Financial regulation: 2004 Q3

Introduction

There were relatively few new financial provisions during 2004 Q3.

First, the regulations governing the Banco de España Settlement Service (SLBE) were updated to include the latest changes introduced by the European Central Bank (ECB) in the Trans-European Automated Real-time Gross settlement Express Transfer (TARGET) system. Specifically, both the issuing and receiving institutions of a payment order can claim compensation for the administrative expenses they may incur in the event of system malfunction.

Second, the regulations on credit institutions' minimum capital were amended to extend the list of multilateral development banks and to reflect the new name in Spanish of two of these banks.

In respect of the securities markets, the following have been established: first, reporting obligations concerning preference shares and other debt instruments, along with information exchange between the tax authorities of the EU regarding certain income obtained by individuals resident in the EU; and second, the information on operations with related parties that the issuing companies of securities traded on official secondary markets must furnish.

Finally, new regulations have been enacted for tax on personal and corporate income and on non-resident income, drawing together all the regulatory provisions in force on these taxes into a single body of rules.

European System of Central Banks: modification of the TARGET system

The ECB Governing Council published Guideline ECB/2004/4 of 21 April 2004 (OJEC of 9 June) amending certain aspects reflected in Guideline ECB/2001/3 of 26 April 2001, which establishes the fundaments of TARGET.

The content of the new Guideline refers essentially to two aspects. First, an express mention is made offering the possibility for the real-time gross settlement systems of the EU Member States that have not adopted the euro to connect up to the TARGET system. The implementation of this aspect does not, however, require a specific amendment of SLBE regulations.

Further, the Guideline amends specific aspects relating to the clearing system in the event of TARGET system malfunction, whereby both the issuing and receiving institutions of a payment order can now claim compensation for the administrative expenses they may incur.

To include these latter changes in SLBE regulations, the Banco de España has published CBE 2/2004 of 23 July 2004, a Circular on the updating of the clearing system in the event of the TARGET system malfunctioning (BOE of 30 July) which amends CBE 2/2003 of 24 June 2003[1].

CBE 2/2003 envisaged that the payment order-issuing institution could make a claim for compensation for interest and for administrative expenses and that the payment-order receiving institution could lodge a claim for compensation only for interest. Now, under CBE 2/2004, the payment order-receiving institution can make a compensation claim for its administrative ex-

1. See "Financial regulation: 2003 Q2". *Economic Bulletin.* Banco de España, July 2003, pp. 78-79.

penses, provided that the participant had not received a payment through TARGET that it expected to receive on the day the system malfunctioned. In this instance, and as was previously the case, compensation could also be claimed for interest if the participant had resorted to the marginal lending facility or if, were a participant without access to this facility involved, it had a debit balance at the close of the session. This possibility is also valid if the national payments system that malfunctioned were that of the receiving institution or, were this not the case, the malfunctioning of the system had occurred in the final hour of the TARGET session, making it technically impossible for the receiving institution to resort to the money market.

Regarding the calculation of the compensation for administrative expenses, the amount set in Circular 2/2003 is halved for payment order-issuing institutions, and is thus set at €50 for the first payment order not completed on the due date with each receiving institution, at €25 for the following four orders directed at the same receiving institution, and at €12.50 for each additional payment order in the same circumstances. These amounts will be identical in the case of the receiving institutions.

Finally, the calculation of compensation for interest both for issuing and receiving institutions remains unchanged. In this respect, it should be recalled that compensation for interest was determined by applying a reference rate to the amount of the unprocessed payment order for each day of the malfunction period. This reference rate will be the lower of the EONIA (euro overnight average index) and the marginal lending facility rate.

Credit institutions: amendment of minimum capital regulations

Commission Directive 2004/69/EC of 27 April 2004 amended 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, as regards the definition of "multilateral development banks", including for the first time in the list of such banks the Multilateral Investment Guarantee Agency, part of the World Bank group.

In order to transpose it into Spanish law, CBE 3/2004 of 23 July 2004 was enacted to enlarge the list of multilateral development banks in Circular 5/1993 of 26 March 1993 on the determination and monitoring of credit institutions' minimum capital.

At the same time, this regulation is being used to include the new names in Spanish of the European Bank for Reconstruction and Development ("Banco Europeo de Reconstrucción y Desarrollo") and the Council of Europe Development Bank ("Fondo para la Reinstalación del Consejo de Europa").

Reporting obligations in respect of preference shares and other debt instruments and of certain income obtained by individuals resident in the European Union

Royal Decree 2281/1998 of 23 October 1998 implemented, inter alia, the provisions applicable to certain obligations to furnish information to the tax authorities.

Recently, Royal Decree 2281/1998 has been amended by Royal Decree 1778/2004 of 30 July 2004 (BOE of 7 August), which establishes the reporting obligations in respect of preference shares and other debt instruments and of certain income obtained by individuals resident in the European Union.

The Royal Decree implements the reporting obligations vis-à-vis the tax authorities of specific individuals or entities mentioned in the regulation. In particular, it stipulates the filing of annual returns with information on the persons authorised to use bank accounts, on certain operations transacted with financial assets and with preference shares and other debt instruments, and on certain income obtained by individuals resident in other European Union Member States.

