Financial regulation: 2010 Q4

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Introduction

In 2010 Q4 numerous pieces of financial legislation were published, as is usual in the final quarter of the year.

The European Central Bank (ECB) made certain changes to the monetary policy instruments and procedures of the Eurosystem. It also updated the conditions for participating in TARGET2, which have subsequently been adapted by the Banco de España.

In relation to credit institutions, five pieces of legislation were published containing the following changes: amendment of the regulations on minimum own funds in order to transpose two recent EU directives; the adaptation of accounting policies to the new rules for the preparation of consolidated annual accounts; the development of certain aspects of the mortgage market; certain technical refinements to the rules on the advertising of banks' services and products; and the introduction of a series of clarifications of the new legal framework for savings banks.

In the area of financial institutions, development of the rules on qualifying holdings in accordance with EU law was completed and, as in the case of credit institutions, the general chart of accounts for insurance companies was adapted to the new rules for the preparation of annual accounts.

In the context of securities markets, three pieces of legislation were promulgated: reform of the regulation of official secondary markets for futures, options and other derivatives; an update of certain administrative procedures and authorisations of venture capital entities; and an update of the accounting rules and financial statements of securitisation SPEs.

In the European sphere, the European System of Financial Supervisors was set up, in order to preserve financial stability and strengthen the coordination of supervision in the EU. In addition, the law on public offerings and the admission of securities to trading has been amended, and the capital requirements for the trading portfolio and resecuritisations have been updated.

Also, the rules on preparation of the consolidated annual accounts and the general chart of accounts have been amended to incorporate the accounting changes in two EU regulations in relation to consolidated and separate financial statements, and business combinations.

Finally, the monetary, financial and fiscal changes contained in the State budget for 2011 are analysed.

European Central Bank: amendment of the regulations on the monetary policy instruments and procedures of the Eurosystem

Guideline ECB/2010/13 of 16 September 2010 (OJ L of 9 October 2010) and Guideline ECB/2010/30 of 13 December 2010 (OJ L of 21 December 2010), which amend Guideline ECB/2000/7 of 31 August 2000 on monetary policy instruments and procedures of the Eurosystem, were published in 2010 Q4.

CHANGES MADE BY GUIDELINE ECB/2010/13

This guideline contains the changes to the definition and implementation of the Eurosystem's monetary policy procedures and operations that the Governing Council of the ECB has decided to make in recent months and which are now incorporated into the text of Guideline ECB/2000/7. The most important changes are discussed below.

The Eurosystem can adopt new measures vis-à-vis counterparties that fail to perform their obligations, both in tenders and in bilateral operations. Specifically, the Eurosystem can impose financial penalties on a counterparty or suspend it from open market operations for a specific period of time when it fails to transfer a sufficient amount of underlying assets or cash to settle or secure the amount of a liquidity providing or absorbing transaction.

The discretionary measures available to the Eurosystem to address concerns regarding the financial soundness of a counterparty are enhanced and strengthened. Thus, on the grounds of prudence, it may suspend, limit or exclude counterparties' access to monetary policy instruments, reject assets, limit the use of assets or apply supplementary haircuts to assets submitted as collateral.

In exceptional circumstances the ECB is permitted, in the case of open market operations, to carry out outright transactions in a centralised manner.[1]

In the section on collateral, the Eurosystem strengthens the requirements that the assets underlying asset-backed securities must meet to be admitted as collateral in its transactions, in order to reduce the claw back risk associated with such bonds. Thus, in addition to those already established,[2] the following now also apply: a) both the originator of the assets and the issuer or, where applicable, the intermediary of the bonds must be incorporated in the European Economic Area (EEA),[3] and b) if they are credit claims, the obligors and the creditors must be resident in the EEA (natural persons) or incorporated in the EEA (legal persons) and, if relevant, the related security must also be located in the EEA.

Where originators or intermediaries have been incorporated in the euro area or in the United Kingdom, the Eurosystem must verify the absence of claw back clauses in those jurisdictions. If the originator or the intermediary, is incorporated in another EEA country, the asset-backed securities can only be considered eligible if the Eurosystem ascertains that its rights would be protected in an appropriate manner against claw back provisions considered relevant by the Eurosystem under the law of the relevant EEA country.[4]

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1. Previously they were only executed in a decentralised manner by the national central banks. **2.** The requirements previously established are the following: a) their acquisition must be governed by the law of an EU Member State; b) they must be acquired by the securitisation special purpose vehicle (or similar entity) from the originator or an intermediary in a manner which the Eurosystem considers to be a "true sale", and be beyond the reach of the originator or its creditors; and c) they must be original, i.e. they must not consist, in whole or in part, actually or potentially, of tranches of other asset-backed securities, credit-linked notes, swaps or other derivatives instruments, or synthetic securities. **3.** The EEA came into existence on 1 January 1994, as the result of an agreement between member countries of the European Union (EU) and the European Free Trade Association (EFTA). Its creation enabled EFTA countries to participate in the EU's single market without having to join the EU. It is made up of the 27 EU countries and the following members of EFTA: Iceland, Liechtenstein and Norway. **4.** An independent legal assessment in a form acceptable to the Eurosystem must be submitted setting out the applicable claw back rules in the country, before the asset-backed securities can be considered eligible. Claw back rules which the Eurosystem considers to be severe and therefore not acceptable include rules whereby the sale of underlying assets can be invalidated by the liquidator solely on the basis that it was concluded within a certain period (suspect period) before the declaration of insolvency of the seller (originator/intermediary), or where such invalidation can only be prevented by the transferee if they can prove that they were not aware of the insolvency of the seller (originator/intermediary) at the time of the sale

As regards the Eurosystem's credit assessment system,[5] the criteria applicable to asset-backed securities are maintained and their credit standards requirements are specified. These securities are required to have two external "triple A" ratings at issuance and to retain a minimum threshold "single A" rating over their lifetime.

Under the rules for the use of eligible assets, as was already the case, counterparties cannot submit assets issued by another entity with which they have close links as collateral, although there have always been a number of exceptions to this. A further exception is now added, namely residential real estate loan-backed structured covered bonds, i.e. certain covered bonds not declared UCITS (undertakings for collective investment in transferable securities)[6] compliant by the European Commission, that fulfil all the criteria that apply to asset-backed securities, together with certain additional criteria[7] that are now introduced.

In addition, the Eurosystem may limit the use of unsecured debt instruments issued by a credit institution or by any other entity with which the credit institution has close links. Thus, such assets may only be used as collateral by a counterparty to the extent that the value assigned to that collateral by the Eurosystem after the application of haircuts does not exceed 10% of the total value of the collateral submitted by that counterparty. This limit does not apply to such assets if they are guaranteed by a public sector entity which has the right to levy taxes, or if the value after haircuts of the assets does not exceed €50 million.

The risk control framework for credit operations is revised. Thus, the Eurosystem may not only exclude certain assets from use in its monetary policy operations, but also counterparties, in particular if the credit quality of the counterparty appears to exhibit a high correlation with the credit quality of the collateral submitted by the counterparty.

Finally, new terms are added and other terms are defined more precisely, changes in statistical regulations are reflected and certain provisions are harmonised to improve coherence and transparency.

CHANGES MADE BY GUIDELINE ECB/2010/30

The most important changes made by Guideline ECB72010/30 are the following:

Fixed term deposits are added as eligible collateral for Eurosystem monetary policy operations and intraday credit.

A new exception is made to the rules for the use of eligible assets, allowing counterparties to submit commercial mortgage loan-backed covered bank bonds issued by another entity with which they have close links as collateral. In parallel with the previous section, these are covered bank bonds not declared UCITS compliant by the European Commission, that fulfil all the criteria that apply to asset-backed securities and certain additional criteria.[8]

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5. The Eurosystem's credit assessment system defines the procedures, rules and techniques which ensure that the requirement for high credit standards imposed by the Eurosystem for all eligible assets is met. **6.** See Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS). **7.** Including, that any residential real estate loans underlying the structured covered bonds must be denominated in euro; the issuer (and the debtor and guarantor, if they are legal persons), must be incorporated in a Member State, their underlying assets must be located in a Member State and the law governing the loan must be that of a Member State. Also, High quality substitute collateral up to 10 % of the cover pool is accepted. **8.** Including, that any commercial mortgage loans underlying the structured covered bank bonds must be denominated in euro; the issuer (and the debtor and guarantor, if they are legal persons), must be incorporated in a Member State, their underlying assets must be located in a Member State and the law governing the loan must be that of a Member State. Also, high quality substitute collateral, for up to 10% of the cover pool, is accepted. This threshold can only be exceeded after an in-depth review by the relevant NCB.

Guideline ECB/2010/13 entered into force on 18 September 2010 and has applied from 10 October 2010, except for Annex II which has applied from 1 January 2011. Guideline ECB/2010/30 entered into force on 15 December 2010 and has applied from 1 January 2011, except for Paragraph 2 of the Annex which will apply from 1 February 2011.

TARGET2: updating of its regulations

Guideline ECB/2010/12 of 15 September 2010 (OJ L of 5 October 2010) was published. This amends Guideline ECB/2007/2 of 26 April 2007 on a Trans-European Automated Real-time Gross settlement Express Transfer system (TARGET2),[9] in order to take into account the updates for TARGET2 release 4.0, in particular to allow participants to access one or more Payments Module (PM) accounts using internet-based access;[10] and (b) to reflect a number of technical changes following the entry into force of the Treaty on the Functioning of the European Union[11] and clarify a few issues. Also, the Resolution of the Banco de España of 6 October 2010 (BOE of 16 November 2010) was published. This amends the Resolution of 20 July 2007[12], approving the general clauses relating to the harmonised conditions for participation in TARGET2-Banco de España (TARGET2-BE),[13] to adapt it to the Guideline ECB/2010/12.

