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Draft Law on regulation, supervision and solvency of credit institutions¹

The draft law on regulation, supervision and solvency of credit institutions (hereinafter referred to as the Draft Law) is part of the process of transposition into Spanish law of the provisions of Directive 2013/36/EU² (also known as “CRD IV”). This directive was approved in conjunction with a regulation³ (known by its initials as “CRR”) which, although directly applicable without the need for transposition since 1 January 2014, allows Member States in certain cases to choose between various regulatory options.

Royal Decree-Law 14/2013 of 29 November 2013 incorporated, on an urgent basis, the most pressing legal changes required to enable supervisors and financial institutions to operate from 1 January in the new EU legal environment arising from the CRD IV-CRR package. It also announced a further text that, besides completing the transposition of the provisions of CRD IV that require legislation, would consolidate the main provisions on the regulation and discipline of credit institutions that hitherto have regulated such area in a dispersed and, on occasions, unconnected manner.

Accordingly, the basic purpose of the Draft Law is to transpose CRD IV, although given the significance of the reform entailed by the CRD IV-CRR package, the opportunity has been taken to unify in a single text the current legal framework for credit institutions.⁴

Content

Title I of the Draft Law contains the general provisions on credit institutions, as well as the rules on the granting, registration and revocation of licences, qualifying holdings, the suitability of senior officers and remuneration policy.

¹The text of the Draft Law has been published in the Official Parliamentary Gazette, Series A, No 80-1 of 14 February 2014. http://www.congreso.es/public_oficiales/L10/CONG/BOCG/A/BOCG-10-A-80-1.PDF#page=1

² Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

³ Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.

⁴ Thus, the Draft Law repeals all provisions of the same or lower rank that conflict with its provisions, including in particular the Banking Regulation Law of 31 December 1946, Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting requirements for financial intermediaries and Law 26/1988 of 29 July 1988 on Discipline and Intervention of Credit Institutions.

Notable in this title is the **expansion of the powers of the Banco de España**. In particular, it is granted the power to revoke the licence of a credit institution and to intervene in a credit institution or provisionally replace its board of directors when there are well-founded grounds to consider that the influence exercised by persons holding a qualifying holding in the institution may be to the detriment of its sound and prudent management, seriously damaging its financial situation. In addition, reference is made to the fact that the Banco de España will exercise its powers without prejudice to the functions attributed to the European Central Bank within the context of the single Supervisory Mechanism⁵ and in cooperation with this institution.

The Ministry of Economic Affairs and Competitiveness, for its part, is given the power to authorise operations of merger, scission or complete or partial transfer of assets and liabilities in which a bank is involved, or any agreement that has similar economic or legal effects to the foregoing.

The Draft Law introduces improvements in the area of **corporate governance** and gives the Banco de España the power to determine which institutions, considering their size, internal organisation and the nature, scale and complexity of their activities must establish a risk committee and which can set up mixed audit committees that assume the functions corresponding to the risk committee.

In relation to **remuneration policies**, the Draft Law incorporates the provisions of CRD IV. The main purpose of such provisions is to ensure that the remuneration policies of institutions are better aligned with their medium-term risks. The Draft Law establishes that the remuneration policy must clearly distinguish the criteria for determining fixed remuneration and variable remuneration, for which purpose it includes certain parameters. Also the Draft Law includes various criteria that must be applied when the variable remuneration components are set. For example, as a general rule, the variable remuneration component must not exceed 100% of the fixed component, and a specific procedure is established in the Draft Law which must be followed in the event that it does exceed this percentage. In relation to payments for early termination of contract, the Banco de España is authorised to define the circumstances that may produce a reduction in the amount of such payments.

Title II regulates the solvency of credit institutions, referring to the assessment that institutions have to make of the adequacy of their capital for the risk assumed and the criteria to be taken into account by the Banco de España when setting the appropriate level of the specific liquidity requirements for each institution.

Also, in accordance with the provisions of CRD IV, the Draft Law introduces “**capital buffers**”, which are additional capital requirements to those envisaged in CRR. Failure to comply with capital buffers entails (i) restrictions on distributions and payments relating to components of common equity tier 1 (such as shares) or additional tier 1 capital (such as contingently convertible bonds) and on the payment of variable remuneration; and (ii) the

⁵ In accordance with Regulation (EU) No 1024/2013 of the Council of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions.

obligation to submit a capital conservation plan that must be approved by the Banco de España.

