# FINANCIAL REGULATION: 2012 Q1

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## Introduction

In 2012 Q1 numerous financial provisions were published.

With respect to monetary policy, the Banco de España made a number of temporary changes to the collateral eligibility requirements for its operations.

In relation to credit institutions, various provisions were published to institute a number of measures: 1) to clean up balance sheets affected by the impairment of real estate-related assets; 2) to modify the public and confidential financial reporting rules, and financial statement formats, and in particular to reflect the provisioning requirements for real estate-related loans; 3) to revise the rules relating to notification to the Banco de España of transactions between residents and non-residents, in accordance with the latest legislation, and 4) to give a new wording to certain financial provisions in relation to the powers of the European supervision authorities.

In the EU sphere, changes were made to the legal regime for the accounting and financial reporting of the European System of Central Banks and to the reporting requirements in relation to external statistics.

As usual in this period, in the field of the securities market, the terms of issuance of State debt were published for 2012 and January 2013.

Finally, the government published various royal decree-laws: the labour market reform; certain measures to protect mortgage debtors who have no resources; certain tax and administrative provisions designed to reduce the budget deficit; an extraordinary mechanism to finance the payment of suppliers of local governments and, where applicable, regional governments; and the adaptation to European law in relation to the reporting and documentation obligations for mergers and spin-offs of share capital companies.

## Banco de España: temporary changes to the collateral eligibility requirements for monetary policy operations

*The Resolution of 15 February 2012 of the Executive Commission of the Banco de España* (BOE of 17 February 2012) on temporary changes to the collateral eligibility requirements for monetary policy operations of the Banco de España was published.

In accordance with the decisions of the Governing Council of the European Central Bank (ECB) of 9 February 2012,[1] the Banco de España has temporarily widened the collateral eligibility requirements laid down in the "General clauses applicable to monetary policy operations", approved by the Resolution of the Executive Commission of the Banco de España of 11 December 1998.

Thus, performing non-mortgage credit claims vis-à-vis non-financial corporations and public-sector bodies, denominated in euro or some other main currency, whose estimated credit risk, as assessed by the Banco de España on the basis of reliable sources, involves

1 Adopted in accordance with the Decision of the ECB of 14 December 2011 on additional temporary measures relating to Eurosystem refinancing operations and eligibility of collateral.

a probability of default of 0.4% or less within a one-year time horizon are eligible collateral for monetary policy operations.

At a later date, the above-mentioned credit claims that fulfil the following conditions may also be eligible collateral: 1) the estimated credit risk, as assessed by the Banco de España on the basis of reliable sources, involves a probability of default of 1% or less within a one-year time horizon, and/or 2) they are not subject to Spanish law (in this latter case, provided the relevant legal analysis has been performed). Where applicable, the decision to accept these loans will be published on the Banco de España's website.

The resolution entered into force on 17 February 2012.

**Balance sheet clean-up of the financial sector**

*Royal Decree-Law 2/2012 of 3 February 2012* (BOE of 4 February 2012) on balance sheet clean-up of the financial sector was published. This legislation seeks to achieve three objectives: 1) to clean up the balance sheets of credit institutions, which have been adversely affected by the impairment of their real estate-related assets; 2) to create incentives for an appropriate and efficient adjustment of excess capacity, and 3) to strengthen the governance of the institutions resulting from integration processes. By these means, it is sought to restore confidence in the Spanish financial system and to bring about a recovery in lending.

The following is a brief summary of the most relevant provisions of this Royal Decree-Law.

MEASURES TO CLEAN UP CREDIT INSTITUTIONS' BALANCE SHEETS

With regard to the business in Spain of credit institutions, new provisions and additional capital requirements have been established to cover the impairment of loans and of assets foreclosed or received in payment of debts relating to development land and to real estate construction or development (hereinafter, special assets) existing at the end of 2011. This is a specific and extraordinary write-down of a specific portfolio of assets and, therefore, does not affect new loans for real estate development granted since 31 December 2011, unless these are to refinance existing loans.

New provisions

For the special assets classified as standard exposures, a one-off general provision equal to 7% of their outstanding amount as at 31 December 2011 will be set aside. The amount of this provision may only be used by institutions to create the specific provisions that may be necessary as a consequence of subsequent reclassification as doubtful or substandard assets of any such loans or of the foreclosure or receipt of assets in payment of such debts.

To determine the impairment of special assets classified other than as standard exposures, the estimation rules in Annex I of the Royal Decree-Law will be applicable.

The Royal Decree-Law establishes provisioning requirements for all loans and foreclosed assets classified other than as standard exposure existing as at 31 December 2011, which may in no case be less than the following percentages:

| | Classified as | |
|---|---|---|
| | Doubtful | Substandard |
| Development land | 60% | 60% |
| Real estate construction and development: | | |
| In progress but halted | 50% | 50% |
| In progress and ongoing | 50% | 24% |
| Completed all types of assets | 25% | 20% |

Unsecured loans for real estate construction and development classified as substandard will have a provision of at least 24%.

The Royal Decree-Law increases the provisions for real estate assets acquired in payment of debts consisting of completed real estate construction or developments, as well as houses arising from loans to households that have not been the borrowers' principal residence, that exist as at 31 December 2011, to a minimum of 25% of the outstanding exposure, or on the basis of the time elapsed up to that date, in accordance with the following percentages:

| Period since acquisition | % |
|---|---|
| Over 12 months and up to 24 | 30 |
| Over 24 months and up to 36 | 40 |
| Over 36 months | 50 |

The Royal Decree-Law also establishes a minimum provision, irrespective of the time on the balance sheet, of 60% for development land, and of 50% for real estate construction or developments in progress.

Additional capital requirements

According to the previous legislation (Royal Decree-Law 2/2011 of 18 February 2011 on strengthening the financial system), credit institutions had to have, in general, core capital[2] equal to at least 8%[3] of total risk-weighted exposure.[4] Now, in addition, they must have an additional surplus equal to the amount that results from the calculations envisaged in Annex II of Royal Decree-Law 2/2012 in relation to special assets. Specifically, this surplus must be equivalent to the sum of the amounts resulting from the calculations detailed below:

1 The financing of land (classified as doubtful or substandard): 80% of the amount of the outstanding exposure.

2 The financing of developments in progress (classified as doubtful or substandard): 65% of the amount of the outstanding exposure.

3 Assets received in payment of debts: 80% of the book value if they are land, and 65% of the book value if they are developments in progress.

In all cases, the provisions already set aside for these assets will be deducted from the resulting amounts.

These provisioning and capital requirements must be complied with before 31 December 2012, except in the case of those institutions that carry out integration processes, as men-

2 Core capital, equivalent to "common equity tier 1" in Basel III with certain differences, is made up basically of the following elements: 1) share capital, excluding non-voting redeemable shares and own shares; 2) paid-in share premium; 3) disclosed reserves, as well as those elements classified as reserves in accordance with the legislation on the own funds of credit institutions and the retained earnings for the period; 4) holdings representing minority interests that correspond to ordinary shares of consolidable group companies; 5) the eligible instruments subscribed for by the FROB within the framework of its regulations, and 6) temporarily, instruments that are mandatorily convertible into shares before 31 December 2014 that comply with certain requirements that guarantee a high loss-absorbing capacity and that do not represent more than 25% of core capital. From the above sum will be deducted, inter alia, losses from previous years, current year losses and intangible assets.

3 This requirement is 10% for those institutions that do not have securities representing at least 20% of their capital held by third parties and that also have a wholesale funding ratio of over 20%.

4 Calculated in accordance with the provisions of Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting obligations of financial intermediaries and of its implementing legislation.

tioned below. Also, before 31 March they must submit to the Banco de España a plan setting out the measures that they plan to adopt for such compliance.

INTEGRATION PROCESSES

Credit institutions that carry out integration processes during 2012 will have 12 months from authorisation of the integration operation to comply with the requirements mentioned above. Integration processes initiated on or since 1 September 2011 may also be subject to these rules. In both cases, they must comply with certain conditions, including the following:

1 The integration of the institutions participating in the operation must generate an initial total balance sheet that is at least 20% larger than the total balance sheet of the business in Spain of the largest of the participating institutions. Upon a proposal from the Banco de España this condition may be waived, when this figure is not achieved, depending on the circumstances of operations of a similar size, although in no event shall the increase be less than 10% of the above-mentioned balance sheet.

2 The integration process must be carried out through operations that involve structural modifications in accordance with current legislation, or operations to acquire institutions in which the FROB has a majority shareholding. These rules will not apply to integration processes based exclusively on contractual links, unless the only participants are credit cooperatives.

3 The participating institutions must adopt measures designed to improve corporate governance and must present a remuneration plan for managers and directors.[5]

4 The integration project must include a quantified objective for the increase in credit to households and small and medium-sized enterprises during the three years following the integration, as well as a plan for disposing of real estate-related assets during the three years following the integration.

The general meetings of shareholders or general assemblies of the integrating institutions must vote in favour of the integration resolution before 30 September 2012. In all cases the integration must be completed before 1 January 2013.

Applications must be presented in the Treasury no later than 31 May 2012, although they will not be required for operations involving the takeover of institutions in which the FROB has a majority holding.