CHANGES MADE BY GUIDELINE ECB/2010/12

Apart from the harmonised conditions for participation in TARGET2,[14] which have already been adopted by each participating national central bank (NCB), the arrangements and supplemental harmonised conditions for participation in TARGET2 using internet-based access (see the new Annex V added to Guideline ECB/2007/2) must now be introduced.

This method of access to the PM account will be incompatible with that provided via the network service provider.[15] However, the participating NCB may choose to have one or more PM accounts, each of which will be accessible by either the internet or the network service provider.

Also, the Governing Council of the ECB is charged with specifying the principles applicable to the security of certificates used for internet-based access.[16]

CHANGES MADE BY THE RESOLUTION OF 6 OCTOBER 2010

It is explicitly established as a condition for accessing TARGET2-BE that participating credit institutions are not subject to restrictive measures adopted by the Council of the European Union or Member States pursuant to the Treaty on the Functioning of the European Union, the implementation of which, in the view of the Banco de España after informing the ECB, is incompatible with the smooth functioning of TARGET2. These same conditions apply to participating entities for access to intraday credit.

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9. TARGET2 is characterised by being a single shared platform, through which all payment orders are submitted and processed and through which payments are received in the same technical manner. **10.** Internet-based access involves participants opting for a Payments Module account that can only be accessed via the internet and submitting payment messages or control messages to TARGET2 by means of the internet. **11.** The consolidated versions of the Treaty on European Union and of the Treaty on the Functioning of the European Union, together with the protocols and annexes thereto, as they result from the amendments introduced by the Treaty of Lisbon signed on 13 December 2007 in Lisbon and which entered into force on 1 December 2009 may be consulted in the Official Journal of the European Union, series C, number 83 of 30 March 2010. **12.** See "Financial regulation: 2007 Q4», *Economic Bulletin*, January 2008, Banco de España, pp. 172-173. **13.** TARGET2 is characterised by being a single shared platform, through which all payment orders are submitted and processed and through which payments are received in the same technical manner. **14.** See Annex II to the Guideline. **15.** The network service provider is the undertaking appointed by the Governing Council of the ECB to supply computerised network connections for the purpose of submitting payment messages in TARGET2. **16.** "Certificate" or "electronic certificate" means an electronic file, issued by the certification authorities, that binds a public key with an identity and which is used for the following: to verify that a public key belongs to an individual, to authenticate the holder, to check a signature from this individual or to encrypt a message addressed to this individual. Certificates are held on a physical device such as a smart card or USB stick, and references to certificates include such physical devices. The certificates are instrumental in the authentication process of the participants accessing TARGET2 through the internet and submitting payment messages or control messages

New events of default by entities are added, on the basis of which the Banco de España will suspend or terminate access to intraday credit, such as where a decision is made by a competent judicial or other authority to implement in relation to the entity a procedure for the winding-up of the entity or any other analogous procedure, or where the entity becomes subject to the freezing of funds and/or other measures imposed by the Union restricting the entity's ability to use its funds. Also new cases are added in which the Banco de España may suspend or terminate, without prior notice, an entity's participation in TARGET2-BE, such as where the participating entity fails to carry out any material obligation or any other participant-related event occurs that threatens the overall stability, soundness and safety of TARGET2-BE.

A new set of clauses is introduced with the harmonised conditions for participation in TARGET2-BE using internet-based access in accordance with Guideline ECB/2010/12. Certain clauses are no longer applicable, others are modified and some supplemental ones are established for the use of internet-based access.

Certain technical requirements are established for entities that wish to open an internet-accessible PM account in TARGET2-BE. Specifically, they must specify whether, in addition to internet-based access, they wish to continue accessing TARGET2 through the network service provider, in which case they will have to apply for a separate PM account in TARGET2.

Participants using internet-based access must implement adequate security controls, in particular those specified in the technical specifications that the Banco de España may issue, to protect their systems from unauthorised use.

The Guideline entered into force on 7 October 2010 and has applied from 22 November 2010, the date on which the Resolution of 6 October 2010 entered into force.

Credit institutions: amendment of the regulations on the determination and control of minimum own funds

CBE 9/2010 of 22 December 2010 (BOE of 30 December 2010) has been published. This amends CBE 3/2008 of 22 May[17] on the determination and control of minimum own funds, in order to transpose two EU directives: Commission Directive 2009/27/EC of 7 April 2009 amending certain Annexes to Directive 2006/49/EC of the European Parliament and of the Council as regards technical provisions concerning risk management, and Commission Directive 2009/83/EC of 27 July 2009 amending certain Annexes to Directive 2006/48/EC of the European Parliament and of the Council[18] as regards technical provisions concerning risk management.

The Circular amends certain rules of CBE 3/2008 with regard to: the capital requirements for credit risk, under both the standardised approach and the internal ratings based approach; credit risk mitigation techniques; securitisation; the treatment of counterparty and trading book risk; and market disclosure obligations. In addition, it takes the opportunity to introduce some technical improvements and some improvements to the wording of the text.

Some changes have been made in relation to securitisation. The circumstances in which it is assumed that there has been a significant transfer of risk to third parties are qualified. Along with the requirement that no implicit support may be provided to the securitisation, one of the following two conditions must be fulfilled:

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17. See "Financial regulation: 2008 Q2", *Economic Bulletin,* July 2008, Banco de España, pp.143-153. **18.** See "Financial regulation: 2006 Q2", *Economic Bulletin,* July 2006, Banco de España, pp.142-144.

a) The originator entity's share of the total capital requirements corresponding to the first loss tranches is 20% or less, when there are no mezzanine tranches, and the originator entity can show that the amount of the first loss tranches exceeds by a substantial margin a reasoned estimate of the expected loss arising from the securitised exposures,[19] or

b) The originator entity's share in the capital requirements for the mezzanine tranches is 50% or less (previously it had to be less than 50%).

If the requirements are not fulfilled, but the originator entity considers that the transfer of credit risk is significant, it must demonstrate this to the Banco de España. The Circular specifies that, in order to do this, the originator entity must show that it has policies and methodologies to ensure that the possible reduction in capital requirements resulting from the securitisation is commensurate with the transfer of risk.

Certain changes are made to the way in which the exposure value of liquidity facilities is calculated. A general credit conversion factor of 50% of nominal value is established. Thus a conversion factor of 0% is no longer applied to eligible liquidity facilities granted to asset-backed commercial paper that are drawable in the event of general market disruption.

The technical criteria applicable in relation to the exemption from individual requirements for subsidiary or parent entities of a consolidatable group of credit institutions are clarified, the identification of public sector entities subject to special weighting is facilitated and the rules for weighting tangible assets received as dation in payment are also clarified.

Other technical improvements made by the Circular arise from adopting the criteria established by the Committee of European Banking Supervisors in the guides it has been releasing on the application of banking directives. These include the elimination of any exemption for the own shares that must be deducted from regulatory capital, as well as for financing to third parties for the acquisition of shares, contributions or other securities that are eligible capital of the entity that has granted it or of other entities of its consolidatable group.[20] Also credit institutions now have the option of not including in their capital the amount of the capital gains (losses)[21] on debt instruments that are recorded as valuation adjustments for available-for-sale financial assets in equity, in order to avoid excessive fluctuations in eligible capital.

Finally, in relation to liquidity risk and the risks arising from securitisation operations, for the period while the transposition of Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009[22] has still to be completed, an annex is introduced containing certain "Guidelines supplementing the rules contained in the Circular", establishing a number of provisions tending to strengthen internal organisation, risk management and internal control, and other relevant aspects.

Apart from some specific exceptions, the Circular entered into force on 31 December 2010.

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19. Previously the only requirement was that the first losses tranches were below 20%. **20.** Previously, shares or the financing of shares for staff of the entity or of its economic group, and shares acquired to hedge other market operations, provided that they did not exceed 1% of the total share capital of the acquiring or financing entity itself, were exempt from the deduction from regulatory capital. **21.** These gross amounts will be made up of the credit balance (in accordance with the provisions of CBE 4/2004) of each of the accounts of the adjustments arising from debt or capital instruments, plus the tax correction applied for their integration in such accounts. **22.** Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 amending Directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management, established in its Annex V a series of provisions tending to strengthen internal organisation, risk management and internal control, and the supervision thereof.

Credit institutions: amendment of public and confidential financial reporting rules

CBE 8/2010 of 22 December 2010 (BOE of 30 December 2010), amending CBE 4/2004 of 22 December 2004 on public and confidential financial reporting rules and formats,[23] has been published.

The purpose of the Circular is to adapt CBE 4/2004 to Commission Regulations (EC) No 494/2009 and No 495/2009 of 3 June 2009, which implemented the revisions of the international financial reporting standard (IFRS) 3 and international accounting standard (IAS) 27, approved by Commission Regulation (EC) No 1126/2008 of 3 November 2008 adopting certain international accounting standards, in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council.[24]

The most important changes introduced by the Circular relate to Chapter three "business combination and consolidation".

The new IFRS 3 emphasises the moment of the taking of control as an event that significantly modifies the economic nature and circumstances of the investment. Thus, the new standard specifies issues previously left undefined, such as the estimation of goodwill when control is taken in stages, transactions with the external shareholders and business combinations carried out exclusively by agreement. At the same time, it introduces certain changes in terms of valuation that affect contingent consideration and contingent liabilities.