It further specifies the reporting obligations certain institutions will have to assume concerning the issuance of preference shares and other debt instruments. Specifically, it details the report-

ing obligations of dominant credit institutions or listed non-credit institutions in respect of the issuance of preference shares and other debt instruments by companies in which the former have a stake or controlling interest.

It incorporates into Spanish domestic regulations Council Directive 2003/48/EC of 3 June 2003 on the taxation of savings income in the form of interest payments. Two aspects are salient here: firstly, the scope of reporting obligations vis-à-vis the tax authorities in respect of certain income obtained by individuals resident in other European Union Member States is specified, the income to be reported is defined, and the parties subject to furnishing information in terms of the different types of income are established.

Secondly, the terms and procedures for information exchange between the tax authorities and the other Member States are stipulated. In particular, a six-month period following the end of the tax year is established, and the procedure to be followed by income-paying agents to identify both the recipient and his/her place of residence in order to supply the information properly is determined so that each Member State receives information on its residents, distinguishing between contractual relations entered into before and on or after 1 January 2004.

Finally, it authorises the Minister of Economy and Finance to determine the period, place and way in which information exchange is made effective.

The entry into force of the Royal Decree shall be on the day following its publication in the BOE, although the regulations incorporated into Spanish law as a result of the approval of Directive 2003/48/EC shall be effective 1 July 2005.

Securities-issuing companies: information on operations with related parties

Law 24/1988 of 28 July 1988[2] on the securities market, under the wording given by Law 44/2002 of 22 November 2002[3] on financial system reform measures, established that issuing companies should necessarily include, in the half-yearly information required by the law, quantified information on all operations entered into by the company with related parties in the manner determined by the Ministry of Economy or, with its express authorisation, the CNMV (National Securities Market Commission). Further, it established that the aforementioned Ministry would determine the transactions on which itemised information would have to be furnished if such transactions were significant in terms of amount or importance, along with the operations with related parties on which information would not (if duly justified) have to be given.

With a view to reinforcing the transparency of listed public limited companies, Law 26/2003 of 17 July 2003[4], amending Law 24/1988 of 28 July 1988 on the securities market, introduced new corporate reporting obligations, such as the annual publication of a corporate governance report, the minimum content of which would include related-party operations by the company with its shareholders and its directors and executives.

To regulate some of these matters, Ministerial Order EHA/3050/2004 of 15 September 2004 (BOE of 27 September) was published on the reporting of the operations with related parties to be provided by companies issuing securities traded on official secondary markets (hereafter, the companies).

The companies shall necessarily include in their half-yearly reports specific, quantified information on all operations entered into by the company with related parties.

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2. See "Regulación financiera: tercer trimestre de 1988", *Boletín Económico*. Banco de España, October 1988, pp. 61 and 62. **3.** See «Financial regulation: 2004 Q4», *Economic Bulletin,* Banco de España, January 2003, pp. 101-113. **4.** See «Financial regulation: 2003 Q3», *Economic Bulletin,* Banco de España, October 2003, pp. 93-94.

The regulation defines two concepts. First, it considers the term related party to be when one such party, or group acting in concert, exerts or has the possibility of directly or indirectly exerting, by virtue of pacts or agreements between shareholders, control over the other party or significant influence[5] in the financial and operational decisions taken by the other party. Further, it considers a related-party operation as whatsoever transfer of funds, services or obligations between the related parties, irrespective of whether any consideration is involved.

In any event, the following types of related-party operations must be reported: the buying and selling of finished or unfinished goods and of property, whether tangible, intangible or financial; the rendering and receiving of services; participation agreements; leasing agreements; financing agreements, including loans and capital contributions, whether in cash or in kind; interest paid or charged, or interest accrued but not paid or collected; dividends and other distributed profits; and contributions to pension schemes and life assurance.

It will not be necessary to report operations between companies of the same consolidated group provided they have been eliminated from the consolidated financial statements and are part of the habitual transactions of the companies. Nor will it be necessary to report on operations that are part of the ordinary business of the company, are made on an arm's-length basis and are of scant significance in respect of the true and fair view of the company.

The information on operations with related parties shall be submitted broken down under the following headings: a) operations entered into with significant shareholders of the company; b) operations entered into with directors and executives of the company; c) operations entered into between persons, companies or entities of the group; and d) operations with other related parties.

Under each heading, quantified information shall be provided on the operations entered into by the company with related parties until their termination. The information will cover the type and nature of the operations transacted, their quantification, the profit or loss accruing on each type of operation for the company, the pricing policy used, terms and conditions of payment, details of the guarantees granted and received and the related parties involved, and any other facet of the operations allowing a proper interpretation of the transaction made. The information may be aggregated when items of similar content are involved.

In any event, the companies issuing securities traded on official securities markets shall be obliged to provide itemised information on related-party operations that are significant in terms of their amount or of their relevance for a proper understanding of the periodic public information.