In particular, the various capital buffers provided for in the Draft Law, in accordance with CRD IV, are as follows:

(i) *Capital conservation buffer*: a non-discretionary buffer, the application of which will be phased in from 2016. Equal to 2.5% of the institution's risk exposure.

(ii) *Countercyclical capital buffer*: specific buffer for each institution, the application of which will be phased in from 2016. It is calculated as the weighted average of the countercyclical buffer percentages applicable in each of the territories in which an institution has exposures. The percentage applicable in Spain will be set by the Banco de España.

(iii) *Buffers for global systemically important institutions (G-SIIs) and other systemically important institutions (O-SIIs)*: buffers specifically applicable to certain institutions by reason of their systemic importance. The Banco de España will identify which institutions are to be considered G-SIIs or O-SIIs and will set the buffer to be maintained by each of these types of institution, which in the case of the G-SIIs will range from 1% to 3.5% and in the case of O-SIIs may not exceed 2%. These buffers will be applicable from 2016, although in the case of G-SIIs their application will be phased in.

(iv) *Systemic risk buffer*: buffer that may be set by the Banco de España to cover non-cyclical systemic or macroprudential risks where there is a risk of disruption in the financial system with the potential to have serious negative consequences for the financial system and the real economy.

As regards the **supervision** of credit institutions, **Title III** of the Draft Law **establishes that the Banco de España, as the supervisory authority**, has to determine the appropriate level of the solvency and liquidity requirements of the institutions subject to its supervision and generally supervise compliance with regulatory and disciplinary rules, including supervision of the systems, strategies, procedures and mechanisms applied by institutions for this purpose, the current or potential risks of institutions and their corporate governance systems and remuneration policies. For this purpose, **the Banco de España broadly maintains the inspection and verification powers in place to date**. Also, as set out in CRD IV, the Draft Law expressly provides that the Banco de España shall conduct yearly stress tests on its supervised institutions to assess their condition and provides for the approval of a yearly supervision programme which takes into consideration the specific supervision needs that some institutions may have in view of their position. When the Single Supervisory Mechanism is launched, the aforementioned powers will be understood as being without prejudice to the powers assumed by the ECB and will have to be exercised in cooperation with the latter.

Additionally, in the context of its prudential supervision work, the Banco de España is equipped by the Draft Law with certain tools envisaged in CRD IV, which comprise, among others, the so-called **Pillar 2 measures** that establish an additional own funds requirement, restrictions on dividend distributions, obligatory risk mitigation, restrictions on certain activities and limits on variable remuneration. These measures may be adopted

as a result of effective non-compliance with applicable regulations or where there is good reason to believe that non-compliance will take place within the next 12 months.

Regarding the Banco de España's **information and publication obligations**, the Draft Law regulates the information on solvency rules which the Banco de España has to publish periodically as well as the obligation to provide information to other authorities in emergency situations. Also, the Draft Law stipulates, in line with the regime currently in force and in accordance with CRD IV, the confidential nature of the data, documents and information held by the Banco de España by virtue of the exercise of its functions, the obligation of secrecy applicable to the employees and persons carrying out or who have carried out any activity for the Banco de España and the exceptions applicable to such obligation of secrecy.

Title IV of the Draft Law sets forth the **penalties** applicable to credit institutions. They broadly coincide with those specified by the current Law 26/1988 of 29 July 1988, although they are updated to include new penalties derived from CRD IV and from the new rules on fitness and transparency. The table of penalties which can be imposed on institutions and on their directors is changed.

Finally, the **additional and final provisions** of the Draft Law regulate a variety of matters, most notably as follows:

1 Amendment of the Securities Market Law (first final provision), mainly to: (i) transpose into Spanish law the prudential supervision regime set out in CRD IV for investment firms, and (ii) set in place the supervisory and penalty regime specified in EU regulations on short sales and market infrastructure (central counterparty clearing houses, trade repositories and OTC derivatives).

2 Amendment of the composition of the DGF management committee (eighth final provision), which will consist of eleven members: one representative of the Ministry of Economic Affairs and Competitiveness, one representative of the Ministry of Financial Affairs and Public Administration, four designated by the Banco de España and five by the associations representing the credit institutions belonging to the DGF (one by savings banks, one by credit cooperatives and three by commercial banks).