To facilitate the application of the acquisition method, already used before the modification, a scheme has been introduced for its application: a) to identify the acquirer entity; b) to establish the date of acquisition; c) to identify, if they exist, assets and liabilities that require a separate accounting treatment to the business combination; d) to identify the assets acquired and liabilities assumed that require, as at the date of acquisition, the adoption of decisions, that should be adequately documented, in order to facilitate the future application of other rules of this Circular;[25] e) to recognise and value the identifiable assets acquired and the liabilities assumed; f) to recognise and value, where appropriate, the minority interest in the business acquired; g) to value the consideration paid, and h) to recognise and value the goodwill or, in the case of a worthwhile acquisition, the profit obtained.

The Circular also introduces the cases that do not comply with the definition of business combination, which are limited to the following: the combination of entities that, both before and after the combination, are under common control; the acquisition of assets and liabilities that do not constitute a business and the creation of a joint venture.

As already established, one of the combined entities, in every business combination, must be identified as the acquirer. The Circular now widens the criteria for identifying which of the entities participating in the combination is the acquirer, when the identification involves doubts or difficulties.

On the acquisition date, as already established, the acquirer must value the identifiable assets acquired and liabilities assumed in a business combination at their fair value.[26] The minority

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23. See "Financial regulation: 2004 Q4», *Economic Bulletin,* January 2005, Banco de España, pp.127-132. **24.** This revision is the result of work performed jointly by the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) to converge accounting standards for business combinations and consolidation. **25.** Such as the designation of a derivative financial instrument as subject to hedge accounting, the classification of a financial instrument as held for trading or the separation of an embedded derivative in a hybrid financial instrument. **26.** As defined by CBE 4/2004, fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. In determining the fair value, no deduction shall be made for the transaction costs that might be incurred due to sale or other disposal. The best evidence of fair value is the market price in an active market.

interest will be measured as the proportional part that external shareholders represent in the difference between the identifiable assets acquired and the liabilities assumed. Guidance is now introduced on locating and treating separate transactions, i.e. those that do not form part of the business combination.[27]

The valuation criteria are introduced in those cases in which there has been delivery of consideration to obtain control of an entity. This consideration shall be valued at fair value on the date of acquisition, unless it remains, as an asset or liability, in the combined entity following the business combination, in which case it shall be measured as its book value before the combination, with the additional clarifications introduced by the Circular.

Another change is introduced in relation to the treatment of acquisition-related expenses, such as advisers' fees. These should be recorded as expenses instead of being capitalised.

Another area that is updated is the recognition and valuation of goodwill or the gain on a worthwhile acquisition. On the acquisition date, the acquirer will compare the sum of the consideration paid plus, where applicable, the fair value at that date of its prior equity interest in the acquired business and the amount of the minority interest, with the net fair value of the identified acquired assets less the assumed liabilities.[28] The treatment of goodwill in business combinations in stages is therefore consistent with the idea that the taking of control is an event that significantly modifies the investment.[29]

Also, the general consolidation criteria are revised, as regards the valuations of the investments in entities classified as associates or jointly controlled entities which lose such status; the measurement bases are updated in the full consolidation method, especially to reflect cases of loss of control of a subsidiary; and the information that the acquirer entity must include in the explanatory notes of the individual accounts in relation to each business combination that has been carried out during the accounting period is added. In turn, the valuation of the impairment of the investments measured by the equity method is revised.

Finally, certain updates are made to the references to previous regulations of mercantile companies, whose consolidated text has been included in the recent Law on Share Capital Companies.[30]

The Circular, which entered into force on 31 December 2010, shall apply to all transactions carried out from 1 January 2011.

Credit institutions: development of certain aspects of the mortgage market

CBE 7/2010 of 30 November 2010 (BOE of 6 December 2010), which develops certain aspects of the mortgage market, regulated by Law 2/1981 of 25 March 1981 on mortgage market regulation,[31] has been published. It also amends CBE 4/2004 of 22 December 2004 on public and confidential financial reporting rules and formats, in accordance with the requirements of the new legislation.

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27. In a business combination separate transactions are, in general, those initiated before the date of the combination and that, essentially, have not been carried out for the benefit of the acquired business or of its previous owners. All transactions carried out for the benefit of the acquirer or the combined entity will be considered to be separate transactions in the business combination. Separate transactions may be the result of relationships or contractual agreements existing prior to the start of negotiations to achieve a business combination or may have been carried out during the negotiation period. **28.** Previously, the acquirer compared the cost of the business combination with the acquired percentage of the net fair value of the assets, liabilities and contingent liabilities of the acquired entity. **29.** A business combination in stages is one in which the acquirer has an equity interest in the acquired entity immediately before the date on which it obtains control. **30.** Contained in Royal Legislative Decree 1/2010 of 2 July 2010, approving the consolidated text of the Law on Share Capital Companies **31.** This Law was extensively amended by Law 41/2007 of 7 December 2007, and some of its aspects were implemented by Royal Decree 716/2009 of 24 April 2009. See "Financial regulation: 2007 Q4", *Economic Bulletin*, January 2008, Banco de España, pp. 176-182.

The essential data for the special accounting register[32] that issuers of covered bonds or mortgage bonds must keep, and that must be included in their annual reports, are established. Specifically, in relation to their lending, among other data, certain information on total mortgage loans and credits shall be gathered, distinguishing those that are eligible to back issues of mortgage bonds or collateralised mortgage bonds or to serve to calculate the limit for the issuance of mortgage covered bonds. As for borrowing, certain information on mortgage bonds shall be included, broken down by issue; as well as on mortgage covered bonds, collateralised mortgage bonds and mortgage transfer certificates, broken down in these cases between securities or certificates issued with and without a public offering, as well as, in both cases, according to their residual maturity.

Technical details are given of the minimum content of the note in the annual report that includes an express declaration of the board of directors or equivalent body of the credit institution on the existence of express policies and procedures in relation to its activities in the mortgage market, so that this body expressly takes responsibility for compliance with mortgage market legislation.[33]

Finally, certain technical criteria are included on issues relating to the securitisation of mortgages guaranteed by a credit institution or insurance company,[34] and in relation to the judgment that must be made regarding the possible equivalence of guarantees granted over real estate located in other EU countries. In both cases the documentation the creditor credit institutions or associations that represent them must submit to the Banco de España are specified.

The Circular entered into force on 26 December 2010.

Credit institutions: advertising of banking services and products

CBE 6/2010 of 28 September 2010 (BOE of 11 October 2010) on the advertising of banking services and products has been published. This Circular is addressed to Spanish credit institutions, to the branches in Spain of foreign credit institutions and also to payment institutions regulated by Law 16/2009 of 13 November 2009 on payment services.[35] The Circular implements those aspects of Ministerial Order EHA/1718/2010 of 11 June 2010[36] on regulation and control of advertising for banking products and services which, by express authorisation, are within the remit of the Banco de España.

Specifically, and given the elimination of the prior administrative authorisation regime by the Ministerial Order mentioned above, the Circular determines the principles which advertising must follow, and the general criteria on the minimum content and format of advertising messages, which are set out in its annex. These criteria should be applied in proportion to the complexity of the banking product or service offered and the characteristics of the medium used to disseminate the advertising.

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32. As established by Royal Decree 716/2009, issuers of mortgage covered bonds or mortgage bonds must keep a special accounting register for the mortgage loans and credits that back such issues, of the substitute collateral and of the financial derivative instruments linked to each issue. **33.** Under Royal Decree 716/2009, institutions issuing mortgage covered bonds or mortgage bonds must include a specific note in their annual report containing, inter alia, an express declaration to this effect. **34.** As regards the conditions that mortgage loans and credits must meet to be eligible to back the issuance of mortgage market securities (mortgage covered bonds, mortgage bonds and collateralised mortgage bonds), Royal Decree 716/2009 established that the ratio between the loan and the appraisal value of the mortgaged asset may exceed the general limit of 80%, without exceeding 95%, if the operation enjoys insurance or a bank guarantee provided by an entity other than the creditor, which must fulfil certain requirements. **35.** See "Financial regulation 2009 Q4" *Economic Bulletin*, January 2010, Banco de España, pp. 150-55. **36.** See "Financial regulation: 2010 Q2", *Economic Bulletin*, July 2010, Banco de España, pp.136-38.

At the same time, the Circular regulates the internal procedures and controls, and the commercial communication policy of credit institutions. This policy must incorporate the general principles mentioned in the annex and, in general, the legislation applicable to their advertising activity. It must also set out the procedures necessary to adapt the products offered and the way in which they are presented to the characteristics of the target group.

A presumption is established, that institutions belonging to certain "advertising self-regulation systems" have adequate internal procedures and controls in the area in question. Among other aims, the intention is to encourage credit institutions to join an approved advertising self-regulating body. For this purpose, the Banco de España will publish on its website, a list of institutions belonging to "advertising self-regulation systems" that comply with certain requirements laid down by the Circular. It will also indicate the system to which each institution belongs, along with its code of conduct.

Credit institutions that are not members of an approved "advertising self-regulation system", or whose advertising does not remain subject to the regime of prior authorisation by the regional government (as is the case of savings banks and certain credit cooperatives), must submit their commercial communication policy and their alternative internal controls to minimise the risks associated with inappropriate advertising to supervision by the Banco de España.

The characteristics and minimum content of the internal register that each institution must keep are specified. This register will be used to conserve and record all documentation corresponding to each advertising campaign and it will be accessible by the Banco de España. In certain cases, the group to which the institution belongs may have a centralised register.