REMUNERATION POLICY AT CREDIT INSTITUTIONS WHICH RECEIVE PUBLIC FINANCIAL SUPPORT FOR THEIR REORGANISATION OR RESTRUCTURING

The directors and managers of credit institutions which are majority-owned by the FROB shall not receive variable remuneration or discretionary pension benefits during 2012.

The variable remuneration of directors and managers of institutions, which are not majority-owned by the FROB but are recipients of the latter's financial support, corresponding to the years during which public financial support is given, will be deferred for three years. This variable remuneration shall be conditional upon results being posted that warrant its

5 In general, they will be in line with the provisions of the Unified Corporate Governance Code for listed companies, and in particular must comply with the provisions of Article 13 of Royal Decree-Law 9/2009 of 26 June 2009 on bank restructuring and strengthening of the capital of credit institutions.

payment and shall be subject to compliance with a plan submitted previously to obtain the above-mentioned support. The Banco de España shall determine whether these conditions are met.

Institutions which are going to request financial support from the FROB for their reorganisation or restructuring, as a prerequisite for obtaining such aid, must include in the contracts regulating their relationship with their directors and managers the minimum content determined by the Minister of Economic Affairs and Competitiveness, which shall include the following rules, among others:

1 Limitations on remuneration according to the various situations mentioned below:

Institutions which are majority-owned by the FROB: the maximum amount of fixed remuneration for all salary items[6] of executive chairmen, managing directors and managers amounts to €300,000 per year. The maximum amount of the total remuneration of other members of collegiate management bodies shall be €50,000 per year.

Institutions which are not majority-owned by the FROB but are recipients of its financial support: the maximum amounts for the posts and items indicated in the previous paragraph shall be €600,000 and €100,000 per year, respectively.

For the purposes of calculating these limits, all the remuneration earned within the group to which the credit institution belongs shall be taken into account.

These limitations shall also apply to institutions which, when this Royal Decree-Law came into force, were already investees of the FROB or had received support from it.

2 Limitations on variable remuneration, expressed as a percentage of fixed remuneration, taking into account the average applied to similar employee categories at institutions comparable in terms of size and complexity, pursuant to the rules established for the above-mentioned credit institutions which are not majority-owned by the FROB, but have received financial support from it:

The limitations may be lifted once the institution has been restructured, through the payment, redemption or disposal of the securities subscribed by the FROB, or when it is considered that the financial support provided has been repaid to the FROB in any other way.

REFORMS OF THE FUND FOR THE ORDERLY RESTRUCTURING OF THE BANKING SECTOR (FROB)

Royal Decree-Law 9/2009 of 26 June 2009 on bank restructuring and strengthening of the capital of credit institutions was amended in order to introduce certain reforms in the FROB.

The deadline for divestment by the FROB of the securities representing capital acquired from the issuer institutions through their disposal via the competitive procedures estab-

6 This shall include per diems earned for membership of the Board of Directors or bodies reporting to the latter.

lished in the above-mentioned regulation is reduced from five to three years. The foregoing is within the performance of its functions to strengthen the capital of credit institutions (Article 9 of Royal Decree-Law 9/2009 of 26 June 2009).

The possibility has been eliminated of the FROB divesting, within one or two years, the securities representing capital acquired from the issuer institutions in favour of third-party investors proposed by the institution benefiting from the FROB's actions.

The instruments which the FROB can acquire within the framework of the measures to support the integration processes of credit institutions are extended (Article 10 of Royal Decree-Law 9/2009 of 26 June 2009) to include instruments which can be converted into shares, compared with the previous situation, in which they were restricted to preference shares. Accordingly, the requirement that issuer institutions agree to the elimination of the preferential subscription right of shareholders or holders of non-voting equity units when the decision to increase capital is adopted or their waiver of this right is extended to the other convertible securities acquired by the FROB.

It is specifically provided that the securities issued and acquired by the FROB are eligible as Tier 1 capital and as core capital without any need for them to be listed on an organised secondary market. For these purposes, the restrictions established by law in relation to the eligibility of capital and core capital shall not be applicable to them.

Finally, the provision assigned to the FROB and charged to the State Budget was increased by €6 billion.

AMENDMENTS TO THE LEGAL REGIME OF SAVINGS BANKS WHICH PERFORM THEIR FINANCIAL ACTIVITY THROUGH A COMMERCIAL BANK

Certain amendments are introduced in Royal Decree-Law 11/2010 of 9 July 2010 on governing bodies and other aspects of the legal regime of savings banks in relation to the regime created for those savings banks which indirectly pursue their financial activity through a commercial bank.

For instance, their organisational structure is simplified by limiting the governing bodies to the General Assembly and the Board of Directors and the existence of the Control Committee is now optional. Similarly, the number of members of the governing bodies and the frequency of their sessions shall be determined by the bylaws of the savings banks in accordance with their economic size and activity.

Also, a limit is set for the distribution of surpluses obtained by savings banks, so that they may not earmark more than 10% of their freely distributable surplus to expenses other than those of welfare projects. However, the Banco de España may authorise higher percentages, if necessary, to meet essential operating expenses of the institutions. Provisions are also introduced to simplify the functioning, frequency and form of calling General Assembly meetings.

They are specifically exempt from complying with obligations referring to customer service departments[7] which, in any event, shall be fulfilled by the commercial bank through which they perform their activity. Similarly, the Banco de España may, on a bank-by-bank basis,

7 Savings banks, like other credit institutions, must attend to and resolve the complaints and claims which users of financial services may submit, in relation to their legally recognised interests and rights. For these purposes, institutions must have a customer service department responsible for attending to and resolving complaints and claims. Furthermore, such institutions may, either individually or in groups based on branches of activity, geographical proximity, turnover or any other criteria, appoint an ombudsman.

adapt compliance with organisational requirements on internal control, audit and risk management or offer exemption from such compliance.

TRANSFORMATION OF SAVINGS BANKS INTO "SPECIAL FOUNDATIONS"

A new arrangement is introduced whereby savings banks may lose their status of credit institutions and be transformed into "special foundations". In accordance with Royal Decree-Law 11/2010 of 9 July 2010, amended by Royal Decree-Law 20/2011 of 30 December 2011, this situation would arise when the savings bank no longer exercised control in the commercial bank in the terms envisaged in Article 42 of the Commercial Code.[8] Now, furthermore, they lose such status when the savings bank reduces its holding so that it does not have 25% of the commercial bank's voting rights, although it maintains a position of control.

These arrangements also apply to savings banks which, in concert, engage solely in their activity as credit institutions through a commercial bank controlled jointly by all of them, forming an institutional protection scheme (IPS). Thus, the loss of control or reduction of the joint holding to below the above-mentioned limit will give rise to the loss, for all of them, of their status of credit institution and their transformation into "special foundations".

Lastly, certain specific legal provisions are established in relation to country-wide "special foundations". Specifically, the State shall be responsible for the supervision and monitoring of "special foundations", whose main scope of action goes beyond a single autonomous community, through the Ministry of Economic Affairs and Competitiveness. Similarly, they shall have legal personality from the registration of their public deed of formation in the corresponding special Register created for this purpose at the Ministry of Economic Affairs and Competitiveness.

OTHER CHANGES

The requirements are modified slightly for instruments mandatorily convertible into ordinary shares, as envisaged in Transitional Provision Three of Royal Decree-Law 2/2011, in relation to their inclusion in core capital. The essential change is that the timeframe for mandatory conversion into ordinary shares is extended from 2014 to 2018; furthermore, the share exchange ratio is not fixed from the outset, provided that the maximum nominal amount that must be delivered has been predetermined.

Finally, provision is made for the smoother management of financial collateral provided by financial institutions to the Banco de España, the ECB or other national central banks (NCBs) of the European Union and, consequently, the Sixth Additional Provision of Law 13/1994 of 1 June 1994 of Autonomy of the Banco de España is amended. Thus, in order to grant the collateral, a statement in writing, or in a legally equivalent form, or a unilateral declaration by the guarantor shall suffice. Also, in order to demonstrate that the asset subject to the collateral has been provided, a statement in writing, or in a legally equivalent form, will suffice without the need for it to be registered in the corresponding register by the institution entrusted with it. For these purposes, a record or note sent by electronic

8 According to Article 42 of the Spanish Commercial Code, control shall be presumed to exist when a company, denoted the parent, has any of the following relationships with another one, denoted the subsidiary: 1) the parent holds a majority of the voting rights in the subsidiary; 2) the parent has the power to appoint or remove a majority of the members of the board of directors of the subsidiary; 3) through agreements with third parties, the parent can exercise a majority of the voting rights in the subsidiary; and 4) the parent has, with its votes, appointed most of the members of the board of directors of the subsidiary in office at the time the consolidated accounts have to be prepared and during the two immediately preceding accounting periods. In particular, this will be presumed to be so if the majority of the members of the subsidiary's board of directors are members of the board of directors or senior managers of the parent or another company controlled by the parent.

means or via any durable media shall be deemed to be a legally equivalent form to a statement in writing.

Where necessary, the collateral may be realised through any of the procedures recognised by the legal system in force, whereas previously it was realised through the corresponding market authority. In the other instances, it continues to be realised through an auction organised by the Banco de España.

The Royal Decree-Law came into force on 4 February 2012.

