4.1. Activities on securities markets

The LSM established the current legal framework for financial activities related to the issuance and trading of securities on regulated markets, as well as the rules applicable to specialised entities, mainly securities dealers. Likewise, the Law expressly recognised that the greater part of these financial activities could be carried on by banks, savings banks and credit co-operatives. However, since membership of stock exchanges was restricted to securities dealers, it was common practice for banking groups to become members by setting up specialised subsidiaries.

This restriction was abolished by Law 37/1998 of 16 November 1998, amending the LSM for the purpose of transposing the Investment Services Directive (56). As a result, all CIs can normally carry on all the activities considered as investment services (both core and non-core services), provided that their legal status does not prohibit such activities, and they can also become members of regulated markets. This also applies to foreign CIs, distinguishing between Community and non-Community institutions.

Accordingly, CIs are governed by the LSM and its implementing provisions, whereby they are subject to the supervision and inspection of the CNMV, which is also assigned the powers to impose sanctions. It should be pointed out that co-operation between the BE and the CNMV is required by law (57) for the purpose of co-ordinating the action of both institutions within their respective fields of competence. Specifically, when the infringement has been committed by a credit institution, disciplinary sanctions are to be imposed on the basis of an opinion from the BE.

With regard to regulated markets, under the LSM the BE is the governing body of the Public Debt Book-Entry Market, dating back to 1987, and runs the Public Debt Book-Entry System, which publishes an annual report with relevant information on this market.

(55) Article 38 of the LDI.

(56) Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field.

(57) The institutional interrelationship is reflected in the composition of the governing bodies of both institutions. Thus, the Vice-president of the CNMV and the Deputy Governor of the BE are ex officio members of the Governing Council of the BE and of the Council of the CNMV, respectively.

4.2. Payment and securities settlement systems

The BE is the manager of two of the payment and settlement systems regulated by Law 41/1999 of 12 November 1999 on payment and securities settlement systems, i.e. the aforementioned Public Debt Book-Entry System (58) and the SLBE (Banco de España Settlement Service, formerly called the Money Market Telephone Service) (59).

The SLBE is a clearing and settlement system providing credit transfer services and ensuring the execution and settlement of transactions carried out by member institutions on money and public debt markets and in other environments. Furthermore, it is one of the components of the TARGET system through which NCBs' real time gross settlement systems and the ECB's payment mechanism are interlinked.

4.3. National Electronic Clearing System

The SNCE (National Electronic Clearing System) was set up under RD 1368/1987 of 18 September 1987, which entrusts the administration and management of the system to the BE. The SNCE ensures the electronic clearing and settlement of documents and other means of payment between member institutions (CIs operating in Spain and the BE).

The SNCE, which is considered as a clearing house pursuant to the Law on Negotiable Instruments and Cheques, currently ensures the clearing of most commercial bills, other payment orders and credit transfers intermediated by CIs, as a result of the virtual disappearance of conventional clearing channels. The SNCE is regulated by the BE (60), assisted by an advisory committee composed of representatives of member institutions.

4.4. Foreign transactions

The liberalisation of foreign transactions brought about by RD 1816/1991 of 20 December 1991, implemented by MO of 27 December 1991, replaced former controls and restrictions by a series of reporting requirements aimed at monitoring transactions for statistical and fiscal purposes. Reporting requirements apply to both individuals involved in the transactions and CIs ensuring payments and receipts between residents and non-residents and providing credit transfer services. Most of the information is transmitted through the BE in accordance with the procedures laid down in the circulars issued by the BE pursuant to the delegation of powers set out in the mentioned RD.

In particular, CIs are required to report on the accounts held in Spain by non-residents. Account holders must be identified and their condition as non-residents must be specified and periodically confirmed. Furthermore, CIs are required to report on a regular basis on banknote stocks and changes in same, balances and movements of accounts held by non-resident creditors in such institutions, interbank transfers and clearing on non-residents' accounts, etc.

4.5. Money laundering

Law 19/1993 of 28 December 1993 on certain measures for the prevention of money laundering transposed into Spanish law the minimum harmonised conditions set out in Direc-

(58) The Bill on the Reform of the Financial System introduces changes in respect of securities clearing and settlement systems.

(59) Regulated under CBE 11/1998 of 23 December 1998. See also CBE 5/1990 of 28 March 1990, CBE 7/1995 of 31 October 1995 and CBE 4/1997 of 29 April 1997.

(60) See mainly CBE 8/1988 of 14 June 1988, which incorporates the rules applicable to the SNCE.

tive 91/308/EEC of 10 June 1991. The purpose of the Law and its implementing Regulation was to prevent and combat the use of CIs, financial intermediaries and other reporting institutions to launder proceeds from drug trafficking, terrorism and organised crime.

For this purpose, the Law set up the Commission for the Prevention of Money Laundering and Monetary Offences, attached to the Ministry of Economy and composed of representatives of different judicial and administrative authorities operating in this field. The Commission is assisted by a Secretariat and an Executive Service (the SEPBLAC) attached to the BE. The Law also laid down two basic requirements (and the relevant infringement procedure) for reporting institutions: the obligation to identify customers and to report to the SEPBLAC any fact or transaction in respect of which there may be indications or certainty that they are related to the laundering of proceeds from the aforesaid activities or which have reached the threshold set out as a warning signal for this purpose.

Directive 2001/97/EC of 4 December 2001, amending Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, has broadened the range of reporting institutions and underlying criminal activities.