Finally, in the exercise of its administrative power to require the cessation or rectification of banking advertising, the Banco de España will contact credit institutions whose products are advertised in the relevant campaign, indicating, with reasons, those aspects of the advertising that do not comply with the applicable legislation and any rectification it may consider appropriate. In this respect, the deadlines and procedures for institutions to object or present submissions are established. Where applicable, the rectification is made by the same means used to disseminate the campaign and with the same scope. All this is without prejudice to any liability they may have incurred under the penalty regime established by Law 26/1988 of 29 July 1988 on discipline and intervention of credit institutions.

The Circular entered into force on 11 December 2010.

Modification of the legal regime for savings banks

Final provisions three and four of Law 36/2010 of 22 October 2010 (BOE of 23 October 2010) on the Fund for the Promotion of Development[37] have made a number of clarifications to the new legal regime for savings banks, which is now regulated by Law 31/1985 of 2 August 1985 on regulation of the basic rules on governing bodies of savings banks[38] and by Royal Decree-Law 11/2010 of 9 July 2010 on governing bodies and other aspects of the legal regime of savings banks.[39]

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37. The purpose of the Law is to create and establish the legal regime for the Fund for the Promotion of Development as an instrument for cooperation and development, managed by the Ministry for Foreign Affairs and Cooperation, through the State Secretariat for International Cooperation. This Fund assumes and extends the functions of the Fund to Aid Development, which was created by Royal Decree-Law 16/1976 of 24 August 1976, on economic regulation, fiscal measures, promotion of exports and domestic trade. **38.** See "Regulación financiera: tercer trimestre de 1985", *Boletín Económico,* October 1985, Banco de España, pp. 61-62. **39.** See "Financial regulation: 2010 Q3", *Economic Bulletin,* October 2010, Banco de España, pp.139-144.

The percentage representation of entities representing collective interests on the governing bodies of savings banks is modified. From now on it will be at least 5% of the voting rights in each body (previously it was subject to a maximum of 10%).

Resolutions of the assembly must be adopted, as a general rule, by a simple majority of the votes of those present (previously only the existence of a simple majority was specified).[40]

Finally, a new exception is envisaged to the limit on the length of the terms of office of members of the governing bodies of savings banks which, generally, cannot exceed 12 years. In those savings banks that resolve to combine with other institutions or to carry on their financial activity indirectly, the appointments in force upon the entry into force of this law may be extended beyond the limit of 12 years and until completion of the term of office in question.

Financial institutions: development of the regime governing qualifying holdings

The following new legal provisions have been promulgated: *CBE 5/2010 of 28 September 2010* (BOE of 11 October 2010) on the list of information which the potential acquirer of a qualifying holding[41] in a credit institution has to send to the Banco de España;[42] *CNMV Circular 5/2010 of 18 November 2010* (BOE of 6 December 2010) on information to be submitted by the potential acquirer for the prudential assessment of purchases of qualifying holdings and of increases in holdings in investment firms and in management companies of collective investment institutions;[43] and Ministerial Order EHA/3241/2010 of 13 December 2010 (BOE of 17 December 2010) approving the list of information to be submitted in the event of acquisition or increase of qualifying holdings and by those intending to hold administrative and management posts in insurance and reinsurance companies and in firms engaging primarily in the holding of ownership interests in such companies.[44]

The requirement for this information is extended to the cases in which such a holding is directly or indirectly increased such that the voting rights or capital held are equal to or more 20%, 30% or 50% or the target entity can be controlled.

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40. The requirement for the attendance of general assembly members and, if applicable, non-voting equity unit holders with a majority of the voting rights is maintained, and also the favourable vote of at least two thirds of the voting rights of those attending is required for the approval and amendment of the articles of association and the internal rules of the savings bank, for the winding-up and liquidation of the institution, its merger or integration with other institutions, its transformation into a special foundation and the decision to carry on its activity indirectly, as provided for in Royal Decree-Law 11/2010. **41.** A qualifying holding in an undertaking is one which represents 10% or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of that undertaking, defined as the ability to appoint or remove members of the Board of Directors. **42.** Royal Decree 1817/2009 of 27 November 2009 amending Royal Decree 1245/1995 of 14 July 1995 on the creation of banks, cross-border activity and other matters relating to the legal regime of credit institutions and Royal Decree 692/1996 of 26 April 1996 on the legal regime of specialised credit institutions entrusted the Banco de España with preparing, through a circular, a list of the information to be provided by the potential acquirer of a qualifying holding in order to assess the latter's suitability and the financial soundness of the proposed acquisition. Also, it was stipulated that the Banco de España had to make public the content of that list on its website. See "Financial Regulation: 2009 Q4", Economic Bulletin, January 2010, Banco de España, pp. 144-146. **43.** In the collective investment institution (CII) area, Royal Decree 1818/2009 of 27 November 2009, which amended the Regulations of CII Law 35/2003 of 4 November 2003 approved by Royal Decree 1309/2005 of 4 November 2005, and, in the investment firm area, Royal Decree 1820/2009 of 27 November 2009, which amended Royal Decree 361/2007 of 16 March 2007 implementing Securities Market Law 24/1988 of 28 July 1988 and Royal Decree 217/2008 of 15 February 2008, entrusted the CNMV with preparing, through a circular, a list of the information to be provided by the potential acquirer for the prudential assessment of qualifying holdings and of the increase in holdings in investment firms and in CII management companies, respectively. Also, it was stipulated that the CNMV had to make public the content of that list on its website. **44.** In the insurance area, Royal Decree 1821/2009 of 27 November 2009, amending the Regulation on the Ordering and Supervision of Private Insurance approved by Royal Decree 2486/1998 of 20 November 1998, on qualifying holdings entrusted the Ministry of Economic Affairs and Finance with approving a list of the information to be provided by the potential acquirer of a qualifying holding in the notification for prudential assessment of qualifying holdings and of the increase in holdings in insurance companies. Also, it was stipulated that the Directorate General of Insurance and Pension Funds (DGSFP) had to make public the content of that list on its website.

The list of all the information to be provided by the potential acquirer, which is located in the annexes of the respective legal provisions, is divided into two parts.

The first part consists of the following: 1) general information on the identity of potential acquirers which, in the case of legal persons, includes a list of the members of the Board of Directors or equivalent body and of the senior officers; 2) additional information to assess the integrity of acquirers, including a description of their professional activities and of the companies they direct or control and, where appropriate, their links or relationships of a financial nature (e.g. credit operations, guarantees, pledges) or of a non-financial type (family relationships, among others) with the entity it is intended to acquire; 3) information on the acquisition and on its basic purpose (strategic investment, portfolio investment, etc.); and 4) information about the financing of the acquisition (i.e. the own and borrowed funds used to acquire the holding).

The second part of the list is devoted to information on the level of holding it is intended to acquire, specifying whether the acquisition of the holding will or will not entail a change in control of the entity. If there is a change in control, the acquirer must submit to the relevant supervisory authority,[45] among other documentation, a business plan containing information on the strategic development plan[46] relating to the acquisition. If the acquisition does not give rise to change in control of the entity, the potential acquirer should provide a document on strategy with detailed information on his intentions and on the objectives and strategies pursued through the proposed acquisition.

Potential acquirers shall give prior notice in writing of their decision to the supervisory authority, indicating the amount of the proposed holding and shall include in that notification the information included in the list. In the event of the absence of any of the circumstances about which information is requested, this shall be expressly confirmed by the person providing the information. For its part, the supervisory authority may, if it sees fit, ask the direct acquirer to provide information on one or more of the persons or entities through which the holding has been acquired.

If the direct or indirect potential acquirer is another credit institution or a supervised financial institution, it is exempted from submitting certain information contained in the first part of the list, in application of the principle of proportionality.

Should the potential acquirer have been assessed in the previous two years, its notifications of subsequent acquisitions should only furnish information constituting an update of that already submitted, along with a declaration that the other information has not changed.

Should the acquisition have taken place involuntarily, for example as a result of the repurchase by the financial institution of its own shares held by other shareholders, or in the event of an increase in capital in which existing shareholders do not participate, the required notification must be made as soon as the shareholder becomes aware that any of the aforementioned thresholds has been crossed (20%, 30% or 50% or the target entity can be controlled), even if it is intended to reduce the level of shareholding so

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45. The Banco de España, CNMV or Directorate General of Insurance and Pension Funds. **46.** The strategic development plan has to indicate the main objectives of the proposed acquisition and how to achieve them, including, among other things: the detailed purpose of the acquisition, the medium-term financial goals (return on equity, cost-benefit ratio, earnings per share, etc.), the main synergies to be pursued within the target financial institution, the possible redirection of activities within the target institution; and general modalities for including and integrating the target institution in the group structure of the acquirer.

that it once again falls below the threshold level,[47] so that its suitability can be assessed.

A specific section of Ministerial Order EHA/3241/2010 details the information to be provided to the Directorate General of Insurance and Pension Funds by the aforementioned natural or legal persons intending to hold administrative or management posts in insurance and reinsurance companies and in firms engaging primarily in the holding of ownership interests in such companies. This information is specified in the list included as Annex II to the Ministerial Order.[48] Should those persons be subjected to supervision by the Directorate General of Insurance and Pension Funds, they would only have to provide the information that had not previously been submitted or that had to be updated.

CBE 5/2010 came into force on 31 October 2010; CNMV Circular 5/2010 came into force on 26 December 2010; and Ministerial Order EHA/3241/2010 came into force on 1 January 2011.