**Credit institutions: amendment of the public and confidential financial reporting rules**

*CBE 2/2012 of 29 February 2012* (BOE of 6 March 2012) (corrigendum, BOE of 14 March 2012) amending CBE 4/2004 of 22 December 2004[9] on public and confidential financial reporting rules and formats was published. Its purpose is to adapt it to the requirements laid down in Royal Decree-Law 2/2012 of 3 February 2012 on balance sheet clean-up of the financial sector.[10]

For this purpose, a new Section V is introduced into Annex IX of CBE 4/2004, which practically reproduces the new provisioning requirements for real estate sector-related loans (hereinafter, special assets) introduced by Royal Decree-Law 2/2012.[11]

The sole exception is contained in Section 1 of Annex I of the Royal Decree-Law, whereby real-estate assets foreclosed or received in payment of debt by credit institutions, which have been on their balance sheet for more than 36 months, must be covered by provisions of at least 40%. This requirement is incorporated into the general treatment in Section IV of the aforementioned Annex IX, so as not to limit it to the assets of that nature existing as at 31 December 2011.

The composition of the types of risk into which operations included in the normal risk category must be classified is modified so that special assets are included in the category "medium-high risk", even when they are secured.

Finally, the confidential statements are updated, with the addition of some new ones and the introduction of certain changes into the special way in which mortgage transactions are recorded in the accounts so as to include the information arising from special assets.

The Circular entered into force on 7 March.

**Regime for cross-border transactions: updating of the regulations**

*CBE 1/2012 of 29 February 2012* (BOE of 6 March 2012) on rules for the notification of cross-border financial transactions was published, which replaces CBE 15/1992 of 22 July 1992 on notification to the Banco de España of transactions between residents and non-residents, and CBE 1/1994 of 25 February 1994 on the accounts in Spain of non-residents, and transactions with banknotes and bills. Its purpose is to adapt the rules on notification to the Banco de España of such transactions by registered institutions to the new regime for the reporting of cross-border financial transactions established by Royal Decree 1360/2011 of 7 October 2011, which amends Royal Decree 1816/1991 of 20 December 1991 on cross-border financial transactions, and Order EHA/2670/2011 of 7 October

9 See "Financial regulation: 2004 Q4", *Economic bulletin,* January 2005, Banco de España, pp. 109-114.

10 See the second section of this article.

11 Specifically, the loans and assets foreclosed or received in payment of debts relating to development land and to real estate construction or development forming part of the business in Spain of credit institutions, which exist as at 31 December 2011 or which arise from the refinancing of the same at a later date.

2011, which amends the Order of 27 December 1991 on the implementation of Royal Decree 1816/1991 of 20 December 1991.

Payment service providers registered with the Banco de España (hereinafter, "registered institutions"),[12] are obliged to notify the Banco de España on a monthly basis, within ten business days of the end of each month, of the following transactions:

1 Cross-border receipts and payments, as well as transfers to and from abroad, denominated in euro or in foreign currency, made on behalf of their customers, when such receipts or payments originate from or are made to accounts held with a payment service provider in another EU Member State or in any other country. Transactions on behalf of other payment service providers are not included.

2 Credits and debits in the accounts of their non-resident customers. Movements in accounts held by other payment service providers will not be included.

3 Shipments and receipts of euro banknotes and coins to/from their foreign correspondents.

In the first two cases, the information that must be supplied includes: identification of the customer; the amount, the currency and the country of origin or destination; the account debited or credited, and other available data, provided that their collection does not affect the automated direct treatment of the payments and can be made automatically. Transactions where the amount is less than €50,000, or such other amount as may be determined by the legislation in force from time to time, are exempt, provided that they do not constitute partial payments.[13]

In the third case, the following data on shipments of banknotes and coins shall be supplied: date of shipment or receipt, dates on which the account is debited or credited, amounts of the banknotes and coins, classified by their denomination, and identification of the foreign correspondent and of the customs or border post through which the shipment is made.

This information must be sent to the Banco de España, by electronic means, in accordance with the formats, conditions and requirements established in the "technical applications" of this Circular.

As for the accounts held with deposit institutions in Spain, registered institutions must identify the holder of the account in euro or foreign currency and must specify whether they are resident in Spain or non-resident. However, they will modify the status of the accounts concerned when they have evidence that there have been changes in the resident or non-resident status in Spain of the customers who hold them. The obligation for registered institutions to request account holders to confirm their non-resident status every two years has been removed.

Registered institutions which, prior to the entry into force of CBE 1/2012, expected to take place on 1 June 2012, are obliged to supply the information required by CBE 15/1992 of

12 Payment institutions are also included now.

13 There were no exemptions under the previous regulations, only the obligation to report transactions individually, in the event that their amount was higher than €3,000, or to report their net amount, if the individual amounts were below this level, provided that they were not partial payments.

22 July 1992 and by CBE 1/1994 of 25 February 1994, must continue to report it for the periods up to 31 December 2013 (the date on which these circulars are repealed), as well as complying with the new obligations laid down in CBE 1/2012.

**Powers of the European Supervisory Authorities: amendment of certain financial legislation**

*Royal Decree-Law 10/2012 of 23 March 2012* (BOE of 24 March 2012) amending certain financial legislation in relation to the powers of the European Supervisory Authorities[14] was published. Its purpose is to adapt national supervisory arrangements to the new European supervisory framework so that Spain acts in coordination with the new European Supervisory Authorities, as well as with other Member States.

The most important changes are as follows.

In general, this Royal Decree-Law introduces the obligation for the Spanish supervisory authorities of the different financial institutions (Banco de España, CNMV and Directorate General of Insurance and Pension Funds) to cooperate with their European counterparts (European Banking Authority, European Securities and Markets Authority, and European Insurance and Occupational Pensions Authority, respectively), as well as with the European Systemic Risk Board. Furthermore, they shall provide these authorities with all the information that they need in order to perform their functions as conferred under European regulations.

BANKING SYSTEM

In the area of credit institutions, Spanish regulations recognise certain powers of the European Banking Authority and the European Systemic Risk Board, which include, most notably, the following:

1 When the Banco de España must take a decision regarding an application for authorisation to use internal credit ratings or internal operational risk measurement methods submitted by a parent credit institution of the European Union and its subsidiaries or, jointly by the subsidiaries of a parent financial holding company, it will promote joint decision-taking in respect of the application with the other supervisory authorities responsible for the supervision of the various entities which are part of the group. In the absence of a joint decision, if any of the competent authorities involved had sent the matter to the European Banking Authority, the Banco de España shall postpone its judgment and shall await the decision that the European Banking Authority may adopt. Subsequently, it will decide in accordance with the European Banking Authority's decision.

2 If the Banco de España enters into bilateral agreements to delegate its responsibility for supervision of a subsidiary to the competent authorities which have authorised said subsidiary and they are supervising the parent, it must inform the European Banking Authority of the existence and the content of such agreements.

3 The Banco de España must also warn, as soon as possible, the European Banking Authority and the European Systemic Risk Board (in addition to the Ministry of Economic Affairs and Competitiveness, and the other supervisory authorities affected) of emergency situations which arise, in particular in those

14 This Royal Decree-Law transposes into Spanish legislation Directive 2010/78/EU of the European Parliament and of the Council of 24 November 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 European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority).

cases where there are adverse developments in financial markets which may compromise market liquidity and the stability of the financial system.

4 When the Banco de España detects that credit institutions, whose parent is a financial institution domiciled outside the European Union, do not have a system of consolidated supervision similar to that established in Spanish regulations, the system of consolidated supervision envisaged in Spanish regulations will be applicable to these institutions. However, the Banco de España may establish other methods for the consolidated supervision of these groups, which will include the power of the Banco de España to require that a parent financial institution be set up which has its registered office in the European Union. In order to check this equivalence, the Banco de España must take into account the guidelines prepared by the European Banking Authority in this connection. Furthermore, the Banco de España must consult the European Banking Authority before taking a decision.

5 As for the supervisory colleges promoted by the Banco de España to facilitate exercising supervisory functions, it must exchange information with the European Banking Authority, in addition to with the other competent authorities of third countries.

6 If the request to open a branch or the freedom to provide services in other Member States by Spanish credit institutions is denied,[15] the Banco de España must inform the European Banking Authority in addition to the European Commission.

7 In the area of sanctions, if disciplinary proceedings are brought which affect a branch of a credit institution authorised in another Member State of the European Union and involve a serious or very serious infringement, the European Commission as well as the European Banking Authority must be notified.

SECURITIES MARKET

In the area of the securities market, most of the above-mentioned obligations are extended to the CNMV in relation to the European Securities and Markets Authority. Furthermore, the CNMV is required to notify said authority in certain specific cases. These include, most notably, the following: 1) prospectuses previously approved by the CNMV so that they have cross-border validity; 2) irregularities or breach of the obligations of issuers of other Member States, arising from the admission to trading on an official secondary market, even prior to adopting the measures to protect investors; 3) the suspension or, if appropriate, the exclusion from trading of certain financial instruments; preventive measures that it may adopt in relation to issuers or holders of financial instruments which may have committed irregularities or failed to comply with the obligations established by Spanish regulations; 4) the authorisation granted to investment services firms and the information about their related programme of activities; 5) the entering into cooperation agreements with the competent authorities of third countries, and 6) the refusal to cooperate or exchange information with other competent authorities in certain cases envisaged in Spanish regulations.

