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Introduction

A number of new financial provisions were adopted in the second quarter of 2013.

The European Central Bank (ECB) brought in new regulations on: 1) refinancing operations and collateral in monetary policy operations; 2) measures to counter non-compliant reproductions of euro banknotes and on the exchange and withdrawal of euro banknotes; and 3) the Eurosystem's provision of reserve management services in euro to central banks and countries not belonging to the euro area and to international organisations.

New Community legislation was also published on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

In turn, the Banco de España created the Electronic Register, a new instrument for the electronic filing of requests, documents and notices.

Relating to credit institutions, three sets of measures were introduced: 1) the criteria for assessing the suitability of persons managing credit institutions; 2) extension of the period available for hybrid capital and subordinated debt instrument management exercises; and 3) a key change to the form of operation of the Central Credit Register (CCR).

In the securities market, four new regulations were published: 1) the key investor information document and the prospectus for collective investment institutions; 2) the disclosure obligations to customers on the assessment of the suitability and appropriateness of financial instruments; 3) the annual remuneration report formats for directors of listed companies and for members of the board of directors and of the oversight committee of savings banks issuing securities admitted to trading on official securities markets; and 4) annual corporate governance report formats for listed companies, savings banks and other entities issuing securities admitted to trading on official securities markets.

At European Union level, three pieces of financial legislation were enacted: 1) changes to the credit rating agency regulations; 2) update of the prudential requirements relating to risk management at certain financial institutions; and 3) European venture capital fund regulations.

The article concludes with comments on the tax and financial aspects of two new regulations: the first, on measures to strengthen the protection of mortgagors, debt restructuring and rented social housing; and the second, on measures to support entrepreneurs and stimulate growth and job creation.

The contents of this article are set out in Table 1.

European Central Bank: refinancing operations and collateral in monetary policy operations

The following three measures were published in the quarter: Guideline ECB/2013/4 of 20 March 2013 (OJEU of 5 April 2013) on additional temporary measures relating to Eurosystem refinancing operations and eligibility of collateral, amending Guideline ECB/2007/9 of 1 August 2007 on monetary, financial institutions and markets statistics; Decision ECB/2013/6 of 20 March 2013 (OJEU of 5 April 2013) on the rules concerning the use as

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collateral for Eurosystem monetary policy operations of own-use uncovered government-guaranteed bank bonds; and Decision ECB/2013/13 of 2 May 2013 (OJEU of 17 May 2013) on temporary measures relating to the eligibility of marketable debt instruments issued or fully guaranteed by the Republic of Cyprus. Guideline ECB/2013/4 came into force on 22 March 2013 and shall apply until 28 February 2015; Decision ECB/2013/6 came into force on 22 March 2013 and Decision ECB/2013/13 on 9 May 2013.

A large part of Guideline ECB/2013/4 recasts into a single text several earlier Guidelines relating to similar temporary measures, and adds new ones. These measures apply temporarily, until the ECB's Governing Council considers that they are no longer necessary to ensure an appropriate monetary policy transmission mechanism.

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OPTION TO REDUCE THE AMOUNT OF, OR TERMINATE, LONGER-TERM REFINANCING OPERATIONS

The procedure whereby credit institutions that are counterparties to Eurosystem operations (hereinafter, institutions)[1] may reduce the amount of or, where appropriate, terminate certain long-term refinancing operations (such actions being collectively referred to as "early repayment") has been included in Guideline ECB/2013/4. This procedure was included, at the time, in Guideline ECB/2013/2 of 23 January 2013 which amended Guideline ECB/2012/18 of 2 August 2012[2] on additional temporary measures relating to Eurosystem refinancing operations and eligibility of collateral.

Thus, the date from when institutions may exercise the early repayment option shall be published in the corresponding tender announcement or by any other appropriate means. Institutions must notify their national central bank (NCB) of both the amount and the date

1 Counterparty institutions are the euro area credit institutions with which the Eurosystem executes certain monetary policy operations. To be eligible as such, institutions must fulfil the uniform euro area-wide general eligibility criteria, that is, they must: 1) be subject to the Eurosystem's minimum reserve requirements; 2) be financially sound; and 3) meet the operating requirements set by the NCBs and, as appropriate, by the ECB.

2 See "Financial regulation: 2012 Q3", Economic Bulletin, October 2012, Banco de España, pp. 65-69.

of the early repayment at least one week in advance. This notice is binding, so if the institution fails to exercise the option on the date set it may be subject to the financial penalties envisaged in Guideline ECB/2011/14 of 20 September 2011[3] on monetary policy instruments and procedures of the Eurosystem, for infringements relating to tenders, bilateral operations and the use of collateral.

ADMISSION OF CERTAIN ADDITIONAL ASSET-BACKED SECURITIES

Guideline ECB/2013/4 incorporates the additional criteria for admission of asset-backed securities, regulated in Guideline ECB/2012/18. Thus, asset-backed securities which do not fulfil the credit assessment requirements envisaged in Guideline ECB/2011/14 but which have two ratings of at least "triple B" at issuance and at any time subsequently are admissible, provided they satisfy certain additional requirements.[4]

They are also subject to the following valuation haircuts: 16% for asset-backed securities that have at least "single A" credit ratings. Asset-backed securities that do not satisfy this requirement and that are backed by commercial mortgages shall be subject to a valuation haircut of 32%, and all others to a valuation haircut of 26%.

As previously, counterparty institutions cannot submit as collateral securities issued or guaranteed by them or by any other institution with which they have close links.[5]

In turn, NCBs may accept as collateral for Eurosystem monetary policy operations asset-backed securities whose underlying assets include residential mortgages[6] and/or loans to small and medium-sized enterprises (SMEs),[7] provided they have two ratings of at least "triple B" (with no need to fulfil any other kind of requirements). These securities shall be limited to those issued before 20 June 2012 and shall be subject to a valuation haircut of 32%.