Insurance companies: amendment of the chart of accounts

Royal Decree 1736/2010 of 23 December 2010 (BOE of 30 December 2010) amended the chart of accounts for insurance companies approved by Royal Decree 1317/2008 of 24 July 2008[49] so as to include the changes made by Royal Decree 1159/2010 of 17 September 2010 establishing rules for the preparation of consolidated annual accounts.

As with credit institutions, the incorporation of the acquisition method is the keystone of consolidation, since it sets the general criteria for including the assets and liabilities of subsidiaries in the consolidated accounts on the date that control is taken. The other changes are similar to those described for credit institutions.

The content of the chart of accounts is adapted to Commission Regulation 1004/2008 amending Regulation 1725/2003 adopting certain international accounting standards and, in particular, the changes to IAS 39 and IFRS 7 approved by the International Accounting Standards Board on 13 October 2008. The adaptation consists of a partial revision of Recording and Valuation Rule 8 (financial instruments) as regards financial asset reclassification, including, in this respect, additional supplementary disclosures in the notes to annual accounts.

The Royal Decree came into force on 31 December 2010 and is to be applied in preparing the individual annual accounts for the accounting periods starting on or after 1 January 2010. If the entities include comparative information from the previous accounting period adapted to the new criteria, the date of first-time application would be that of the previous year, i.e. 1 January 2009.

Official secondary markets for futures, options and other derivatives: new regulations

Royal Decree 1282/2010 of 15 October 2010 (BOE of 16 October 2010) regulating the official secondary markets for futures, options and other derivatives repealed the previous regulations contained in Royal Decree 1814/1991 of 20 December 1991.[50]

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47. If the shareholder intends to reduce the level of shareholding so that it once again falls below the threshold level within a period of less than three months, it should state how it intends to do so and expressly undertake not to exercise the voting rights carried by the excess shares. **48.** Basically, the list in Annex II refers to the following information: identity of the natural or legal persons; detailed description of their activities; list, where applicable, of the members of the Board of Directors or equivalent body and of the senior officers; relevant information for assessing integrity; description of links or relationships of a financial nature (loans, guarantees and collateral) or of a non-financial nature (including family relationships) and description of any other link, interest, relationship or activity which could give rise to a conflict of interest with the insurance company, reinsurance company or the group of which it forms part; and, in this case, the measures to be adopted to remedy that conflict of interest. **49.** See "Financial Regulation: 2008 Q3", Economic Bulletin, October 2008, Banco de España, pp. 137-139. **50.** See "Regulación financiera: cuarto trimestre de 1991", Boletín Económico, January 1992, Banco de España, pp. 63 and 64.

The aims of this Royal Decree are: to bring Spanish regulation into line with the regulatory standards prevailing in the relevant international markets; to promote the introduction of new products, services and lines of business in the Spanish derivatives markets; to reduce the systemic risk associated mainly with the clearing and settlement of derivatives contracts; and to help deepen the single European market through the establishment of agreements and links with other Union derivatives markets to promote interoperability, efficiency gains and the choice of market infrastructure by users.

The main changes introduced by the Royal Decree are as follows:

BROADENING OF SCOPE OF APPLICATION

The Royal Decree extends the range of products that can be traded and registered in these markets, which are not limited to futures and options, but also include all the derivatives defined in Securities Market Law 24/1988 of 28 July 1988,[51] whatever the underlying asset may be.

The Royal Decree provides that the market operator may offer trading, registration, clearing, settlement and counterparty services. Also, the market operator may carry out central counterparty activities in accordance with the provisions of the Securities Market Law, subject to the specificities of and as may be provided by market regulations.[52]

Further, it is provided that the market operator may carry out counterparty functions in respect of contracts traded in markets or in trading systems not managed by the market operator, when the latter has entered into the appropriate agreements to carry out the functions of a central counterparty clearing house, in accordance with the provisions regulating that market or trading system.

UPDATING OF MARKET REGULATION

The content of the market regulations and of the general terms and conditions of contracts are updated and certain references, such as those to order type and trading hours, are omitted.

The compulsory intervention of the operators of the markets in which the underlying assets of futures and options are traded is discontinued.[53] This intervention shall only be made at the initiative of the CNMV when special circumstances may disrupt normal market operations or such a measure is warranted to protect investors.

The market regulations provide for the division of the central register into various sub-registers containing details of the contracts of customers of market members.[54]

Each futures and options market is no longer required to have its own market operator and the definition thereof is updated as required by the Securities Market Law.

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51. See "Regulación financiera: tercer trimestre de 1988", Boletín Económico, October 1988, Banco de España, pp. 61 and 62. **52.** In the exercise of those activities, the market operator may establish agreements with other resident and non-resident entities whose functions are similar or which manage securities clearing and settlement systems, are shareholders of those entities or admit them as shareholders. Such agreements shall require the prior approval of the CNMV or, where applicable, of the government. **53.** Under the previous legislation, the Minister for Economic Affairs and Finance, for economic policy reasons and upon a prior report from or at the proposal of the CNMV, with a report from the operators of the futures and options markets and of the markets in which the underlying assets of the futures or options are traded, could suspend trading in one or more traded contracts or even temporarily suspend all activity in them in the event of special circumstances which could seriously disrupt normal operations. **54.** Thus the accounting register for contracts will be made up of a central register (current system) kept by the market operator and of sub-registers kept by the members authorised to do so. These have to comply with the requirements set in the market regulations for managing those registers, without prejudice to any obligations imposed on them by this Royal Decree for the keeping of such registers.

MARKET OPERATORS

The own funds of market operators are strengthened. They must not be less than €18 million (previously €9 million) or than the total collateral provided by the market operator. However, it is provided that the Ministry of Economic Affairs and Finance or, with its express consent, the CNMV may determine a lower minimum amount of own funds depending on the characteristics of the market in question and on the adequacy of those own funds and their liquidity, in accordance with the risks assumed at any time and the stress tests and other similar techniques used.

OFFICIAL SECONDARY FUTURES AND OPTIONS MARKET MEMBERS

The Royal Decree updates the entities eligible to become market members and the regulation of access to such status, which will continue to be granted by the market operator. As a new development, the conditions are specified for becoming a member with restricted trading and registration-requesting capacity for counterparty purposes solely in futures and options and other financial instruments with a non-financial underlying asset.[55]

Also, should the market operator carry out central counterparty functions, it is provided that the entities acting as central securities depository and other central counterparty clearing houses may become market members. In any event, the market operator may reject the participation of those entities that do not admit the participation, on a reciprocal basis, of the market operator in their systems.

COLLATERAL

The regulations on collateral to be provided by members and by customers are updated. The collateral depends on the open positions taken by them or for which they are liable, the type of member in question and the functions carried out by those members in accordance with market regulations.

Further, a collective collateral regime is established. This will be compulsory either for all members or, where appropriate, for certain types of members. The market regulations must specify the criteria for determining the members required to make contributions, the criteria for determining the amount of those contributions and the purpose thereof.[56]

Lastly, the basic principles of the regime governing non-compliance by members and customers, which will be included in the market regulations, are laid down. Specifically, the reasons for non-compliance, the measures to be taken and the procedures and actions to be carried out by the market operator or market members are specified. In the event of non-compliance, the measures may consist of temporary suspension of the member or customer, termination or transfer of registered contracts, realisation of collateral and, ultimately, loss of market member or customer status.

The Royal Decree came into force on 17 October 2010, although the authorised financial futures and options markets have an adaptation period of six months from that date.

Venture capital entities: update of certain administrative procedures and authorisations

CNMV Circular 3/2010 of 14 October 2010 (BOE of 29 October 2010) on administrative procedures for the authorisation of venture capital entities ("ECRs" by their Spanish abbreviation) and their management companies ("SGECRs" by their Spanish abbreviation), for amendment

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55. Thus they have to: a) have recognised and accredited experience and professionalism in the sector of the related non-financial underlying asset; b) have minimum own funds of €50,000; c) have the necessary organisational resources to adequately perform the function of market member; and d) comply with any additional requirements of solvency, organisation and specialisation that may be set by the market operator. **56.** It is also provided that the market regulations may establish a regime governing the contribution of collateral by the market operator based on the functions performed by it, on the nature of the contracts subjected to registration, trading, clearing and settlement and counterparty services, on the types of members participating in the market and on the functions performed by them.

of their internal rules and articles of association and for the communication of changes in directors and managers replaced CNMV Circular 4/1999 of 22 September 1999 in order to adapt its content to the new legal framework established by Law 25/2005 of 24 November 2005[57] regulating venture capital entities and their management companies.

The formal steps of the projects to set up ECRs and SGECRs must be submitted to the CNMV, which, once it has verified that the proposed project complies with current legislation, will issue the compulsory administrative authorisation. However, in the case of venture capital funds not to be created under a public deed, the CNMV can be requested to combine in a single act the authorisation of the fund and its registration in the related administrative register.[58]

The Circular updates and expands the information to be included in the management rules and articles of association. Specifically, in addition to the information stipulated in previous legislation, they must include the basic characteristics of the units/shares, indicating the regime governing the issuance and redemption of units/shares, the frequency with which the value of units/shares is to be calculated for subscription and redemption purposes, and the reasons for winding up venture capital funds and how they are to be liquidated, stipulating how the assets are to be distributed and the notification requirements to be met previously.

The standards of commercial, business or professional integrity for the people taking up senior management positions (directors, general managers or similar officers) in venture capital companies are strengthened, and an internal code of conduct is required.