Finally, all the references made in the regulations to the Committee of European Securities Regulators (CESR) are replaced by the European Securities and Markets Authority (its successor).

15 The refusal may arise because the Banco de España has reasons to question, given the specific project, the suitability of the administrative structures or the financial situation of the credit institution.

PENSION PLANS AND FUNDS

Similarly, the reporting obligations to the European Insurance and Occupational Pensions Authority are extended to the Directorate General of Insurance and Pension Funds.

Specifically, note that in the case of the cross-border activity of occupational pension funds, the Member States where the pension funds perform this activity will be stated in the administrative register. The Directorate General of Insurance and Pension Funds will communicate this information to European Insurance and Occupational Pensions Authority.

It will also be notified of the decisions adopted to prohibit the activities of occupational pension funds, the reasons for which must be stated and communicated to the corresponding fund. Likewise, this Authority will also be notified of requirements for the discontinuation of activity made to unauthorised occupational pension funds and the special monitoring administrative measures comprising the prohibition on admitting new plans into the funds or new members or contributions, and the ban on cross-border activity.

SECURITIES PAYMENT AND SETTLEMENT SYSTEMS

It should be underlined that the Banco de España and the CNMV, plus the European Commission, must notify the European Securities and Markets Authority, at its request, of all the information necessary for it to perform its functions in relation to the securities payment and settlement systems recognised by them. Finally, if an insolvency proceeding is brought against a participant in a securities payment and settlement system, both supervisory bodies will notify the European Systemic Risk Board, the other Member States and the European Securities and Markets Authority.

Lastly, in the case of financial conglomerates, the competent Spanish authorities shall cooperate among themselves, with the Joint Committee of the European Supervisory Authorities and with the rest of the competent authorities in the framework of the additional supervision of entities belonging to these conglomerates. This system for exchanging information may be extended to the European Systemic Risk Board, in addition to the NCBs, the European System of Central Banks (ESCB) and to the ECB.

The Royal Decree-Law came into force on 24 March.

**European System of Central Banks: amendment of the legal framework for accounting and financial reporting**

*Guideline ECB/2011/27 of 21 December 2011* (OJ L of 24 January 2011) amending Guideline ECB/2010/20 of 11 November 2010 on the legal framework for accounting and financial reporting in the ESCB was published.

Given the diversity of monetary policy operations, it needs to be clarified in Annex IV to Guideline ECB/2010/20, "*Composition and valuation rules for the balance sheet*", that certain provisions related to monetary policy operations may differ and may not necessarily be Eurosystem provisions.

From the entry into force of this Guideline, the provisions for credit exposures arising from monetary policy operations which are recorded on the liabilities side of the balance sheet of central banks in the ESCB include provisions recorded in proportion to the ECB's subscribed capital (Eurosystem provisions) and provisions recorded for other monetary policy operations.

The Guideline came into force on 31 December 2011.

**Guideline of the European Central Bank on the statistical reporting requirements in the field of external statistics**

*Guideline ECB/2011/23 of 9 December 2011* (OJ L of 3 March 2012), on the statistical reporting requirements of the ECB in the field of external statistics was published which replaces Guideline ECB/2004/15 of 16 July 2004. As this latter Guideline – which is now repealed – was subject to various changes and as new amendments are currently being introduced, it is appropriate to recast it in one text for the purposes of clarity.

The previous statistics are maintained: balance of payments statistics (monthly and quarterly); international reserves statistics; international investment position statistics, and new monthly statistics on cross-border shipments of euro banknotes are introduced.

The biggest change in the quarterly balance of payments statistics is the more detailed sectoral breakdown required. For direct investment NCBs are required to submit the following sectoral breakdown: deposit-taking corporations except the central bank; general government; financial corporations other than MFIs; and, now non-financial corporations, households and non-profit institutions serving households are added. For the portfolio investment assets and other investment items the breakdown by institutional sector follows the standard components of the IMF comprising: the central bank; deposit-taking corporations except the central bank; money market funds; general government; and now financial corporations other than MFIs and non-financial corporations, households, and non-profit institutions serving households are added.

For the new monthly statistics on cross-border shipments of euro banknotes, the NCBs must provide, from now on, information on the monthly imports and exports of euro banknotes by euro area Member States to countries outside the euro area, as specified in Annex II. A breakdown by denomination is required on a best estimate basis.

Their objective is to estimate holdings of euro banknotes by entities outside the euro area. These statistics are necessary to facilitate decision-making regarding the issuance of euro banknotes in particular with respect to planning euro banknote production, management of stocks and the coordination of the issuance and transfers of euro banknotes between NCBs and the ECB in accordance with their respective competencies. They also contribute to the assessment of monetary and foreign exchange developments and the role of the euro as an investment currency outside the euro area.

The same criteria are maintained as those described in the previous regulations as regards the quality of statistical information. However, the Guideline permits the use of optimum estimates based on sound statistical methodologies for data of insignificant or negligible size for the euro area, or for data that cannot be collected at a reasonable cost provided that the analytical value of the statistics is not compromised.

The deadlines for data transmission have also changed. Thus, the data required for compiling the monthly balance of payments shall be provided to the ECB by the forty-fourth calendar day 44$^{th}$) following the end of the month to which the data relate (previously it was the 30$^{th}$ business day following the end of the month to which they refer).

The data required for the compilation of the quarterly balance of payments and the quarterly international investment position which were provided previously to the ECB in the three months following the end of the quarter to which the data refer, will now be submitted in accordance with the following time frame:

1 By the eighty-fifth (85$^{th}$) calendar day following the end of the quarter to which the data relate, from 2014 to 2016;

2 By the eighty-second (82nd) calendar day following the end of the quarter to which the data relate, in 2017 and 2018;

3 By the eightieth (80th) calendar day following the end of the quarter to which the data relate, from 2019.

The data required for the compilation of the international reserves statistics shall be made available to the ECB by the tenth calendar day following the end of the month to which the data relate (previously it was three weeks).

Lastly, the data required on the cross-border shipments of euro banknotes shall be made available to the ECB by the thirty-fifth (35th) day following the end of the month to which they refer.

The first transmission of data relating to balance of payments, international investment position and international reserves statistics, in accordance with the Guideline, shall take place in June 2014, and the first transmission of data relating to cross-border shipments of euro banknotes shall take place in March 2013.

The Guideline came into force on 1 March 2012.

**State debt: terms of issuance for 2012 and January 2013**

Law 39/2010 on the State Budget for 2011 authorised the Minister for Economic Affairs and Finance to increase State debt in 2011 with the limitation that the outstanding balance thereof at end-2011 should not exceed the balance as at 1 January 2011 by more than €43,626 million. This authorisation of indebtedness can be extended, for the same amount and in the same terms, for 2012 since the previous year's budget has been automatically extended until the new budget is approved.

In line with usual practice as this time of year, *Ministerial Order ECC/41/2012 of 16 January 2012* providing for the creation of State debt during 2012 and January 2013 was published and certain powers were delegated to the General Secretary of the Treasury and Financial Policy (BOE of 17 January 2012) and the *Resolutions of 18 and 23 January 2012 of the GeneralSecretariat of the Treasury and Financial Policy* (BOE of 23 and 27 January 2012), providing for certain issues of Treasury bills and of medium- and long-term government bonds, and the schedule of tenders for 2012 and for January 2013, were published.

Broadly, the existing instruments and issuance techniques remain in place. Thus issuance continues to be through ordinary and special tenders (competitive and non-competitive bids),[16] and by other procedures. In particular, a portion or the full amount of an issue could be transferred at an agreed price to one or several financial institutions which underwrite its placement. Similarly, outright sales or the sale under repos of newly issued securities or expanded existing issues that the Treasury might have in its securities account may be performed.

In competitive tenders, bidders shall state the nominal amount and the interest rate requested by them. The minimum nominal amount continues to be €1,000 and bids above that amount shall be expressed in whole-number multiples thereof and the bids accepted

16 Competitive tenders are those indicating the price, expressed as a percentage of the nominal value, that the bidder is willing to pay for the debt, or the percentage interest rate desired by the bidder; non-competitive tenders are those indicating neither price nor interest rate. Non-competitive bids shall be accepted in full and shall be allotted at the weighted average price or at the price equivalent to the weighted average interest rate.

shall be allotted in each case at the price equivalent to the requested interest rate or at the weighted average interest rate, as applicable on the basis of the result of the tender.[17]

In non-competitive tenders, the minimum nominal amount also remains at €1,000 and bids for higher amounts must be whole-number multiples of this, with the provision that the total nominal amount of the non-competitive bids submitted by a single bidder in each tender may not exceed €1 million, although this limit is raised to €300 million in the case of certain institutions.[18] The bids accepted shall in all cases be allotted at the price equivalent to the weighted average interest rate.

Provision is again made to exclude, for the purpose of calculating weighted average price and interest rate, any competitive bids for Treasury bills and medium- and long-term government bonds not considered to be representative of the market situation, so as not distort the result of the tenders.

Lastly, as in previous years, tenders will be followed by a second round reserved for those financial institutions that have acquired market-maker status which will be conducted in accordance with the regulations governing market makers.