ADMISSION OF CERTAIN CREDIT CLAIMS

As established in Guideline ECB/2012/18, credit claims that do not satisfy the Eurosystem eligibility criteria, stipulated in Guideline ECB/2011/14, are admissible. NCBs that decide to accept such credit claims must establish eligibility criteria and risk control measures in accordance with their national law. These criteria and control measures will be subject to the prior approval of the ECB's Governing Council.

In exceptional circumstances, and subject to the approval of the Governing Council, NCBs may accept credit claims governed by the law of any Member State other than that in which the accepting NCB is established.

3 See "Financial regulation: 2011 Q4", Economic Bulletin, January 2012, Banco de España, pp. 113-114.

4 These additional requirements include: 1) the assets backing the asset-backed securities must belong to certain asset classes (residential mortgages, loans to small and medium-sized enterprises, commercial mortgages, auto loans, leasing and consumer finance); 2) they cannot include non-performing, structured, syndicated or leveraged loans; and 3) the transaction documents of the asset-backed securities must include servicing continuity provisions.

5 "Close links" are deemed to exist between a counterparty institution and an issuer/debtor/guarantor of collateral when: 1) the counterparty institution holds directly or indirectly, through one or more companies, 20% or more of the capital of the issuer/debtor/guarantor; 2) the issuer/debtor/guarantor holds directly or indirectly, through one or more companies, 20% or more of the capital of the counterparty institution; or 3) a third party holds more than 20% of the capital of the counterparty institution and more than 20% of the capital of the issuer/debtor/guarantor, directly or indirectly, through one or more companies.

6 Residential mortgages, besides residential real estate mortgage-backed loans, also include guaranteed residential real estate loans (without a real estate mortgage) if the guarantee is payable promptly on default. Such guarantee may be provided in different contractual formats, including insurance contracts, provided that they are granted by a public sector entity or a financial institution subject to public supervision. The credit assessment of the guarantor for the purposes of such guarantees must comply with credit quality step 3 in the Eurosystem's harmonised rating scale over the life of the transaction.

7 SMEs are entities, irrespective of their legal form, engaged in an economic activity where the annual turnover for the entity or, as appropriate, for the consolidated group is less than €50 million.

ACCEPTANCE OF CERTAIN GOVERNMENT-GUARANTEED BANK BONDS

As established in Guideline ECB/2012/18, NCBs may accept bank bonds guaranteed by a Member State that is subject to a European Union/International Monetary Fund programme,[8] or by a Member State whose credit assessment does not meet the Eurosystem's minimum requirement for issuers and guarantors of marketable assets established in Guideline ECB/2011/14.[9]

Institutions may not submit as collateral for Eurosystem monetary policy operations bank bonds issued by themselves or by institutions closely linked to them and guaranteed by a European Economic Area (EEA)[10] public sector entity in excess of the nominal value of such bonds already submitted as collateral on 3 July 2012.

Decision ECB/2013/6 of 20 March 2013 set 1 March 2015 as the latest date for institutions to use guarantees of this kind in their monetary policy operations. In exceptional circumstances, the ECB's Governing Council may grant temporary derogations from this prohibition, for a maximum of three years. Requests for derogations must be accompanied by funding plans in which the requesting institutions indicate how they will phase out their own use of these bank bonds in the three years following the granting of the derogation.

ADMISSION OF CERTAIN ASSETS DENOMINATED IN POUNDS STERLING, YEN OR US DOLLARS AS ELIGIBLE COLLATERAL

Guideline ECB/2013/4 incorporates the content of Guideline ECB/2012/23 of 10 October 2012 which amended Guideline ECB/2012/18 of 2 August 2012 on additional temporary measures relating to Eurosystem refinancing operations and eligibility of collateral. Thus, marketable debt instruments denominated in pounds sterling, yen or US dollars shall constitute eligible collateral for Eurosystem monetary policy operations, provided that: 1) they are issued, held or settled in the euro area; 2) the issuer is established in the European Economic Area (EEA);[11] and 3) they fulfil all the other eligibility criteria contained in Annex I to Guideline ECB/2011/14.

The Eurosystem applies valuation markdowns to these instruments: 16% on collateral denominated in pounds sterling or US dollars and 26% on collateral denominated in yen.

ELIGIBILITY OF MARKETABLE DEBT INSTRUMENTS ISSUED OR FULLY GUARANTEED BY THE REPUBLIC OF CYPRUS

Marketable debt instruments issued or fully guaranteed by the Republic of Cyprus do not meet the Eurosystem's credit quality thresholds applicable to marketable debt instruments as established in Annex I to Guideline ECB/2011/14 of 20 September 2011 on monetary policy instruments and procedures of the Eurosystem.[12] However, taking into consideration the economic and financial adjustment programme for Cyprus reflected in the Memorandum of Understanding concluded between the Republic of Cyprus and the European Commission,[13] the ECB's Governing Council has decided that these marketable debt instruments have a credit quality standard sufficient to warrant their eligibility as collateral for Eurosystem monetary

8 Currently Greece, Ireland and Portugal.

9 The high credit quality requirement for marketable assets is based on certain criteria, such as accepted credit assessment by external credit assessment institutions (ECAIs), which must be equal to or exceed the credit quality threshold, which must comply with credit quality step 3 in the Eurosystem's harmonised rating scale. In the absence of an (acceptable) ECAI credit assessment of the issuer, high credit standards can be established by means of guarantees provided by financially sound guarantors, subject to certain requirements. The financial soundness of a guarantor is assessed on the basis of ECAI credit assessments meeting the Eurosystem's credit quality threshold.

10 The EEA was created on 1 January 1994 following an agreement between European Union (EU) and European Free Trade Area (EFTA) member countries and allowed EFTA member countries to participate in the EU's internal market without having to join the EU. It comprises the 27 EU countries and the following EFTA members: Iceland, Liechtenstein and Norway.

11 See footnote 10 above.

12 See footnote 9 above.

13 For that purpose, it shall be considered a euro area Member State subject to a European Union/International Monetary Fund programme for the purposes of the provisions of Guideline ECB/2013/4 of 20 March 2013, together with Ireland, Greece and Portugal.

policy operations, irrespective of any external credit assessment. They shall, however, be subject to the specific haircuts set out in the Annex to the Decision.