As a new feature, the Circular requires a manual for the prevention of money laundering. For this purpose, the CNMV draws on the compulsory report from the Executive Service of the Commission for the Prevention of Money Laundering and Monetary Offences as regards the suitability of the procedures included in that manual.[59]

Amendments to the management rules or articles of association generally have to follow the same procedure as that envisaged for their authorisation and require, among other things, an explanation of the reasons for the requested changes to the articles of association or management rules.

Unlike the previous circular, the new Circular lists a series of changes to the management rules or articles of association of ECRs considered to be of minor importance and thus not requiring prior authorisation, such as change of domicile, change of name, capital increases with a charge to venture capital company reserves and asset increases at venture capital funds up to the level of their commitment.

The Circular came into force on 30 October 2010.

Securitisation SPVs: update of accounting rules, annual accounts and financial statements

CNMV Circular 4/2010 of 14 October 2010 (BOE of 5 November 2010) amended CNMV Circular 2/2009 of 25 March 2009[60] on accounting rules, annual accounts, public financial statements and confidential statistical returns of securitisation SPVs.

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57. See "Financial Regulation: 2005 Q4", Economic Bulletin, January 2006, Banco de España, pp. 120-123. **58.** Previously, in all cases, once the CNMV had verified that the proposed project complied with current legislation, it sent to the Ministry of Economic Affairs and Finance the related report and authorisation proposal together with the documentation submitted for that purpose. **59.** Law 10/2010 of 28 April 2010 on the prevention of money laundering and terrorist financing included SGECRs and those venture capital companies not managed by a management company among the entities subject to the obligations established by this Law. They must therefore have procedures and bodies for the prevention of money laundering. **60.** See "Financial Regulation: 2009 Q1", Economic Bulletin, April 2009, Banco de España, pp. 197-198.

The main new feature in this Circular is the amendment, for fiscal reasons, of Rule 13 on impairment of securitised assets.

Until it was amended, Rule 13 on asset impairment of Circular 2/2009 stipulated that models based on statistical methods could be used to determine impairment losses on financial assets. The amendment by the CNMV specifies those statistical models, for which purpose it establishes a methodology similar to that currently required by the Banco de España in Annex IX of CBE 4/2004 in respect of specific provisioning for doubtful assets due to customer arrears.[61]

In this respect, a general treatment is introduced which consists in applying certain percentages of impairment based on the age of the past-due outstandings[62] of any single loan, such that the provision reaches 100% from the age of 12 months.

Specific treatments are stipulated for real estate mortgage loans, finance leases, loans secured by certain collateral and available-for-sale financial assets. In the first, the impairment of financial assets classified as doubtful will be estimated based on the nature of the asset subject to the right in rem.[63] In the second, this same impairment estimation method shall be applied if the leased asset is real estate; if it is personal property, the loss shall be that estimated, which shall, at a minimum, be the difference between the carrying amount of the financial assets and 75% of the fair value of the leased assets.

To record provisions for the impairment of specific loans with partial cash collateral, the allowance percentages listed in the general treatment shall be applied to the difference between the amount at which they are recorded in assets and the present value of the deposits. The impairment of loans with partial collateral consisting of holdings in monetary financial institutions or government debt securities or other financial instruments quoted on active markets shall be provisioned by applying these percentages to the difference between the amount at which they are recorded in assets and 90% of the fair value of such financial instruments.

The amount of the impairment losses on securities included in the available-for-sale financial asset portfolio shall be the positive difference between their acquisition cost, net of any principal repayment and amortisation, and their fair value, less any impairment loss previously recognised in the income statement.

Lastly, the new Circular updates certain annexes to Circular 2/2009 as a result of the amendment of asset impairment rules, and makes certain changes to the public financial statements sent to the CNMV in order to make them easier to complete.

The Circular came into force on 6 November 2010.

European System of Financial Supervisors

The Union adopted *Regulation 1092/2010 of the European Parliament and of the Council of 24 November 2010* (OJ L of 15 December 2010) on European Union macro-prudential over-

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61. The methodology is based on CBE 4/2004 of 22 December 2004 amended by CBE 3/2010 of 29 June 2009 in order to allow a treatment consistent with that used by institutions with similar assets. **62.** Specifically, 25% of the doubtful asset when the first instalment is up to 6 months past-due, 50% when it is up to 9 months past-due, 75% when it is up to 12 months past-due and 100% thereafter. **63.** The estimate of the value of the financial claims received as security will, at a maximum, be the appraisal value, weighted as follows: by 80% for completed housing constituting the borrower's principal residence; by 70% for rural property in use and completed multi-purpose offices and commercial and industrial premises; by 60% for other completed housing; and by 50% for land parcels, building plots and other real estate assets.

sight of the financial system and establishing a European Systemic Risk Board (ESRB) and *Council Regulation 1096/2010 of 17 November 2010* (OJ L of 15 December 2010) conferring specific tasks upon the European Central Bank (ECB) concerning the functioning of the ESRB.

Also adopted were *Regulation 1093/2010 of the European Parliament and of the Council of 24 November 2010* (OJ L of 15 December 2010) establishing a European Supervisory Authority (European Banking Authority); *Regulation 1094/2010 of the European Parliament and of the Council of 24 November 2010* (OJ L of 15 December 2010) establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority); *Regulation 1095/2010 of the European Parliament and of the Council of 24 November 2010* (OJ L of 15 December 2010) establishing a European Supervisory Authority (European Securities and Markets Authority); and *Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010* (OJ L of 15 December 2010) amending Directives 98/26/EC, 2002/87/EC, 2003/6/EC, 2003/41/EC, 2003/71/EC, 2004/39/EC, 2004/109/EC, 2005/60/EC, 2006/48/EC, 2006/49/EC and 2009/65/EC in respect of the powers of the European Supervisory Authorities.

The main new feature of this raft of legislation is the creation of the European System of Financial Supervisors (ESFS). Its main aim is to ensure proper application of rules and regulations in the financial sector, preserve its stability and confidence, and ensure that the consumers of financial services are appropriately and sufficiently protected.

The ESFS will comprise the aforementioned three new European Supervisory Authorities (ESAs), the ESRC, the Joint Committee of the European Supervisory Authorities (Joint Committee) and the competent supervisory authorities of the Member States.

The Joint Committee shall be composed of the ESAs and the ESRC. The former shall cooperate regularly and closely with the ESRC to ensure cross-sectoral consistency of activities and reach common positions in the supervision of financial conglomerates and in other cross-sectoral matters.

EUROPEAN SUPERVISORY AUTHORITIES

The respective ESAs replace the Committee of European Banking Supervisors,[64] the Committee of European Insurance and Occupational Pensions Supervisors[65] and the Committee of European Securities Regulators.[66] Also, the authorities assume all the tasks and competences of those committees including the continuation of ongoing work and projects, where appropriate.

Their main aim is to ensure consistent application of financial sector rules and regulations with the same objectives as the ESFS. They will especially contribute to: a) improving the functioning of the internal market, including in particular a sound, effective and consistent level of regulation and supervision, b) ensuring the integrity, transparency, efficiency and orderly functioning of financial markets, c) strengthening international supervisory coordination, d) preventing regulatory arbitrage and promoting equal conditions of competition, e) ensuring the taking of investment and other risks are appropriately regulated and supervised, and f) enhancing customer protection.

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64. Created pursuant to Commission Decision 2009/78/EC. **65.** Created pursuant to Commission Decision 2009/79/EC. **66.** Created pursuant to Commission Decision 2009/77/EC.

In the exercise of their tasks, they shall pay particular attention to any systemic risk[67] posed by financial institutions, the failure or poor functioning of which may impair the operation of the financial system or the real economy.

The ESAs were created on 1 January 2011[68] and will each comprise: a Board of Supervisors, a Management Board, a Chairperson, an Executive Director and a Board of Appeal.

The respective regulations set out in detail the functions and competences of the ESAs. These include most notably the following: a) to contribute to the establishment of high-quality common regulatory and supervisory standards and practices, in particular by providing opinions to the Union institutions; b) to develop guidelines, recommendations, and draft regulatory and implementing technical standards; c) to contribute to the consistent application of legally binding Union acts, in particular by contributing to a common supervisory culture; d) to monitor and assess market developments in their areas of competence, including where appropriate trends in credit, in particular, to households and SMEs; and e) to foster depositor and investor protection.

Regarding tasks related to consumer protection, they shall promote transparency, simplicity and fairness in the market for consumer financial products or services across the internal market, particularly by: a) collecting, analysing and reporting on consumer trends; b) reviewing and coordinating financial literacy and education initiatives by the competent authorities; c) developing training standards for the industry; and d) contributing to the development of common disclosure rules.

ESAs may adopt guidelines and recommendations addressed to competent authorities or financial market participants with a view to promoting the safety and soundness of markets and convergence of regulatory practice, and may establish consistent, effective and efficient supervisory policies. They may temporarily prohibit or restrict certain financial activities that threaten the orderly functioning and integrity of financial markets or the stability of the whole or part of the Union's financial system.

Regarding emergency action, in the case of adverse developments which may seriously jeopardise the orderly functioning and integrity of financial markets or the stability of the whole or part of the financial system in the Union, ESAs shall actively facilitate and coordinate any actions undertaken by the national competent supervisory authorities of Member States. In certain conditions, ESAs may urge the competent authorities to take the measures needed to deal with the situation. If they do not take those measures, the ESAs may adopt decisions addressed to the financial institutions directly subject under Union law, including the cessation of any financial practice when necessary to urgently remedy the situation.