Finally, the CNMV may allow individual exemptions from compliance with these obligations if the information runs counter to the public interest or is seriously detrimental to the company disclosing it because an industrial, trade or financial secret or some piece of information that may adversely affect its competitive position is involved, provided that such exemption does not mislead the public regarding facts and circumstances the knowledge of which is essential for assessing the securities concerned.

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5. "Significant influence" shall be understood as the possibility of designating or removing a member of the company's board of directors, or of having proposed such designation or removal. The term is also understood to cover participation in the financial and operational decisions of a company, even though control is not exerted.

New regulations for tax on personal and corporate income and on non-resident income

INTRODUCTION

The fourth additional provision of Law 46/2002 of 18 December 2002 on the partial reform of personal income tax, amending the Laws on corporate income tax and on non-resident income, established, under the wording in Law 62/2003 of 30 December 2003 on fiscal, administrative and social measures, that the Government should draft and approve within fifteen months from the entry into force of this Law the revised texts on tax on personal income, on non-resident income and on corporate income. In compliance therewith, the government published Royal Legislative Decree 3/2004 of 5 March 2004, approving the revised text of the Law on personal income tax; Royal Legislative Decree 5/2004 of 5 March 2004, approving the revised text of the Law on non-resident income tax; and Royal Legislative Decree 4/2004 of 5 March 2004, approving the revised text of the Law on corporate income tax.

NEW PERSONAL INCOME TAX REGULATIONS

Royal Decree 214/1999 of 5 February 1999, which approved the personal income tax regulations now being repealed, contained the regulatory provisions implementing Law 40/1998 of 9 December 1998 on personal tax and other tax rules. So as to consolidate in a single regulatory text all the regulatory provisions published since that date, Royal Decree 1775/2004 of 30 July 2004 (BOE of 4 August) was promulgated, approving the personal income tax regulations.

Technical amendments of references made in the previous text are introduced into this Royal Decree owing to the recent approval of certain regulations, such as Law 22/2003 of 9 July 2003 on bankruptcy, and Law 58/2003 of 17 December 2003 on general tax measures. Also included are the new instances under which it is obligatory to file a return and which affect taxpayers entitled to a deduction for having a "cuenta ahorro-empresa" (a savings account in which money deposited is earmarked for setting up a new company) or who make contributions to protected funds for disabled people or to retirement security policies. The legislation likewise reflects the obligations of representatives designated by insurance corporations and by the management companies of collective investment institutions operating in Spain under a regime of free provision of services to withhold and pay in tax on account. Finally, the amounts that were still in pesetas have been converted into euro.

NEW CORPORATE INCOME TAX REGULATIONS

Royal Decree 537/1997 of 14 April 1997, which approved the corporate income tax regulations now being repealed, contained the regulatory provisions implementing the tax regime for corporate income taxpayers, regulated by Law 43/1995 of 27 December on corporate income tax. Likewise, all the regulatory provisions published since that date have been consolidated in a single text further to the promulgation of Royal Decree 1777/2004 of 30 July 2004 (BOE of 6 August), approving the corporate income tax regulations.

As in the foregoing case, this Royal Decree introduces certain technical amendments arising from the publication of specific legislation, such as the aforementioned bankruptcy and general tax measures laws, and Royal Decree 867/2001 of 20 July 2001 on the legal regime of investment services companies. Regarding this latter Royal Decree, the exemption from the obligation for all investment services companies to withhold interest received is extended.

A further case in which there is no obligation to withhold is that for income arising from a change in pension commitments instrumented in a group insurance contract that has been subject to a financing scheme that has not been implemented completely.

The regulatory provisions implementing the regime governing the reinvestment of extraordinary profits, contained in Law 43/1995 of 27 December 1995, have been eliminated. Further, the list of parties obliged to make a withholding or a payment on account has been completed, including representatives of certain institutions operating in Spain under a regime of free provi-

sion of services, designated in accordance with the provisions of Law 30/1995 of 8 November 1995 on the regulation and supervision of private insurance, and of Law 35/2003 of 4 November 2003 on collective investment institutions, respectively. Finally, the amounts still featured in pesetas have been converted into euro.

NEW NON-RESIDENT INCOME TAX REGULATIONS

Royal Decree 326/1999 of 26 February 1999, which approved the Regulation on the taxation of non-resident income and is now being repealed, contained the regulatory provisions implementing the regime governing the taxation of non-resident taxpayers, as established by Law 41/1998 of 9 December 1998 on the taxation of non-resident income and tax rules. As in the previous cases, Royal Decree 1776/2004 of 30 July 2004 (BOE of 5 August) was promulgated, which approved the Regulation on the taxation of non-resident income and which draws together in a single regulation all the regulatory provisions published since that date.

This Royal Decree re-numbers the articles and certain chapters of the Regulation, adapting itself to the order followed in the consolidated text of the Law, and it makes technical amendments of references made in the text of certain regulations, in accordance with the publication of the aforementioned General Tax Law, and of Royal Decree 1496/2003 of 28 November 2003 approving the Regulation governing billing obligations.

Finally, by virtue of Law 35/2003 of 4 November 2003 on collective investment institutions, the list of parties obliged to make a withholding or payment on account is completed, including the designated representatives acting on behalf of management companies operating under a regime of free provision of services.

18.10.2004