SUSPENSION OF THE CREDIT QUALITY THRESHOLD REQUIREMENTS FOR CERTAIN MARKETABLE INSTRUMENTS

Guideline ECB/2013/4 includes in its articles certain ECB Decisions[14] which establish that the Eurosystem's credit quality thresholds, set out in Guideline ECB/2011/14, shall not apply to marketable debt instruments issued or fully guaranteed by central governments of Member States subject to a European Union/International Monetary Fund programme, unless the Governing Council decides that the respective Member State does not comply with the conditions for financial support and/or the macroeconomic programme.

Lastly, Annex III to Guideline ECB/2007/9 of 1 August 2007 was amended, relating to the calculation of the lump sum allowance to be used by each credit institution to calculate its minimum reserves.[15]

Measures to counter non-compliant reproductions of euro banknotes and on the exchange and withdrawal of euro banknotes

Guideline ECB/2013/11 of 19 April 2013 (OJEU of 30 April 2013) amending Guideline ECB/2003/5 of 20 March 2003 on the enforcement of measures to counter non-compliant reproductions of euro banknotes and on the exchange and withdrawal of euro banknotes was published, with a view to including in its articles the provisions of Decision ECB/2013/10, also of 19 April 2013 (OJEU of 30 April 2013), which made certain technical amendments to Decision ECB/2003/4 of 20 March 2003 on the denominations, specifications, reproduction, exchange and withdrawal of euro banknotes.

The new developments relate mainly to the exchange of damaged euro banknotes. As established in Decision ECB/2003/4, NCBs charge a fee to exchange euro banknotes that have been mutilated or damaged as a result of the use of anti-theft devices. However, that fee, of 10 euro cents per damaged banknote, shall not be charged when the damage results from an attempted or actual robbery or theft.

Decision ECB/2013/10 establishes that NCBs shall pay payment service institutions[16] that hold accounts with them the value of any genuine euro banknotes accidentally damaged by the use of anti-theft devices that are presented for exchange, on the day of receipt of the banknotes. The aim is to support endeavours to enhance the security of the cash cycle and avoid penalising the use of anti-theft devices.

Institutions that present for exchange, in one or more transactions, damaged banknotes with a value of €7,500 or more shall have to present documentation on the origin of the banknotes and identification of the customer or, where applicable, of the owner. This obligation shall also apply if there is any doubt regarding whether or not the threshold of €7,500 has been reached, to prevent the use of the financial system for the purpose of money laundering and terrorist financing.[17]

Both the Guideline and the Decision came into force on 1 May 2013.

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14 Decision ECB/2011/4 of 31 March 2011 on temporary measures relating to the eligibility of marketable debt instruments issued or guaranteed by the Irish government; Decision ECB/2011/10 of 7 July 2011 on temporary measures relating to the eligibility of marketable debt instruments issued or guaranteed by the Portuguese government; and Decision ECB/2012/32 of 19 December 2012 on temporary measures relating to the eligibility of marketable debt instruments issued or fully guaranteed by the Hellenic Republic.

15 Each credit institution deducts a maximum lump sum designed to reduce the administrative cost of managing very small reserve requirements. The maximum lump sum allowance is €100,000.

16 In particular, credit institutions, along with payment service providers and any other institutions engaged in the handling and distribution to the public of notes and coins.

17 In accordance with Directive 2005/60/EC of the European Parliament and of the Council, of 26 October 2005, on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

European Central Bank: Eurosystem reserve management services

Guideline ECB/2013/14 of 15 May 2013 (OJEU of 24 May 2013), amending Guideline ECB/2006/4, of 7 April 2006, on the Eurosystem's provision of reserve management services in euro to central banks and countries located outside the euro area and to international organisations was published.

One of the aims of Guideline ECB/2006/4 was to ensure that Eurosystem reserve management services were provided on a uniform basis, establishing certain minimum common features[18] of contractual arrangements with "customers" (which included countries, central banks or monetary authorities not belonging to the euro area and international organisations to which such services are provided by a Eurosystem member).

Guideline ECB/2013/14 introduces an additional condition, which is that the customer must confirm to the Eurosystem member that it complies with all European Union and national laws on the prevention of money laundering and terrorist financing, insofar as and to the extent applicable to it, including instructions given by competent authorities, and that it is not involved in money laundering or terrorist financing.

The Guideline came into force on 15 May 2013 and shall apply from the sixth week from that date.

New Community legislation on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms

Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 (OJEU of 27 June 2013) on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012[19] on OTC derivatives, central counterparties and trade repositories was published, along with Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 (OJEU of 27 June 2013) on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate, and repealing Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006[20] relating to the taking up and pursuit of the business of credit institutions and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006[21] on the capital adequacy of investment firms and credit institutions.

The Regulation came into force on 28 June and shall apply as from 1 January 2014, with certain exceptions, some of which are noted below, where a different schedule applies. The Directive came into force on 17 July and must be transposed by the Member States before 31 December 2013, with certain exceptions which shall be phased in up to 2019.

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18 Thus, such contractual arrangements had to: a) state that the customer's counterparty was a Eurosystem member and that the contractual arrangement did not per se create customer rights or entitlements vis-à-vis other Eurosystem members (which provision did not prevent a customer from having arrangements with more than one Eurosystem member); b) determine the mechanisms that could be used to settle securities held by customers' counterparties; c) indicate that certain transactions within the framework of Eurosystem reserve management services shall be carried out on a best effort basis; d) state that the Eurosystem member may make suggestions to customers as to the timing and execution of a transaction to avoid conflicts with the Eurosystem's monetary and exchange rate policy, and that such member shall not be liable for any consequences that such suggestions may have for customers; and e) indicate that the fees that Eurosystem members charge to their customers for the provision of these services are subject to review.