TREASURY BILLS

As in previous years, the Resolution sets out the schedule of tenders to be held in 2012 and January 2013. The schedule states the dates of ordinary tenders and the maturity of Treasury bills, setting the issues and the calls-for-tender simultaneously with the publication of the schedule. However, for reasons of demand or issuance policy, the Treasury may hold additional tenders to those announced.

As in 2011, three-, six-, twelve- and 18-month Treasury bills will be auctioned regularly every month, and the grouping of issues in monthly maturities has been retained to improve their liquidity.[19] The 18-month Treasury bills offered for sale in odd months will have the same maturity as those issued in the previous month, so as to allow a sufficient degree of liquidity from the moment they are issued.

Tenders will continue to be held on the third Tuesday of each month for twelve-month and 18-month bills, and on the following Tuesday for three- and six-month bills. Original maturities may differ from the stated periods by the number of days necessary to allow the grouping of bills in a single monthly maturity, coinciding with the issue date of twelve-month and 18-month bills to make for more convenient reinvestment.

As regards other features, the procedure and allotment of tenders will be the same as in 2011, including the submission of bids in terms of the interest rate quoted on secondary markets, so as to simplify bidding for subscribers. Thus, in competitive tenders bidders will indicate the interest rate desired and the bids which are accepted will be allotted, in

17 The competitive bids accepted are used to calculate the weighted average price of the tender, expressed as a percentage of the nominal value and rounded up to three decimal places. The allotment price is determined as follows: bids made at the minimum price are allotted at that price; bids between the minimum price and the weighted average price are allotted at the bid price; and bids above the weighted average price, along with non-competitive bids, shall pay the weighted average price.

18 The Wage Guarantee Fund, the Commercial Bank Deposit Guarantee Fund, the Social Security Reserve Fund, the Investment Guarantee Fund, Sociedad Estatal de Correos y Telégrafos and Sociedad Estatal de Participaciones Industriales (SEPI), or any other public-sector entity or government-owned firm designated by the Treasury.

19 In shorter-term bill issues (three or six months), the Treasury uses the same classes of securities as it used in the past for longer-term (generally eighteen-month) bills in order to keep the same range of securities on the market but with a higher volume, and thus improve their liquidity

each case, at the price equivalent to the interest rate bid or the weighted average as appropriate, based on the outcome of the auction.

MEDIUM- AND LONG-TERM GOVERNMENT BONDS

The Resolution sets out the schedule of tenders to be held in 2012 and January 2013, indicating the dates of the ordinary tenders and the maturity, setting the issues and the call for bids simultaneously with the publication of the schedule. The issuance criteria and procedures are essentially the same as in 2011. The initial maturities will be three and five years for medium-term bonds, and ten, fifteen and thirty years for long-term bonds. Also, bond classes issued in the past will be re-opened with new tranches in order to ensure their liquidity and meet investor demand in the relevant segments by increasing the average volume of outstanding issues. The new issues will bear the nominal interest rate specified in the related Resolution. Provision is also made for the issuance of medium- and long-term bonds tied to some index.

As in the previous year, tenders will, save exceptions, take place on the first Thursday of each month for medium-term bonds and on the third Thursday for long-term bonds. The procedure and allotment of tenders will be unchanged.

The Ministerial Order came into force on 17 January 2011 and the Resolutions on 19 and 24 January 2011.

**Urgent labour market reform measures**

*Royal Decree-Law 3/2012 of 10 February 2012* (BOE of 11 February 2012 on urgent labour reform measures was enacted.

From the standpoint of financial regulation, the seventh additional provision of Royal Decree-Law 3/2012 complements Royal Decree-Law 2/2012 of 3 February 2012 on clean-up of the financial sector balance sheet in respect of the establishment of a specific remuneration regime applicable to the directors and managers of credit institutions that receive government financial support for balance sheet clean-up and restructuring, as regards limitations on severance payments. Additionally, it sets certain rules on the termination of credit institution directors' or managers' contracts due to the imposition of sanctions and on the suspension of those contracts due to suspension of the directors or managers or certain cases of provisional replacement thereof.

SEVERENCE PAYMENTS FOR TERMINATION OF CONTRACT

Credit institutions majority owned or financially supported by the FROB may in no case make severance payments for contract termination exceeding the lower of the following amounts: a) twice the maximum bases set in Royal Decree-Law 2/2012 of 3 February 2012 on clean-up of the financial sector balance sheet;[20] or b) two years of stipulated fixed remuneration.

Exempted from this ceiling are those directors and managers who joined the institution or group after or at the same time as the FROB took a holding or extended financial support to it. In this case, the Banco de España may, in view of the contractually stipulated conditions and of the results of the balance-sheet clean-up plan, authorise higher amounts than those established in Royal Decree-Law 2/2012, subject always to the limit of two years of the originally stipulated remuneration.

20 The maximum bases are set out in Rules 3 and 4 of Article 5.3.a) of Royal Decree-Law 2/2012 of 3 February 2012 on clean-up of the financial sector balance sheet. Rule 3 sets a maximum fixed remuneration of €300,000 for executive chairpersons, managing directors and managers of credit institutions majority owned by the FROB. Rule 4 stipulates that for credit institutions not majority owned by the FROB but which receive financial support from it, such maximum fixed remuneration shall be €600,000.

TERMINATION OF CONTRACT DUE TO IMPOSITION OF SANCTIONS

The imposition of sanctions for very serious infringements[21] on persons holding the post of director or manager of a credit institution under an employment contract, including the labour relationships of a special nature of senior managers, shall, for the purposes of labour legislation, be considered to be a serious breach of duty, which shall be cause for disciplinary dismissal and may give rise to termination of the contract. Also, the imposition of such sanctions shall be deemed to be due cause for extinguishment or termination of contracts other than employment contracts.

In these cases, the persons referred to above shall not be entitled to compensation of any amount or in any form, regardless of the legal provision, individual or collective employment contract or agreement, or civil or commercial contract or agreement in which payment of compensation is envisaged.

SUSPENSION OF CONTRACT DUE TO IMPOSITION OF SANCTIONS

The suspension of contract of persons holding the post of director or manager of a credit institution may take place for the following reasons: 1) the persons holding the post of director or manager of a credit institution are found to be presumably responsible for very serious infringements and provisionally suspended from their duties, and 2) there is serious non-compliance with the implementation schedule or the specific measures envisaged in the action plan,[22] and the Banco de España decides to replace provisionally the board or management of the credit institution.

The suspension of contract shall entail mutual exoneration from the obligations to work or provide services and to remunerate such work or provision of services.

The Royal Decree came into force on 12 February 2012.

**Urgent measures to protect mortgagors without funds**

*Royal Decree-Law 6/2012 of 9 March 2012* (BOE of 10 March 2012) on urgent measures to protect mortgagors without funds was enacted. Its purpose is to establish measures to foster the restructuring of the mortgage debt of persons suffering extraordinary difficulty in meeting payments, and to set in place mechanisms to make mortgage foreclosure procedures more flexible.

MEASURES TO FOSTER THE RESTRUCTURING OF MORTGAGE DEBT

The protection model designed is based on a code of good practices for the viable restructuring of mortgage debts on the principle residence, which is supplemented by tax measures.

Code of good practices

The code of good practices ("the Code") set out in the annex to Royal Decree-Law 6/2012 (see summary in Table 1) may be voluntarily followed by credit institutions and others whose professional activities include the granting of mortgage loans. Compliance by them will be supervised by a control committee consisting of representatives of the Ministry of Economic Affairs and Competitiveness, the Banco de España, the CNMV and the Spanish Mortgage Association.

It shall be applied to debtors within the exclusion threshold who hold loans for the purchase of houses the purchase price of which does not exceed certain levels[23] applicable at the date of its entry into force.

21 See Article 12.1 of Law 26/1988 of 29 July 1988 on credit institution discipline and intervention.

22 Provided in Articles 6 and 7 of Royal Decree-Law 9/2009 of 26 of June 2009 on bank restructuring and strengthening of the capital of credit institutions.

23 The values are as follows: 1) municipalities of more than 1,000,000 inhabitants: €200,000; 2) municipalities of between 500,001 and 1,000,000 inhabitants or forming part of the metropolitan areas of municipalities of more than 1,000,000 inhabitants: €180,000; 3) municipalities of between 100,001 and 500,000 inhabitants: €150,000; and 4) municipalities of up to 100,000 inhabitants: €120,000.