EUROPEAN SYSTEMIC RISK BOARD (ERSB)

The ERSB[69] will ensure the supervision of the Union's financial system, assuming responsibility for the macro-prudential oversight of the financial system within the Union in order to prevent or mitigate systemic risks and avoid periods of widespread financial distress.

The ESRB shall have a General Board, a Steering Committee, a Secretariat, an Advisory Scientific Committee and an Advisory Technical Committee. The ESRB's tasks will include the following: a) determining and/or collecting and analysing all the relevant and necessary infor-

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67. Systemic risk means a risk of disruption in the financial system with the potential to have serious negative consequences for the internal market and the real economy. All types of financial intermediaries, markets and infrastructure may be potentially systemically important to some degree. **68.** The headquarters of the European Banking Authority will be in London, those of the European Securities and Markets Authority in Paris and those of the European Insurance and Occupational Pensions Authority in Frankfurt am Main. **69.** The ESRC's headquarters will be in Frankfurt am Mein.

mation for achieving its objectives; b) identifying and prioritising systemic risks; c) issuing warnings where such systemic risks are deemed to be significant and, where appropriate, making those warnings public; d) issuing recommendations for remedial action in response to the risks identified and, where appropriate, making those recommendations public; and g) cooperating closely with all the other parties to the ESFS and, in particular, providing the ESAs with the information on systemic risks required for the performance of their tasks.

When significant risks in the financial system are identified, the ESRB shall provide warnings and, where appropriate, issue recommendations for remedial action , including, where appropriate, for legislative initiatives. These warnings or recommendations may be of either a general or a specific nature and shall be addressed in particular to the Union as a whole or to one or more Member States, or to one or more of the ESAs, or to one or more of the national supervisory authorities.

The ESRB, in close cooperation with the other parties to the ESFS, shall elaborate a colour-coded system corresponding to situations of different risk levels, so as to classify them by seriousness.

The ECB shall carry out the functions of the ESRB Secretariat, providing analytical, statistical, logistical and administrative support to the ESRB. Among others, the Secretariat's tasks are as follows: the collection and processing of information, including statistical information, determined by the ESRB; the preparation of the analyses necessary to carry out the tasks of the ESRB; and making available to the ESAs the risk information required by them to carry out their tasks.

The regulations came into force on 16 December 2010 (general application from 1 January 2011) and Directive 2010/78/EU came into force on 4 January 2011.

Amendment of European legislation on public offerings and on the admission of securities to trading

The Union adopted *Directive 2010/73/EU of the European Parliament and of the Council of 24 November 2010* (OJ L of 11 December 2010) amending Directives 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.

The changes to Directive 2003/71/EC are as follows. The threshold amount of securities included in an offering above which the Directive is applicable is raised from €2.5 million to €5 million, offerings for lower amounts being outside its scope of application. Similarly, the threshold total amount of the offering of non-equity securities issued in a continuous or repeated manner by credit institutions above which the Directive is applicable is raised from €50 million to €75 million.

The threshold above which it is required to publish a prospectus in an offer of securities addressed to individual investors is raised to an acquisition of €100,000 per investor (previously the threshold was €50,000).

For the purposes of private placement of securities, the definition of "qualified investors" is broadened to include existing professional clients considered as such in accordance with Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments.

The prospectus shall contain information concerning the issuer and the securities to be offered to the public, along with a summary that concisely provides key information in the language in which the prospectus was originally drawn up. However, where the prospectus relates to the admission to trading on a regulated market of non-equity securities having a denomination of at least €100,000 (previously €50,000), there shall be no requirement to provide a summary.

Where securities are guaranteed by a Member State, an issuer, an offeror or a person asking for admission to trading on a regulated market shall be entitled to omit information about such guarantor when drawing up the prospectus.

The changes to Directive 2004/109/EC are as follows. The exemptions from its scope of application continue to include issuers that issue solely debt securities admitted to trading on a regulated market, but the threshold denomination per unit is raised from €50,000 to €100,000; also exempt are issuers of debt securities denominated in a currency other than euro where the value of such denomination per unit is, at the date of the issue, equivalent to at least €100,000 (previously €50,000). However, temporarily, the previous amounts remain in force for those debt securities which had already been admitted to trading on a regulated market in the Union before 31 December 2010.

Where only holders of debt securities whose denomination per unit amounts to at least €100,000 (previously €50,000) or, in the case of debt securities denominated in a currency other than euro whose denomination per unit is, at the date of the issue, equivalent to at least €100,000 (previously €50,000), are to be invited to a meeting, the issuer may choose as venue any Member State, provided that all the facilities and information necessary to enable such holders to exercise their rights are made available in that Member State. Likewise, the previous amounts temporarily remain in force for those debt securities which had already been admitted to trading on a regulated market in the Union before 31 December 2010, for as long as such debt securities are outstanding.

The Directive came into force on 31 December 2010 and the Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 1 July 2012.

Community directive on capital requirements for the trading book and for resecuritisations, and the supervisory review of remuneration policies

The Union adopted *Directive 2010/76/EU of the European Parliament and of the Council of 24 November 2010* (OJ L of 14 December 2010) amending Directives 2006/48/EC[70] and 2006/49/EC[71] as regards capital requirements for the trading book and for resecuritisations, and the supervisory review of remuneration policies.

SUPERVISORY REVIEW OF REMUNERATION POLICIES

In order to address the potentially detrimental effect of poorly designed remuneration structures on the sound management of risk and control of risk-taking behaviour by individuals, the requirements of Directive 2006/48/EC to have in place systems, strategies, procedures and mechanisms for effective risk management were reviewed and supplemented by an express obligation for credit institutions and investment firms (hereafter "institutions") to establish and maintain, for categories of staff whose professional activities have a material impact on their risk profile, remuneration policies and practices that are consistent with effective risk management.

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70. Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions. **71.** Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions.

Those categories of staff should include at least senior management, risk takers, staff engaged in control functions and any employee whose total remuneration, including discretionary pension benefit provisions, takes them into the same remuneration bracket as senior management and risk takers.

Having regard to the principle of proportionality, remuneration policies and practices should be applied to all aspects of remuneration including salaries, discretionary pension benefits[72] and any similar benefits.

In application of said principle of proportionality, only institutions that are significant in terms of their size, internal organisation and the nature, the scope and the complexity of their activities are required to establish a *remuneration committee* as an integral part of their governance structure and organisation.

The assessment of the performance-based components of remuneration should be based on longer-term performance and take into account the outstanding risks associated with the performance. The assessment of performance should be set in a multi-year framework of at least three to five years, in order to ensure that the assessment process is based on longer term performance and that the actual payment of performance-based components of remuneration is spread over the institutions' business cycle.

A substantial portion of the variable remuneration component, such as 40% to 60%, should be deferred over an appropriate period of time. Moreover, a substantial portion of the variable remuneration component must consist of shares or other share-linked instruments, subject to the legal structure of the institution concerned or, in the case of a non-listed institution, other equivalent non-cash instruments and, where appropriate, other long-dated financial instruments that adequately reflect the credit quality of the institution.

Institutions must ensure that the total variable remuneration does not limit their ability to strengthen their capital base. If this occurs, Member States' competent authorities are empowered to limit variable remuneration, inter alia, as a percentage of total net revenue. Also, the authorities are empowered to impose, whenever the situation so requires, qualitative or quantitative measures on the relevant institutions that are designed to address problems that have been identified in relation to their remuneration policies. Qualitative measures available to the competent authorities include requiring the institutions to reduce the risk inherent in their activities, products or systems, including by introducing changes to their structures of remuneration or freezing the variable parts of remuneration. Quantitative measures include a requirement to hold additional own funds. In the event of non-compliance, the competent authorities shall have the power to impose or apply financial and non-financial penalties or other measures. Those penalties or measures shall be effective, proportionate and dissuasive.

Lastly, institutions should disclose detailed information on their remuneration policies, practices and, for reasons of confidentiality, aggregated amounts for those members of staff whose professional activities have a material impact on the risk profile of the credit institution or investment firm. That information should be made available to all stakeholders (shareholders, employees and the general public).

TRADING PORTFOLIO AND RESECURITISATION

The provisions on prudent valuation in Directive 2006/49/EC are extended to all instruments measured at fair value, whether in the trading book or non-trading book of institutions. Where the

72. "Discretionary pension benefits" means enhanced pension benefits granted on a discretionary basis by a credit institution to an employee as part of that employee's variable remuneration package, which do not include accrued benefits granted to an employee under the terms of the company pension scheme.

application of prudent valuation would lead to a lower carrying value than actually recognised in the accounting, the absolute value of the difference has to be deducted from own funds.

The standards for internal models to calculate market risk capital requirements are strengthened. Similarly, the use of internal models to calculate securitisation risks in the trading book has had limits placed on it and a standardised capital charge for securitisation positions in the trading book is now required by default.

The Directive extends for a further year, i.e. until 31 December 2011, the transitional floors being applied to credit institutions which calculate risk-weighted exposures by the Internal Ratings Based Approach (the IRB Approach) or Advanced Measurement Approaches.

Specific risk charges for securitisation positions have to be aligned with the capital requirements in the banking book since the latter provide for a more differentiated and risk-sensitive treatment of securitisation positions.

In the field of securitisation, disclosure requirements of institutions have been considerably strengthened. Institutions must particularly take into account the risks of securitisation positions in the trading book.