19 See "Financial regulation: 2012 Q3", Economic Bulletin, October 2012, Banco de España, pp. 96-100.

20 See "Financial regulation: 2006 Q2", Economic Bulletin, July 2006, Banco de España, pp. 142-144.

21 See "Financial regulation: 2006 Q2", Economic Bulletin, July 2006, Banco de España, pp. 144-146.

These two provisions incorporate into European legislation the liquidity and capital measures adopted by the Basel Committee on Banking Supervision (BCBS), designed to strengthen the solvency of the banking system (Basel III), and represent a new legal framework regulating the taking up and pursuit of the business of credit institutions and investment firms (hereinafter, institutions) and their supervision and prudential risk management, as a first step towards banking union.

Table 2 contains the main new developments relating to own funds items and requirements.

NEW DEVELOPMENTS IN REGULATION (EU) No 575/2013

The Regulation establishes mandatory uniform rules for institutions on: 1) own funds requirements relating to credit risk, market risk, operational risk and settlement risk; 2) requirements limiting large exposures; 3) the liquidity coverage requirement relating to entirely quantifiable, uniform and standardised elements of liquidity risk, once the corresponding delegated act has been implemented by the Commission; 4) the introduction of a leverage ratio; and 5) reporting and public disclosure requirements.

Own funds items

The Regulation revises the concept of own funds and the own funds items required of institutions. Own funds are made up of Tier 1 and Tier 2 capital; in turn, Tier 1 capital is the sum of Common Equity Tier 1 and Additional Tier 1 capital. In other words, Tier 1 capital comprises instruments that are able to absorb losses on a going concern basis, whereas Tier 2 capital instruments will absorb losses essentially when the institution becomes non-viable.

Common Equity Tier 1 capital comprises: 1) capital instruments (shares or other equity instruments) issued and paid up by the institution, provided the conditions established in the Regulation are satisfied; 2) share premium accounts related to the capital instruments; 3) retained earnings and accumulated other income; 4) other reserves and funds for general banking risk where they are available to the credit institution for unrestricted and immediate use to cover risks or losses as soon as these occur; and 5) interim or year-end profits before the institution has taken a formal decision confirming the final profit or loss for the year, although these may be included only with the permission of the competent authority.

The items to be deducted from Common Equity Tier 1 capital include: 1) losses for the current financial year; 2) intangible assets; 3) deferred tax assets that rely on future profitability; 4) amounts resulting from the calculation of expected losses, for institutions calculating risk-weighted exposure amounts using the Internal Ratings Based (IRB) Approach; 5) defined benefit pension fund assets on the balance sheet of the institution; 6) holdings of own Common Equity Tier 1 instruments; 7) reciprocal cross-holdings of Common Equity Tier 1 instruments with other financial sector institutions which, in the view of the competent authority, are designed to artificially inflate the own funds of the institution; 8) the amount of the institution's direct, indirect and synthetic holdings of Common Equity Tier 1 instruments in financial sector institutions, where it has a significant investment in those institutions; 9) the amount of items required to be deducted from the Additional Tier 1 items that exceeds the Additional Tier 1 capital of the institution; and 10) the exposure amount of certain items that qualify for a risk weight of 1,250%, where the institution deducts that exposure amount from the amount of Common Equity Tier 1 items as an alternative to applying a risk weight of 1,250%.

Additional Tier 1 capital comprises certain (hybrid) capital instruments and the related share premium accounts. Among other requirements, to qualify as Additional Tier 1

OWN FUNDS ITEMS

TABLE 2

COMMON EQUITY TIER 1 CAPITAL	
Components	Deductions
Capital instruments issued and paid up	Losses for the current year and expected losses, where applicable
Share premium accounts	Intangible assets
Retained earnings and accumulated other income	Holdings of own Common Equity Tier 1 instruments
Other reserves	Reciprocal cross-holdings of Common Equity Tier 1 instruments with other financial sector institutions
Interim profits	Holdings of Common Equity Tier 1 instruments in other financial sector institutions where there is a significant investment
	Amount of items required to be deducted from Additional Tier 1 items that exceeds Additional Tier 1 capital
ADDITIONAL TIER 1 CAPITAL	
Components	Deductions
Hybrid capital instruments, subject to certain conditions	Holdings of own Additional Tier 1 instruments
Related share premium accounts	Reciprocal cross-holdings of Additional Tier 1 instruments with other financial sector institutions
	Holdings of Additional Tier 1 instruments in other financial sector institutions where there is a significant investment
	Amount of items required to be deducted from Tier 2 items that exceeds Tier 2 capital
TIER 2 CAPITAL	
Components	Deductions
Capital instruments and subordinated loans, subject to certain conditions	Holdings of own Tier 2 instruments
Related share premium accounts	Reciprocal cross-holdings of Tier 2 instruments with other financial sector institutions
Certain credit risk adjustments	Holdings of Tier 2 instruments in other financial sector institutions where there is a significant investment

OWN FUNDS REQUIREMENTS AND CAPITAL BUFFERS

Common Equity Tier 1 capital ratio	4.5% (Common Equity Tier 1 capital / total risk-weighted exposure amounts)
Tier 1 (Common Equity Tier 1 + Additional Tier 1) capital ratio	6% (Tier 1 capital / total risk-weighted exposure amounts)
Total capital ratio	8% (total own funds / total risk-weighted exposure amounts)
Capital conservation buffer	Common Equity Tier 1 capital equal to 2.5% of total risk-weighted exposure amounts
Countercyclical capital buffer	Common Equity Tier 1 capital equal to 0%- 2.5% of total risk-weighted exposure amounts, according to the countercyclical buffer rates that apply in the countries where the credit exposures are located.
Systemic risk buffers	Common Equity Tier 1 capital equal to 1%- 5% of total risk-weighted exposure amounts. A distinction is drawn between global systemically important institutions (G-SIIs) and other systemically important institutions (O-SIIs). Competent authorities may establish institution-specific capital buffers, which in some cases shall be supplementary and in other cases the higher of the two shall apply.