SUMMARY OF THE "CODE OF GOOD PRACTICES FOR THE VIABLE RESTRUCTURING OF MORTGAGE DEBTS ON THE PRINCIPLE RESIDENCE" TABLE 1

| | |
|---|---|
| **1. Measures prior to mortgage foreclosure: mortgage debt restructuring** | |
| Scope | Debtors within the exclusion threshold may request and obtain from the creditor institution the restructuring of their mortgage debt so as to make it viable in the medium and long term. |
| Characteristics of the restructuring plan: | The institution must notify and offer to the debtor a restructuring plan providing for the implementation and overall financial consequences of application of the following measures: |
| | — Four-year principal repayment grace period. |
| | — Lengthening of repayment term to a total of 40 years from the loan origination date. |
| | — Reduction of the applicable interest rate to Euribor + 0.25% during the grace period. |
| | — Also, institutions may consolidate the mortgagor's debts. |
| **2. Supplementary measures for cases in which the restructuring plan is inviable** | |
| Scope | To be applied when the restructuring plan is inviable. An inviable plan is deemed to be one in which the monthly mortgage instalment exceeds 60% of the combined income of all members of the household unit. |
| Partial acquittance whereby outstanding principal is reduced: | In this case the debtor may request a partial acquittance whereby the outstanding principal is reduced. The institution has the power to accept or reject it within one month. |
| | To determine the partial acquittance, the institution shall use one of the following calculation methods and, in any event, notify the result to the debtor, regardless of whether or not the institution decides to grant the partial acquittance: |
| | — Reduction of 25%. |
| | — Reduction equal to the difference between the principal repaid and the proportional part of the total loan principal defined by the ratio of the number of instalments paid by the debtor to the total number of instalments due. |
| | — Reduction equal to the difference between the present value of the house and the value which results from subtracting from the initial appraisal vaue twice the difference from the loan. |
| **3. Measures to replace mortgage foreclosure: dation of principal residence in payment** | |
| Scope | Uses when neither the restructuring plan nor the supplementary measures, if any, are viable. |
| Effect of dation in payment: | In these cases, the institution is obliged to accept delivery of the mortgaged asset by the debtor either to the institution or to such third party as it may designate, and, as a result, the debt shall be definitively settled (both that secured by the mortgage and any personal liability of the debtor and of third parties to the insitution as a consequence thereof). |
| | The debtor, if he so requests when he applies for the dation in payment, may remain in the house as a tenant, paying an annual rent of 3% of the total amount of the debt at the date of dation in payment. During this time, past-due rent shall incur late-payment interest of 20%. |
| | Institutions may agree with debtors on the assignment of a portion of the gain arising on the sale of the house, as consideration for any cooperation of the debtor in that disposal. |
| | This measure shall be be applicable if a foreclosure procedure is under way in which an auction has been announced of if the house is subject to subsequent liens. |

SOURCES: Boletín Oficial del Estado (Spanish Official State Gazette) and Banco de España.

For the purposes of the Royal Decree-Law, the debtors under a loan secured by a mortgage on their principle residence are deemed to be within the exclusion threshold if all the following circumstances apply to them: 1) all members of the household unit[24] lack income from employment or from economic activities; 2) the mortgage instalment exceeds 60% of the total net income received by all members of the household unit; 3) the members of the household unit lack any other assets or proprietary rights sufficient to satisfy the debt; 4) the loan in question is secured by a mortgage on the only house owned by the debtor and was granted for the purchase of that house; 5) the loan is not backed by any other collateral or guarantee, or, should there be a guarantee, with all the guarantors are in circumstances 2) and 3) above; and 6) if there are co-debtors not in the household unit, they are in circumstances 1), 2) and 3) above.

The Code includes three phases of action. The first, designed to enable the viable restructuring of the mortgage debt through submission to the requesting debtor of a plan setting out

24 A household unit comprises the debtor, the debtor's not legally separated spouse or registered partner and any children of whatever age who live in the dwelling.

measures (such as a principal repayment grace period, temporary reduction of the interest rate or lengthening of the total repayment period) to assist in repayment of the debt. The second phase is envisaged for cases in which the restructuring plan is not viable. In this situation, the institutions may optionally offer debtors a partial acquittance of debt. And the third, intended for when neither of the first two measures is able to reduce debtors' mortgage obligations to a financially viable level, provides that the debtors may request, and the institutions must accept, dation in payment as the definitive means of releasing the debtor from his debt. In this case, households may remain in their house for two years paying a bearable rent.

From the time a credit institution agrees to adhere to the Code, either of the parties (institution or debtor) may compel the other to execute a public deed of novation of contract resulting from application of the provisions in the Code. The cost of that deed execution shall be borne by the party that requests it.

The parties adhering to the Code shall send quarterly to the Banco de España certain information including, inter alia, the number, volume and characteristics of the transactions requested, executed and denied in application of the Code and the complaints processed, if any, for non-compliance with the Code by credit institutions. Lastly, they shall ensure that the Code is made known as widely as possible, particularly among customers.

Regardless of whether the Code is applied, the penalty interest applicable to all mortgage loans is made more moderate from the time the debtor accredits to the institution that he is within the exclusion threshold. It shall be, at a maximum, the result of adding to the interest under the loan a rate of 2.5% on the outstanding loan principal.

Tax measures

The consolidated text of the Transfer Tax and Stamp Tax Law enacted by Legislative Royal Decree 1/1993 of 24 September 1993 was amended to make the public deeds of mortgage loan novation pursuant to this Royal Decree-Law exempt from the progressive stamp tax on notarial deeds.

The consolidated text of the Law Regulating Local Government Finances enacted by Legislative Royal Decree 2/2004 of 5 March 2004 was amended so that, in the transfers made for the dation in payment envisaged in the Code of Good Practices, the party responsible for paying in the tax charge is deemed to be the institution acquiring the building, and that institution may not demand from the taxpayer the amount of the tax obligations paid.

Law 35/2006 of 28 November 2006 relating to personal income tax and partially amending the laws on corporate income tax, on non-resident income tax and on wealth tax so that any capital gain of debtors arising from the dation in payment of their house is exempt from personal income tax.

The notarial and registration fees derived from settlement of mortgage rights in rem in cases of dation in payment of a mortgage debtor within the exclusion threshold of this Royal Decree Law shall be paid in the proportion of 50%.

The debtor shall not bear any additional cost of the financial institution that acquires, free of mortgage lien, the ownership of the asset previously subject to mortgage.

MECHANISMS FOR MAKING MORTGAGE FORECLOSURE PROCEDURES MORE FLEXIBLE

The Royal Decree-Law introduces basically two mechanisms to enhance the flexibility of procedures for foreclosing on the debtor's principle residence, including the collective one subject to the Code. The first mechanism tends to simplify the out-of-court foreclosure

procedure, and the second extends the aid to tenants under the Housing and Refurbishment Plan 2009-2011 to the persons subject to a court decision of eviction as a result of mortgage foreclosure processes.

Out-of-court foreclosure procedure

The procedure for out-of-court mortgage foreclosure[25] on a debtor's principle residence has been changed. The law provided that, inter alia, this procedure must have been agreed on by the parties when they entered into the mortgage. Another of its features is that mortgage foreclosure takes place before a notary public (the main difference from court-mandated mortgage foreclosure).

The new features now introduced are that foreclosure on an asset takes place through a single auction[26] with a reserve price equal to 70% of the foreclosure value specified in the mortgage deed. If bids are received for an amount equal to or greater than 70% of the value at which the asset would have been auctioned, the asset will be awarded to the highest bidder. If the bids are below that percentage, the debtor has a period of ten days to find a third party offering at least that amount or a lower amount sufficient to satisfy in full the forecloser's claim. Otherwise, the creditor may request that the property be foreclosed for 60% of the appraisal value. If the creditor does not exercise this right, the property will be foreclosed to the highest bidder, provided that the amount offered exceeds 50% of the appraisal value or, if less, covers at least the total amount claimed.

If there are no bidders in the auction, the creditor may, within a period of 20 days, request foreclosure for an amount equal to or greater than 60% of the appraisal value.[27]

The Government shall, within six months from the entry into force of the Royal Decree-Law, enact regulations to simplify the out-of-court sale procedure. Such regulations shall provide for, among other measures, electronic auctions.

Availability of rental housing to persons evicted and those subject to mortgage foreclosure flexibility measures

The persons subject to a court decision of eviction from their principal residence as a result of court or out-of-court mortgage foreclosure proceedings may, after 1 January 2012, benefit from the aid to tenants on the terms set in Royal Decree 2066/2008 of 12 December 2008 regulating the State Housing and Renovation Plan 2009-2012.[28]

Aid is also available to applicants who enter into rental contracts as a result of application of the dation in payment (*dación en pago*) envisaged in the Code of Good Practices when their household income does not exceed 2.5 times the Multipurpose Public Indicator of Income (*Indicador Público de Renta de Efectos Múltiples*) defined in Royal Decree 2066/2008.

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25 The out-of-court foreclosure procedure is set out in Articles 234 to 236 of the Decree of 14 February 1947 enacting the Mortgage Regulation.

26 Previously there was a maximum of three auctions: in the first auction the minimum foreclosure value (reserve price) was that specified in the mortgage deed; if the auction was declared void, the second auction was held with a reserve price equal to 75% of that of the first; if the second auction also failed to attract bids, a third auction was held without a reserve price. In any of those auctions, the creditor was empowered to request that the asset be foreclosed at the value specified in the mortgage deed.

27 The amount at which the creditor may request foreclosure was raised by Royal Decree-Law 8/2011 of 1 July 2011 from 50% to 60% of the property's appraisal value.

28 The requirements are set out in Articles 38 and 39 of that Royal Decree. Thus, the conditions applying to beneficiaries include the requirement that their household income does not exceed 2.5 times the IPREM. The aid may not be granted if, for example, the applicant owns another dwelling or is a partner or equity holder of the legal person acting as landlord. The amount of the aid shall consist of a subsidy whose annual maximum shall be 40% of the annual rent to be paid and subject to a limit of €3,200 per dwelling, regardless of the number of rental contract holders. The maximum duration of this subsidy shall be two years, provided there is no change in the circumstances that gave rise to the initial recognition of entitlement to aid. This subsidy may not be obtained again until at least five years have elapsed from the date of said recognition.