The term "resecuritisation" is introduced. It means a securitisation where the risk associated with an underlying pool of exposures is tranched and at least one of the underlying exposures is a securitisation position. Credit institutions investing in resecuritisations are required to exercise due diligence also with regard to the underlying securitisations and the non-securitisation exposures ultimately underlying the former.

Credit institutions must assess whether exposures in the context of asset-backed commercial paper programmes constitute resecuritisation exposures, including those in the context of programmes which acquire senior tranches of separate pools of whole loans where none of those loans is a securitisation or resecuritisation exposure, and where the first-loss protection for each investment is provided by the seller of the loans.

Institutions are permitted to choose whether to apply a capital requirement to or deduct from own funds those securitisation positions that receive a 1,250% risk weight, irrespective of whether the positions are in the trading or the non-trading book.

The powers granted to the Commission are broadened so that it can carry out the appropriate technical adjustments to the two directives to ensure uniform application thereof and to take account of developments on financial markets.

The Directive came into force on 15 December 2010.

Changes in the rules for preparing consolidated annual accounts and in the chart of accounts

Royal Decree 1159/2010 of 17 September 2010 (BOE of 24 September 2010) repealed Royal Decree 1815/1991 of 20 December 1991, laid down rules for preparing consolidated annual accounts and altered the Spanish general chart of accounts (*Plan General de Contabilidad* or "PGC" by its Spanish abbreviation) approved by Royal Decree 1514/2007 of 16 November 2007[73] and the general chart of accounts for small and medium-sized enterprises approved by Royal Decree 1515/2007 of 16 November 2007.[74]

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73. See "Financial Regulation: 2007 Q4", Economic Bulletin, January 2008, Banco de España, pp. 196-198. **74.** See "Financial Regulation: 2007 Q4", Economic Bulletin, January 2008, Banco de España, pp. 198 and 199.

The purpose of the Royal Decree is to transpose to Spanish law Commission Regulations 494/2009 and 495/2009 of 3 June 2009 amending Regulation 1126/2008 of 3 November 2008 adopting certain international accounting standards in accordance with Regulation 1606/2002 of the European Parliament and of the Council as regards, respectively, International Accounting Standard 27 (Consolidated and Separate Financial Statements) and International Financial Reporting Standard 3 (Business Combinations).

The new rules for the preparation of consolidated financial statements are structured, as previously, in six sections: i) parties to consolidation, ii) obligation to prepare consolidated financial statements, consolidation methods and equity method, iii) full consolidation method, iv) proportionate consolidation method and equity method, v) other rules applicable to consolidation, and vi) rules for preparing consolidated financial statements.

It should be noted that the consolidation rules regulate the criteria used to account for elimination of investment and equity by reference to the *acquisition method* set forth in the PGC, with such adaptations and clarifications as are needed for consolidated entities.

The acquisition method regulated in Recording and Valuation Rule 19 "Business Combinations" of the PGC[75] is the keystone of consolidation, since it sets the general criteria for including the assets and liabilities of subsidiaries in the consolidated accounts on the date that control is obtained. Once the criteria for recognising and measuring the financial statement items of the group companies have been unified, the acquisition method requires those items to be aggregated and subsequently eliminated from the standpoint of the group as the reporting entity, and not as a mere prolongation of the individual financial statements of the controlling company.

The Royal Decree came into force on 25 September 2010 and is to be applied in preparing the consolidated financial statements for the first accounting period starting on or after 1 January 2010. If the entities include comparative information from the previous accounting period adapted to the new criteria, the date of first-time application would be that of the previous year, i.e. 1 January 2009.

State budget for 2011

Following the usual practice in December, *Law 39/2010 of 22 December 2010* (BOE of 23 December 2010) on the State budget for 2011 was promulgated. Notable from the standpoint of financial regulation were the following.

GOVERNMENT DEBT

The government is authorised to increase the outstanding State debt in 2011, subject to the condition that it shall not exceed the level at the beginning of the year by more than €43,626 million (the limit for last year's budget was €78,136 million). This limit may be exceeded during the course of the year with prior authorisation of the Ministry of Economic Affairs and Finance, and those cases in which it shall be automatically revised are laid down.

In relation to State government guarantees, mention should be made of the authorisation of government guarantees to back fixed-income securities issued by securitisation special purpose vehicles, aimed at improving the financing of corporate productive activity, for which an amount of €3 billion (the same as in the previous budget) has been established.

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75. The PGC continues to set the acquisition method as the only possible alternative for accounting for business combinations. The PGC explains how to identify the acquirer in accordance with IAS 27. The equity of the acquirer will continue to be recorded at the same carrying amount, unlike that of the acquiree, which must generally be recorded at fair value.

TAXES

With regard to personal income tax, the individual and household minimums and the employment income deduction remain unchanged. The tax rates applicable to incomes above €120,000 and €175,000 are raised moderately from 43% to 44% and from 43% to 45%, respectively.

The taxation of multi-year compensation was also changed, a limit of €300,000 being introduced on the amount of gross income to which the 40% rebate will be applied.[76]

The rebate for birth or adoption of children (set at €2,500) was struck down and the tax credit for house purchase or rental changed. Thus, with effect from 1 January 2011 the personal income tax credit for investment in principal residence will only apply to taxpayers whose taxable income is less than €24,107.20 per year, although it remains in place temporarily for purchasers who bought their house before that date. The tax credit for rental of principal residence was also changed to put it on an equal footing with that for house purchase. In addition, the reduction in the net income from renting out residential real estate is raised from 50% to 60%. This reduction will be 100% when the tenant is between 18 and 30 years of age (previously between 18 and 35 years of age).

The rebates to compensate for the loss of tax benefits affecting certain taxpayers under the current personal income tax law, regulated by Law 35/2006 of 28 November 2006, remain in place. The first establishes for 2010 a tax credit for purchase of principal residence for taxpayers who purchased their principal residence before 20 January 2006. The amount is equal to the difference between the tax credit resulting from application of the previous personal income tax legislation (Legislative Royal Decree 3/2004 of 5 March 2004),[77] in force until end-2006, and that under Law 35/2006.[78]

The second rebate will affect those receiving in 2010 certain income from capital arising over a period exceeding two years. On one hand, income from capital obtained from transfer to third persons of capital from financial instruments entered into prior to 20 January 2006 shall qualify for a reduction of 40%, as it did under the previous personal income tax law. On the other, income received in the form of deferred capital arising from life and disability insurance policies taken out prior to 20 January 2006 shall qualify for a 40% or 75% reduction, as envisaged under the previous personal income tax law.

For transfers of real estate not used in business activities, the updated acquisition cost adjustment coefficient of 1% remains in place.

Another change affects open-end investment companies. Specifically, a tax rate equal to that on savings income (between 19% and 21%) will be levied on revenue derived from share capital reductions with refund of shareholders' contributions[79] and on distributions of share

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76. Previously a 40% rebate was generally applied to gross income arising over a period of more than two years not obtained on a periodic or recurring basis and to that legally deemed to have been obtained manifestly irregularly over time. **77.** See "Financial Regulation: 2004 Q1", Economic Bulletin, April 2004, Banco de España, pp. 99 and 100. **78.** During 2010 a tax credit may be taken, in general, for 15% of the amounts paid for the purchase or renovation of the principal residence, with a maximum of €9,015.18 per annum. In 2006, although the same tax credit was available, in general, when the purchase was made using borrowed funds, in the two years following the purchase the tax credit was for 25% of the first €4,507.59 and for 15% of the remainder up to €9,015.18. Subsequently, these percentages were 20% and 15%, respectively. **79.** In this case a limit is set, which is the larger of the following amounts: a) the increase in the net asset value of the shares from their acquisition or subscription date to the date of the capital reduction, and b) when the capital reduction is carried out using undistributed earnings, the amount of those earnings. In this respect, capital reductions, whatever their purpose, are deemed to affect first the portion of the share capital originating from undistributed earnings, until it is cancelled. The excess over this limit shall reduce the acquisition cost of the shares involved until they are cancelled. In turn, any resulting excess shall be included as investment income from share holdings in any type of firm, as stipulated for the distribution of share premiums.

premiums to shareholders (this measure is applied in an equivalent manner in corporate income tax).

In corporate income tax, the main new measure is intended to allow SMEs to continue under the applicable special regime for the three years immediately following that in which they exceed the threshold of €8 million of turnover.[80] This measure is extended to firms that exceed the threshold as a result of a corporate restructuring, provided that all the firms involved meet the aforesaid condition. Furthermore, capital increases in 2011 and 2012 by firms eligible under this measure are exempt from transfer tax under the "corporate transactions" heading.

Also, Spanish legislation is adapted to Community law in respect of the financial goodwill deduction, which will cease to apply for purchases of securities representing holdings in the own funds of entities resident in another Union Member State made from 21 December 2007.

The tax on the income of non-residents is modified to adapt Spanish legislation to Union law. To do this, the percentage of holding required for exemption of dividends distributed by subsidiaries resident in Spain to parents resident in the European Union or to their permanent establishments is made equal to the percentage of holding required under the corporate income tax law in respect of the application of the 100% tax credit to avoid double domestic taxation of dividend payments.

Other financial measures relate to the legal interest rate and the late-payment interest rate, which are unchanged at 4% and 5%, respectively.

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80. This amount has risen to €10 million under Royal Decree-Law 13/2010 of 3 December 2010 on fiscal, labour and deregulatory actions to foster investment and job creation. This legislation has also improved the tax thresholds of that special regime. Thus the tax rate is 25% on the portion of taxable income between €0 and €300,000 (previously that rate applied to the portion between €0 and €120,202.41). The rate on the rest of taxable income is 30%.