SOURCES: BOE and Banco de España.

capital: 1) the instruments cannot be purchased by the institution, its subsidiaries or companies with which there are control links; 2) they cannot be secured or subject to a guarantee provided by any group company that enhances the seniority of claims in the event of insolvency or liquidation; 3) they must be perpetual and the provisions governing them must include no incentive for the institution to redeem them; 4) where the provisions governing the instruments include one or more call options, those options may be exercised at the sole discretion of the issuer; 5) the instruments may be redeemed or repurchased only when authorised by the competent authority, and not before five years after the date of issuance;[22] 6) the institution shall not indicate explicitly or implicitly that the competent authority would consent to a request to call, redeem or repurchase the instruments; and 7) the provisions governing the instruments require that, if a trigger event[23] occurs, the principal amount of the instruments be written down on a permanent or temporary basis or the instruments be converted to Common Equity Tier 1 instruments.

The items to be deducted from Additional Tier 1 capital include: 1) direct, indirect and synthetic holdings of own Additional Tier 1 instruments, including any such instruments that the institution could be obliged to purchase as a result of contractual obligations; 2) direct, indirect and synthetic holdings of Additional Tier 1 instruments in financial sector institutions with which the institution has reciprocal cross-holdings which, in the view of the competent authority, are designed to artificially inflate the institution's own funds; 3) direct, indirect and synthetic holdings of Additional Tier 1 instruments in financial sector institutions, where the institution has a significant investment in those institutions; and 4) the amount of items required to be deducted from Tier 2 items that exceeds the Tier 2 capital of the institution.

Tier 2 capital includes capital instruments and subordinated loans, and the related share premium accounts provided they meet certain conditions, and certain credit risk adjustments for institutions calculating risk-weighted exposure amounts in accordance with certain provisions established in detail in the Regulation.

Among other requirements, to qualify as Tier 2 capital: 1) the capital instruments or subordinated loans cannot be purchased by the institution, its subsidiaries or companies with which there are control links; 2) the claim on the principal amount of the instruments must be wholly subordinated to claims of all non-subordinated creditors; 3) the capital instruments or subordinated loans cannot be secured or subject to a guarantee provided by any group company that enhances the seniority of claims in the event of insolvency or liquidation; 4) they may be redeemed or repurchased only when authorised by the competent authority, and not before five years after the date of issuance;[24] 5) there shall be no explicit or implicit indication that the instruments or subordinated loans would or might be redeemed or repurchased early, as applicable, by the institution other than in the event of insolvency or liquidation of the institution, and the institution cannot otherwise provide such an indication; and 6) the provisions governing the instruments or

22 They may be redeemed or repurchased before five years provided that the institution replaces them with own funds instruments of equal or higher quality or that it evidences that, after the redemption, it satisfactorily meets the combined capital buffer requirements.

23 A trigger event shall be deemed to exist where the Common Equity Tier 1 capital ratio of the institution referred to in article 92.1.a) falls below: 1) 5.125%; or 2) a level higher than 5.125%, where determined by the institution and specified in the provisions governing the instrument.

24 As in the case of Additional Tier I instruments, they may be redeemed or repurchased before five years provided that the institution replaces them with instruments of equal or higher quality or that it evidences that, after the redemption, it satisfactorily meets the combined capital buffer requirements.

subordinated loans, as applicable, shall not give the holder the right to accelerate the future scheduled payment of interest or principal, other than in the event of insolvency or liquidation of the institution.

The items to be deducted from Tier 2 capital include: 1) direct, indirect and synthetic holdings of own Tier 2 instruments, including any such instruments that the institution could be obliged to purchase as a result of contractual obligations; 2) direct, indirect and synthetic holdings of Tier 2 instruments in financial sector institutions with which the institution has reciprocal cross-holdings which, in the view of the competent authority, are designed to artificially inflate the institution's own funds; and 3) the amount of direct, indirect and synthetic holdings of Tier 2 instruments in financial sector institutions, where the institution has a significant investment in those institutions.

The competent authority shall grant permission for an institution to reduce, repurchase or redeem Common Equity Tier 1, Additional Tier 1 or Tier 2 instruments where: 1) the institution replaces them with own funds instruments of equal or higher quality on terms that are sustainable for the income capacity of the institution; 2) the institution has demonstrated to the satisfaction of the competent authority that, following the action in question, its own funds would exceed the own funds requirements and the capital buffer requirements defined in Directive 2013/36/EU by a sufficient margin.

Prudential filters

Institutions shall not include any of the following items in own funds: 1) fair value reserves related to gains or losses on cash flow hedges of financial instruments that are not valued at fair value, including projected cash flows; 2) gains or losses on liabilities of the institution valued at fair value that result from changes in the institution's own credit standing; and 3) all fair value gains and losses arising from the institution's own credit risk related to derivative liabilities. For that purpose, institutions shall not offset fair value gains and losses arising from the institution's own credit risk with those arising from its counterparty credit risk.

Save in accordance with the provisions of the preceding paragraph, institutions shall not make adjustments to remove from their own funds unrealised gains or losses on their assets or liabilities measured at fair value. During the period from 1 January 2014 to 31 December 2017 institutions shall include in the calculation of their Common Equity Tier 1 items only the applicable percentage of unrealised losses related to assets or liabilities measured at fair value, and reported on the balance sheet, excluding those referred to in the preceding paragraph and all other unrealised losses reported as part of the profit and loss account.

Likewise, during that same period, institutions shall remove from their Common Equity Tier 1 items the applicable percentage of unrealised gains related to assets or liabilities measured at fair value and reported on the balance sheet, and all other unrealised gains, with the exception of those related to investment properties reported as part of the profit and loss account. The residual amount shall not be removed from Common Equity Tier 1 items. In both cases the applicable percentage will be between 20% and 100% and will be phased in up to the end of the period.

A point to note is that certain minority interests qualify for inclusion in consolidated Common Equity Tier 1, Additional Tier 1 and Tier 2 capital, according to the nature of the instruments concerned, provided that they are of a subsidiary of the institution and that they belong to persons other than those included in the consolidation. By way of

exception, minority interests that are funded directly or indirectly by the parent of the institution or its subsidiaries shall not qualify as consolidated Common Equity Tier 1 capital.