In particular, the rental contracts entered into as a result of application of the Code shall be deemed to be house rental contracts and subject to Law 29/1994 of 24 November 1994 on urban tenancy, with certain special features. Thus, the term of these rental contracts shall be two years, without renewal rights unless there is a written agreement between the parties. The rent during the two-year period shall be set in conformity with Code.

At the end of the two-year contract period, if the tenant does not vacate the house, the landlord may initiate the eviction procedure. That procedure shall include claiming at the market rate any unpaid rent for the months in which the house was improperly occupied.

OTHER DEVELOPMENTS

Amendments were made to Royal Decree-Law 11/2010 of 9 July on governing bodies and other aspects of the legal regime of savings banks. Thus, regarding the transformation of savings banks into special foundations, Royal Decree-Law 2/2012 of 3 February on clean-up of the financial sector balance sheet stipulated that it falls to the Spanish State to supervise and control special foundations whose primary area of operations extends beyond an autonomous region, through the oversight to be exercised by the Ministry of Economic Affairs and Competitiveness. Now it is specified that in cases of segregation, the special foundation's area of operations shall be deemed to be that of the bank resulting from the segregation.

The Royal Decree-Law came into force on 11 March 2012.

**Tax and administrative measures to reduce the government deficit**

*Royal Decree-Law 12/2012 of 30 March 2012* (BOE del 31) introduced diverse tax and administrative measures to reduce the government deficit. These measures supplement those contained in Royal Decree-Law 20/2011 of 30 December 2011 on urgent budgetary, tax and financial measures to correct the budget deficit.

The most notable measures from the standpoint of financial regulation are as follows.

MEASURES RELATING TO THE FINANCIAL SYSTEM

Given the special features of the activity of the *Instituto de Crédito Oficial* (due to the high proportion of financing to SMEs and to the self-employed through government-funded credit facilities), it was decided to set – for the purpose of determination and control of its minimum own funds – a risk weight of 20% for exposures to financial institutions of EU Member States, regardless of their original or residual maturity.

TAX MEASURES

The bulk of the measures are in the area of corporate income tax, governed by Legislative Royal Decree 4/2004 of 5 March 2004. Specifically, the following changes have been made for the tax periods of 2012 and 2013:

1 The maximum annual limit on goodwill deductibility is reduced from 5% to 1% for both corporate acquisitions and business restructurings.

2 The maximum annual limit on the deductibility of the difference between the acquisition cost of the acquirer's holding and the own funds of the transferor that has not been attributed to acquired assets and rights is reduced from 5% to 1%.

3 The upper limit on tax credits to encourage certain activities is reduced from 35% to 25% of gross tax payable, less tax credits to prevent domestic and international double taxation and rebates. This limit also includes the tax credit for reinvestment of extraordinary income.

4 A floor is set on partial payments for taxpayers whose net turnover in the previous twelve months is €20 million or more. In these cases, such payments may not be less than 8% of the net income per the period income statement for the first 3, 9 or 11 months of each calendar year, less any tax losses not yet offset by the taxpayer.

The following corporate income tax measures are instituted indefinitely:

1 Financial expenses arising from debts to group companies are deemed to be non-deductible regardless of residence and of the obligation to prepare consolidated financial statements if those debts are for the acquisition from other group companies of holdings in the capital or own funds of any firm, or for the making of contributions to the capital or own funds of other group companies, unless the taxpayer provides evidence of valid economic reasons for such transactions.

2 The overall limit on the deduction of net financial expenses is set at 30% of operating profit for the year.[29] However, any undeducted net financial expenses may be deducted in the tax periods ending in the following 18 years, together with those of the current tax period, subject to the aforementioned overall limit. By contrast, if the net financial expenses of the tax period do not reach the overall limit, the difference from that limit will be added to the deduction in the next five tax periods until that difference is exhausted.

3 The rules on exemptions in transfers of holdings in companies not resident in Spain are changed so as to make the exemption dependent on the proportion of the total period of ownership of the holding represented by the time during which the exemption requirements have been complied.[30]

4 Progressive elimination of accelerated depreciation with maintenance of employment (regulated in the eleventh additional provision of the Corporate Income Tax Law), which is extended to personal income tax. Also, taxation is imposed on the income obtained in the subsequent transfer of the asset subject to that accelerated depreciation.

Meanwhile, exclusively for 2012, a special levy (8%) is imposed on dividends and income of foreign origin derived from the transfer of equity securities of companies not resident in Spain. Such income does not carry entitlement to apply the double taxation tax credit.

Finally, special tax reporting is established for certain incomes, such that taxpayers[31] that own assets or rights not corresponding to the income declared under certain taxes may submit an additional return (provided for in this Royal Decree-Law) to regularise their tax situation, provided that they owned those assets or rights prior to the end of the last tax

29 For these purposes, net financial expenses are defined as the excess of financial expenses over revenues derived from the assignment to third parties of proprietary capital accrued in the tax period, excluding certain expenses specified in Article 14 of the Corporate Income Tax Law. The operational beneficiary shall be determined on the basis of the operating profit per the period income statement, after removing certain items such as fixed asset depreciation and adding others such as financial income from interests in equity instruments, subject to certain limitations.

30 These requirements are as follows: 1) the percentage of direct or indirect holding in the capital or own funds of the non-resident entity is at least 5%; 2) the investee was taxed under a foreign tax of the same or similar nature to this tax in the period in which the profit distributed or subject to an equity interest was earned; and 3) the profit distributed or subject to an equity interest arises from the performance of business activities abroad.

31 Be they taxpayers under personal income tax, corporate income tax or non-resident income tax.

period whose reporting deadline expired before the Royal Decree-Law came into force. In this case, they must submit a return or pay in the amount which results from applying a percentage of 10% to its amount or acquisition cost. Compliance shall not carry claimability of penalties, interest or surcharges.

The Royal Decree-Law came into force on 31 March 2012.

**Extraordinary financing mechanisms for payment of local and regional government suppliers**

*Royal Decree-Law 4/2012 of 24 February 2012* (BOE of 25 February 2012) set out information obligations and procedures necessary to establish a financing mechanism for payments to local government suppliers, and *Royal Decree-Law 7/2012 of 9 March 2012* (BOE of 10 March 2012), amended by *Royal Decree-Law 10/2012 of 23 March 2012* (BOE del 24), set up the Fund for Financing Payments to Suppliers.

Royal Decree-Law 4/2012 aims to provide the conditions necessary for local governments to meet their outstanding payment obligations to suppliers stemming from the tendering out of works, supplies or services. For this purpose it sets in place an extraordinary financing mechanism, of which regional governments can also avail themselves.

Royal Decree-Law 7/2012 sets up the *Fondo para la Financiación de los Pagos a Proveedores* (Fund for Financing Payments to Suppliers, hereafter "the Fund") and regulates the terms and conditions of transactions for paying the outstanding obligations of local governments and, where applicable, of the regional governments that have availed themselves of this financing mechanism.

SCOPE

The outstanding payment obligations to suppliers and contractors[32] have to meet the following conditions: 1) they must be due, net and claimable; 2) the related invoice or demand for payment was issued before 1 January 2012 and 3) they relate to works, services or supplies falling within the scope of the consolidated Public Sector Contracts Law enacted by Legislative Royal Decree 3/2011 of 14 November 2011.

Excluded are local government agents' obligations to State general government or any of its constituent bodies or agents, to regional governments or any of their constituent bodies or agents, to other local government agents and to the social security system.

PROVISION OF INFORMATION BY LOCAL GOVERNMENTS

Local governments must, by 15 March, send electronically to the Ministry of Financial Affairs and Public Administration a certified list of all outstanding payment obligations meeting the aforementioned three requirements accompanied by the following information: 1) identification of contractor, which shall include employer or tax identification number, company name and registered office; 2) principal amount of the outstanding payment obligation and any VAT or Canary Islands general indirect tax, not including interest, legal costs or any other ancillary costs; 3) date of recording in the administrative register of the invoice, any supplementary invoice for rectification purposes or equivalent demand for payment prior to 1 January 2012; and 4) evidence of whether the contractor initiated legal proceedings to enforce payment before 1 January 2012.

If partial payments of debts to contractors were agreed with them, the aforementioned certificate shall state the total outstanding amount at the time it was issued. In such cases, the local governments must inform of any maturities occurring up to 31 December 2012.

32 A contractor is defined as the successful tenderer for a contract and also the assignee to whom receivables under the contract have been transferred.

ADJUSTMENT PLAN

The financial controller shall submit to the plenary session of the local government an adjustment plan for approval by 31 March. It must contain, inter alia, the following: 1) sufficient current revenue to finance its current expenses and debt repayments, including the debt entered into within the framework of this Royal Decree-Law; 2) current revenue projections; 3) description and application schedule of the structural reforms to be implemented; and 4) measures for reducing the administrative burden of citizens and firms to be adopted as provided by Resolution of the government's Standing Committee for Economic Affairs. This plan may include, inter alia, changes to the organisation of the local government.

Once approved by the plenary session, the adjustment plan shall be sent electronically to the competent body of the Ministry of Financial Affairs and Public Administration, which will assess it and communicate the assessment to the local government within 30 calendar days from the date the plan was received. That assessment, if not communicated within said time period, shall be deemed to be unfavourable.