Own funds requirements

Institutions shall at all times satisfy the following own funds requirements:

1) Common Equity Tier 1 capital ratio of 4.5%.

2) Tier 1 (Common Equity Tier 1 + Additional Tier 1) capital ratio of 6%.

3) Total capital ratio of 8%.

By way of exception, during 2014 the competent authorities may establish the following own funds requirements: a Common Equity Tier 1 capital ratio of 4% to 4.5%, and a Tier 1 capital ratio of 5.5% to 6%.

In addition to these own funds requirements, institutions shall also have to satisfy the capital buffer requirements described in detail in Directive 2013/36/EU and discussed later in this article.

Institutions shall calculate their capital ratios as follows:

1) Common Equity Tier 1 capital ratio: Common Equity Tier 1 capital of the institution expressed as a percentage of the total risk exposure amount, as explained below.

2) Tier 1 capital ratio: Tier 1 capital of the institution expressed as a percentage of the total risk exposure amount.

3) Total capital ratio: the own funds of the institution expressed as a percentage of the total risk exposure amount.

The total risk exposure amount shall be calculated as the sum, inter alia, of: 1) the risk-weighted exposure amounts for credit risk and dilution risk in respect of all the institution's business activities, excluding risk-weighted exposure amounts from its trading book; 2) the own funds determined for the trading book, for position risk; 3) the own funds determined for foreign-exchange risk, settlement risk and commodities risk; 4) the own funds calculated for credit valuation adjustment risk of OTC derivative instruments other than credit derivatives recognised to reduce risk-weighted exposure amounts for credit risk; 5) the own funds determined for operational risk; and 6) the risk-weighted exposure amounts determined for counterparty risk arising from the institution's trading book for certain types of transactions and agreements.

It is noteworthy that, with the exception of the above-mentioned risk-weighted exposure amounts for credit risk, dilution risk and counterparty risk, to calculate all other exposure amounts institutions shall multiply the own funds requirements established by 12.5.

The Regulation lays down certain requirements for the reporting of own funds to the competent authorities, and certain specific reporting requirements related to each national property market to which institutions are exposed.

The following sections of the Regulation contain detailed provisions on the requirements, management and capital requirements of the above-mentioned risks. In comparison with the previous legislation, the coverage of certain risks that were previously unidentified, especially counterparty risks in derivatives transactions, has been strengthened.

Liquidity risk

One new development in the Regulation are the detailed rules on liquidity risk, which was previously given only a generic mention, introducing a short-term liquidity coverage ratio (LCR) and a net stable funding ratio (NSFR).

Short-term liquidity coverage ratio. Institutions shall hold levels of liquidity buffers sufficient to face any imbalance between liquidity inflows and outflows under gravely stressed conditions over a period of 30 days. In addition, institutions shall report to the competent authorities liquid assets that meet certain conditions established in the Regulation, such as assets: 1) that are unencumbered or available; 2) that are not issued by the institution itself, its parent or its subsidiaries; 3) whose price is generally agreed upon by market participants and can easily be observed in the market, or whose price can be determined by a formula that is easy to calculate; 4) that are eligible collateral for standard liquidity operations of a central bank of a Member State or, if the liquid assets are held to meet liquidity outflows in the currency of a third country, of the central bank of that third country; and 5) that are listed on a recognised market or are tradable on active outright sale markets or via a simple repurchase agreement on approved repurchase markets.

The value of a liquid asset shall be its market value, subject to certain haircuts (ranging from 0% to 20%) to reflect, at least, the duration, the credit and liquidity risk and typical repo haircuts in periods of general market stress. Institutions shall also report their liquidity inflows and outflows, as established in the Regulation.

In turn, the Regulation grants powers to the Commission to determine, by means of a delegated act, the short-term liquidity coverage requirement, specifying under which circumstances competent authorities have to impose specific inflow and outflow levels on credit institutions in order to capture the risks to which they are exposed. The delegated act shall be approved by 30 June 2014 and the liquidity coverage requirement shall be phased in as from 1 January 2015 as follows: 60% of the LCR in 2015; 70% as from 1 January 2016; 80% as from 1 January 2017; and 100% as from 1 January 2018. This schedule shall be reviewed before 30 June 2016 in order to assess whether it should be modified, in light of market and international regulatory developments.

Member States may maintain or introduce national provisions in the area of liquidity requirements before binding minimum standards are specified and introduced by means of the above-mentioned delegated act.

Stable funding ratio. Institutions shall ensure that long-term obligations are adequately met with a diversity of stable funding instruments, under both normal and stressed conditions. These shall include: 1) Tier 1 and Tier 2 capital instruments; 2) other preferred shares and capital instruments in excess of the Tier 2 allowable amount with effective maturity of one year or more; and 3) certain liabilities indicated, such as retail deposits.

Lastly, where an institution does not meet, or expects not to meet, the short-term liquidity coverage ratio or, as applicable, the stable funding ratio, including during periods of stress, it shall immediately notify the competent authorities and shall submit to them, without

undue delay, a plan for the timely restoration of compliance. Until compliance has been restored, the institution shall file a daily report at the end of each business day, unless the competent authorities authorise a lower reporting frequency or a longer reporting delay. Competent authorities shall only grant such authorisations based on the individual situation of an institution and taking into account the scale and complexity of its activities. They shall monitor the implementation of the restoration plan and shall require a more speedy restoration if appropriate.

Leverage ratio

Another new development in the Regulation is the introduction of the leverage ratio, to be calculated as an institution's capital measure divided by its total exposure measure and expressed as a percentage, where the capital measure is the Tier 1 capital and the total exposure measure is the sum of the exposure values of all assets and off-balance sheet items not deducted when determining the Tier 1 capital. Institutions shall calculate the leverage ratio as the simple arithmetic mean of the monthly leverage ratios over a quarter.

Institutions shall determine the exposure value of assets in accordance with certain principles, including: 1) the exposure value of an asset item shall be the accounting value remaining after applying specific credit risk adjustments, additional value adjustments and other own funds reductions related to the asset item, established in the Standardised Approach for calculation of credit risk; 2) physical or financial collateral, guarantees or credit risk mitigation purchased shall not be used to reduce exposure values of assets; and 3) loans shall not be netted with deposits.

The Regulation also determines the exposure value of repurchase transactions, securities lending or commodities borrowing transactions, long settlement transactions and margin lending transactions, including off-balance sheet items, and the exposure value of off-balance sheet items.

Institutions shall submit to the competent authorities all necessary information on the leverage ratio and its components.

By 31 October 2016 the European Banking Authority (EBA), established by Regulation (EU) No 1093/2010 of the European Parliament and of the Council, of 24 November 2010, shall report to the Commission its conclusions on certain issues, including: 1) whether the leverage ratio is the appropriate tool to suppress the risk of excessive leverage on the part of institutions in a satisfactory manner and degree; 2) defining business models that reflect institutions' overall risk profiles and introducing differentiated leverage ratio levels for those business models; and 3) whether changes to the calculation methodology would be necessary to ensure that the leverage ratio can be used as an appropriate indicator of the risk of excessive leverage, and if so, indicating which changes, and whether using Common Equity Tier 1 capital as the capital measure of the leverage ratio would be more appropriate for the intended purpose of tracking the risk of excessive leverage and, if so, what would be the appropriate calibration of the leverage ratio.

Lastly, by 31 December 2016, the Commission shall submit a report to the European Parliament and the Council on the impact and effectiveness of the leverage ratio, which is set to be harmonised and to enter into force on 1 January 2018. In the meantime, Member States may apply such measures as they consider appropriate, including measures to mitigate macroprudential or systemic risk in a specific Member State.

Reporting and public disclosure requirements

The Regulation lays down the reporting and disclosure requirements for institutions, which shall have policies to ensure that their disclosures convey their risk profile comprehensively to market participants. However, they shall only be required to disclose information that is material,[25] and not proprietary[26] or confidential.[27]

Institutions may determine the most appropriate medium, location and means of verification to comply effectively with the disclosure requirements established. Lastly, the Regulation sets out the technical criteria on transparency and disclosure of information, specifically institutions' risk management objectives and policies.

NEW DEVELOPMENTS IN DIRECTIVE 2013/36/EU

The Directive has two main aims: to update national provisions on access to the activity of institutions (credit institutions and investment firms); and to establish a single set of prudential regulations in the European Union. In the legislative part, the regulations on capital buffers, in the framework of the new rules on capital adequacy for institutions, are particularly significant.

The main new developments are highlighted below.

General requirements for access to the activity of credit institutions

As in the previous legislation, Member States shall require that applications for authorisation include: a programme of operations, setting out the types of business envisaged and the structural organisation of the credit institution; the identity of at least two persons who will effectively direct the business; the identity of shareholders or members, whether direct or indirect, natural or legal persons, that have qualifying holdings,[28] and the amount of those holdings. A new development is that, where there are no qualifying holdings, the identity of the 20 largest shareholders or members must be provided. The minimum initial capital requirement of €5 million remains; likewise, under certain conditions, authorisations may be granted to certain types of credit institutions that do not meet that requirement, provided they have capital of at least €1 million.

Also as previously, the authorisations granted and the terms of the authorisations shall be notified to the EBA, which may draw up draft regulatory technical standards to specify: 1) the information to be provided to the competent authorities in applications for authorisation of credit institutions, including the programme of operations; 2) the requirements applicable to shareholders and members that have qualifying holdings; and 3) obstacles that could prevent effective exercise of the supervisory functions of the competent authority.

The new Directive also maintains the disclosure obligations and the assessment criteria relating to any natural or legal persons that intend to acquire or dispose of a qualifying holding, or to increase or reduce a qualifying holding in a credit institution so that the proportion of the voting rights or of the capital held would be equal to or more than 20%, 30% or 50%, or so that the credit institution would become their subsidiary.

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25 Information shall be regarded as material if its omission or misstatement could change or influence the assessment or decision of a user that is relying on that information to make economic decisions.

26 Information shall be regarded as proprietary to an institution if disclosing it publicly could undermine its competitive position. It may include information on products or systems which, if disclosed to competitors, would render an institution's investments less valuable.

27 Information shall be regarded as confidential if there are obligations to customers or other counterparty relationships binding an institution to confidentiality.

28 A qualifying holding is a direct or indirect holding in a company that represents 10% or more of the capital or of the voting rights or that makes it possible to exercise a significant influence over the management of that company.

Consistent with the rationale of the previous legislation, the Directive envisages that authorised credit institutions shall obtain the single passport or licence recognised throughout the European Union for pursuit of all or part of the activities listed in Annex I to the Directive (a list of typical activities of credit institutions subject to mutual recognition), either through a branch or by provision of services. In addition, similar requirements for disclosure, notification and interaction between competent authorities are established.

Prudential supervision of institutions

Responsibility for the prudential supervision of institutions continues to lie with the competent authorities of the home Member State, without prejudice to the provisions of the Directive on cooperation with the competent authorities of the host Member State. It is noted, in particular, that the competent authorities shall supply each other with all information on the management and ownership of such institutions that may facilitate their supervision, especially with regard to liquidity, solvency, deposit guarantee, the limiting of large exposures and other factors that may influence the systemic risk posed by the institutions, such as administrative and accounting procedures and internal control mechanisms.

The competent authorities of the home Member State shall immediately inform the competent authorities of all host Member States in the event that liquidity stress occurs or can reasonably be expected to occur. That information shall also include details of the elaboration and implementation of a recovery plan and of any prudential supervision measure taken in that context.