EXTRAORDINARY FINANCING MECHANISM

If the assessment is favourable, the adjustment plan shall be deemed to be authorised and the financing mechanism shall be set in motion. The final details of the adjustment plan shall be specified immediately by Resolution of the government's Standing Committee for Economic Affairs. This mechanism may be implemented over time in successive phases which may not extend beyond this year. The criteria for priority in the payment of obligations shall include the following: 1) discount offered on the principal amount of the outstanding payment obligation; 2) legal proceedings to enforce payment of the obligation in question were initiated before 1 January 2012, and 3) age of the outstanding payment obligation. However, in a press release of 8 March 2012, the Ministry of Financial Affairs and Public Administration rectified these criteria to give preference to the payment of the oldest debts. In addition, it ruled out the possibility of compulsory partial acquittance of debt.

To finance their payment obligations, local governments shall enter into a long-term debt-incurrence transaction the financial conditions of which shall be set by the government's Standing Committee for Economic Affairs. This transaction could entail the assignment to the State of the local government's share in State taxes in the amount necessary to meet those payment obligations, provided that it does not affect compliance with other obligations derived from the debt-incurrence transactions envisaged in the adjustment plan.

The generation of a cash deficit for overheads in the period of repayment of the debt-incurrence transaction shall entail the prohibition to make further investments in the following year financed by debt (irrespective of whether those investments are tangible, intangible or financial, direct or indirect through subsidies granted to subsidiaries).

If local governments do not enter into the aforementioned debt-incurrence transaction, of if they enter into it but default on the related payment obligations, the competent body of the Ministry of Financial Affairs and Public Administration or the competent public agent shall make the appropriate withholdings with a charge to the payment orders issued to satisfy its share in State taxes, provided that this does not affect compliance with other obligations derived from the debt-incurrence transactions envisaged in the adjustment plan.

Also, arrangements are set in place to monitor the adjustment plan. In accordance with this monitoring, the local governments entering into debt-incurrence transactions must submit annually to the Ministry of Financial Affairs and Public Administration a report on the execution of adjustment plans. This report will be quarterly in some local governments.

To ensure repayment of the amounts derived from the debt-incurrence transactions entered into, local governments may be subjected to control actions by the National Audit Office.

FUND FOR FINANCING PAYMENTS TO SUPPLIERS

This Fund is a public law entity within the Ministry of Economic Affairs and Competitiveness, to which it is attached through the State Secretariat for Economic Affairs and Business Support, and will be under the stewardship of the Ministry of Financial Affairs and Public Administration Ministry of Financial Affairs and Public Administration, to which it reports operationally.

It has an endowment of €35,000 million charged to the State budget for 2011. It is empowered to raise funds through any type of debt-incurrence transaction in the capital markets, and those transactions will be guaranteed by the State.

The Fund will be administered, managed and directed by a Steering Council consisting of representatives of the State Secretary for the Budget and Expenditure, of the State Secretary for Public Administration, of the State Secretary for Economic Affairs and Business Support and of the State Secretary for the Treasury and Financial Policy. Also forming part of the Steering Council, with the right to speak but not to vote, will be a representative of the Attorney General and a representative of the National Audit Office.

The Steering Council shall have, inter alia, the following functions: 1) to establish management guidelines; 2) to monitor and assess the Fund's activity; 3) to decide on how to use the income obtained; 4) to approve the draft operational and capital budgets; 5) to prepare and approve the annual accounts; and 6) to adopt the relevant resolutions, including the procurement of services from private or public entities, to provide the Fund with the necessary human and physical resources.

The Fund shall enter into credit transactions with local governments and, where appropriate, with the regional governments that avail themselves of the extraordinary financing mechanism to pay their outstanding obligations.

The utilisation of the financing granted to local and regional governments shall be through direct payments to suppliers, the Fund being subrogated to such claims as the suppliers may have on those local and regional governments for the amount effectively paid.

The credit transactions entered into by local government shall be guaranteed by the withholdings envisaged in Royal Decree-Law 4/2012. Should the local government not have entered into the debt-incurrence transaction, the withholding shall be used to offset the financial expenses and costs incurred.

Finally, the debts incurred by the Fund to raise funds shall be subject to the same tax regime as State debt, both for residents and for non-residents.

Royal Decree-Law 4/2012 and Royal Decree-Law 7/2012 came into force on 26 February 2012 and 11 March 2012, respectively.

**Share capital companies: simplification of reporting and documentation requirements in the case of mergers and divisions**

*Royal Decree-Law 9/2012 of 16 March 2012* (BOE of 17 March 2012) on simplification of reporting and documentation requirements in the case of mergers and divisions of share capital companies amended the consolidated text of the Share Capital Companies Law enacted by Legislative Royal Decree 1/2010 of 2 July 2010 and Law 3/2009 of 3 April 2009 on structural changes to companies. Its purpose is to transpose into Spanish law Directive

2009/109/EC of the European Parliament and of the Council of 16 September 2009 amending Council Directives 77/91/EEC, 78/855/EEC and 82/891/EEC, and Directive 2005/56/EC as regards reporting and documentation requirements in the case of mergers and divisions.

The most significant new developments are as follows.

WEBSITE AND ELECTRONIC COMMUNICATIONS

The status of websites and electronic communications is enhanced in order to facilitate the functioning of companies and enable greater cost savings. Having a website is made compulsory for listed companies, while it continues to be optional for other share capital companies.

The resolution to create, change, transfer or remove a website shall be entered in the competent Mercantile Register and published in the Official Gazette of the Mercantile Register (*Boletín Oficial del Registro Mercantil* – BORM). The company shall ensure the security of the website, the authenticity of the documents published, free access to the website and the possibility of downloading and printing its contents.

Communications between the company and equity holders, including remittance of documents and information, may be by electronic means if the equity holder has expressly agreed to it.

CHANGES REGARDING COMPANY MERGERS

If various listed public limited companies whose securities are admitted to trading on an official secondary market or on a regulated market domiciled in the European Union participate in a merger, the merger balance sheet may be replaced by the 6-monthly financial report of each of them, provided that the report relates to a period ended and was made public in the six months preceding the date of the draft terms of merger. The report shall be made available to the shareholders in the same way as that stipulated for the merger balance sheet.

If the merging companies have a website, the directors must include on that website the common draft terms of merger, which shall be published free of charge in the BORM along with the identification of the website where they are located. They shall remain on the website until expiry of the deadline for creditors to exercise their right to oppose the merger. Similarly, the website shall also include the notice of the general meeting which is to decide on the merger or the individual communication of that announcement to equity holders, along with the related documentations stipulated in the previous legislation.[33]

The independent experts' report on the draft terms of merger is substantially shortened in the following cases: 1) if so agreed unanimously by the voting equity holders of all the merging companies, and 2) if the acquiring company owns directly or indirectly all the shares or other equity of the acquired company or companies. In these situations, the report shall be limited to stating an opinion on whether the assets and liabilities contributed by the companies being dissolved is at least equal to the capital of the new company or to the amount of the increase in capital of the acquiring company.

Provision is made for the right of creditors to oppose the merger in respect of the financial claims existing before the draft terms of merger were lodged with the Mercantile Register

33 Including the common draft terms of merger or, where applicable, the directors' reports of each company on the draft terms of merger; the reports of independent experts; the annual accounts and management reports of the last three years; the merger balance sheet of each of the merging companies, etc.

and, now, where applicable, before the date that the draft terms of merger are made available on the companies' respective websites. If the merger took place despite the exercise, in accordance with law, of a legitimate creditor's right to oppose it, without the debtor company submitting collateral or providing a joint and several guarantee in its favour, the creditor may approach the Mercantile Register in which the merger was recorded to demand that a margin note be inserted in the entry made to evidence the exercise of that right. Accordingly, it is permitted that, in the six months following the date of that margin note, proceedings may be initiated before the commercial courts against the acquiring company or against the new company to demand the provision of security for payment of the claim.

CHANGES REGARDING DIVISIONS OF COMPANIES

The main new development is the simplification of the formalities required in the case of a division due to the formation of new companies. Thus it is no longer necessary to submit the directors' report on the draft terms of merger, the independent experts' report or the division balance sheet if the shares or other equity units of each of the new companies are allocated to the equity holders of the company being divided in proportion to their rights in the capital of that company.

VALUATION OF NON-MONETARY CONTRIBUTIONS IN PUBLIC LIMITED COMPANIES

The new legislation raises to three the number of new cases in which it is not necessary to submit an independent experts' report to value the non-monetary contributions in the formation or in capital increases of public limited companies. They are as follows: 1) if, in the formation of a new company by merger or division, an independent experts' report has been prepared on the draft terms of merger or division; 2) if the capital increase is made for the purpose of delivering the new shares or other equity units to the equity holders of the acquired or spun-off company and an independent experts' report has been prepared on the draft terms of merger or division; and 3) if the capital increase is made for the purpose of delivering the new shares to the equity holders of the company targeted by a takeover bid.

Lastly, the Royal Decree-Law makes certain changes to the wording of the rules on equity holders' entitlement to be insulated against the claims of other creditors in cases of cross-border merger and of transferral of registered office abroad.

The Royal Decree-Law came into force on 18 March 2012.

31.3.2012.