Another key point is that the competent authorities shall review and evaluate the arrangements, strategies, processes and mechanisms used by institutions and the own funds and liquidity held by them, to ensure that they provide sound management and coverage of their risks. Competent authorities shall also establish the frequency and intensity of this review and evaluation, which shall in any event be updated at least on an annual basis, having regard to the size, systemic importance, nature, scale and complexity of the activities of the institution concerned. They shall also carry out stress tests on institutions they supervise, to facilitate the process.

Treatment of risks

Member States shall ensure that the management bodies of institutions approve and periodically review the strategies and policies for taking up, managing, monitoring and mitigating the risks to which they are or might be exposed, including those posed by the macroeconomic environment in which they operate in relation to the stage of the economic cycle.

Institutions that are significant in terms of their size or internal organisation or of the scale or complexity of their activities must establish a *Risk Committee* made up of members of the management body who do not perform executive functions in the institution and who shall have the knowledge, expertise and experience needed to fully understand and monitor the institution's risk strategies and risk appetite. Competent authorities may allow institutions that are considered less significant to establish joint audit and risk committees, whose members must also have the knowledge, expertise and experience needed to belong to both the risk and the audit committee.

Competent authorities shall encourage institutions that are significant in terms of their size or internal organisation or of the complexity of their activities to develop internal credit risk assessment capacity and to make greater use of the Internal Ratings Based (IRB) Approach to calculate their own funds requirements for credit risk, especially where their exposures are material in absolute terms and they also have a large number of material

counterparties. They shall also ensure that those solvency assessments do not rely exclusively on external credit ratings, such as those provided by external credit assessment institutions (ECAIs).

Institutions shall also be encouraged to use internal models to calculate their own funds requirements for: specific risk of debt instruments in the trading book; default and migration risk, where their exposures to specific risk are material in absolute terms and where they have a large number of material positions in debt instruments of different issuers; concentration risk; securitisation risk; market risk; interest rate risk from non-trading book activities; operational risk; liquidity risk; and risk of excessive leverage.

Governance and remuneration policies

The Directive regulates the general principles of governance and remuneration policies for institutions, which largely derive from Directive 2006/48/EC which it repeals. Regarding governance, institutions shall have: 1) robust governance arrangements, including a clear organisational structure with well-defined, transparent and coherent lines of responsibility; 2) effective processes to identify, manage, monitor and report the risks to which they are or might be exposed; and 3) adequate internal control mechanisms, including sound administration and accounting procedures, together with remuneration policies and practices consistent with sound and effective risk management.

Member States shall ensure that institutions that are significant in terms of their size or internal organisation or of the complexity of their activities establish a *Nomination Committee* made up of members of the management body who do not perform executive functions in the institution concerned.

Regarding remuneration policies, competent authorities shall ensure that institutions, when establishing and applying their overall remuneration policies, comply with principles, approved by their managing bodies, which ensure that such policies are consistent with sound and effective risk management and do not encourage risk-taking in excess of the level of tolerated risk of the institutions. The remuneration policy shall be consistent with the business strategy, objectives, values and long-term interests of the institution and shall include measures to prevent conflicts of interest. It shall be subject, at least once a year, to a central and independent internal review, to verify that it complies with the remuneration guidelines and procedures established by the management body in its supervisory function. The remuneration of senior officers in risk management and compliance functions shall be directly overseen by the remuneration committee or, in the absence of a remuneration committee, by the management body in its supervisory function.

Taking into account national pay-setting criteria, the remuneration policy shall draw a clear distinction between: 1) basic fixed remuneration, which should primarily reflect relevant professional experience and the level of responsibility in the organisation, as set out in the corresponding job description as part of the terms of employment; and 2) variable remuneration, which should reflect not only a sustainable and risk-adjusted performance but also a performance in excess of that required to meet the job description.

The following principles shall apply to variable remuneration: 1) where it is performance-related, the total remuneration shall be based on a combined assessment of individual, business unit and institution-wide performance, and when assessing individual performance, both financial and non-financial criteria shall be considered; 2) the performance assessment shall be set in a multi-year framework so as to ensure that the assessment process is based on long-term performance and that the actual payment of performance-based remuneration is

spread over a period which takes account of the underlying business cycle of the credit institution and its business risks; 3) the total variable remuneration must not limit the ability of the institution to strengthen its capital base; 4) guaranteed variable remuneration is not consistent with sound risk management or with the pay-for-performance principle and shall not be a part of prospective remuneration plans; 5) guaranteed variable remuneration shall be exceptional, it shall be used only for new hires and when the institution has a sound and strong capital base and shall be limited to the first year of employment; and 6) fixed and variable components of total remuneration shall be appropriately balanced. The fixed component shall represent a sufficiently high proportion of the total remuneration so as to ensure optimum flexibility in application of the variable components, including the possibility of no variable components being paid.

Institutions shall set appropriate ratios between the fixed and variable components of total remuneration, applying the following principles: 1) the variable component shall not exceed 100% of the fixed component of each individual's total remuneration (Member States may set a lower maximum percentage); and 2) shareholders, owners or members of institutions may be authorised to approve a higher maximum percentage, provided the overall level of the variable component does not exceed 200% of the fixed component of each individual's total remuneration (Member States may set a lower maximum percentage).

Institutions that benefit from government intervention are subject to limits on remuneration, especially on variable remuneration. Specifically, in addition to the above, the following principles shall apply:

1) Where it is inconsistent with the maintenance of a sound capital base, variable remuneration shall be strictly limited to a specific percentage of net revenue.

2) The relevant competent authorities shall require institutions to restructure remuneration to bring it in line with sound risk management and long-term growth, including, where appropriate, setting limits on remuneration for members of management bodies.

3) Members of management bodies shall receive no variable remuneration unless this can be justified.

Competent authorities shall compile information on the number of individuals in each institution receiving remuneration of €1 million or more per financial year, including their job responsibilities, the business area involved and their main salary components, bonuses, long-term incentive awards and pension contributions. That information shall be forwarded to the EBA, which shall publish it on an aggregate home Member State basis in a common reporting format. The EBA may draw up guidelines to facilitate the use and ensure the consistency of the information compiled.

Capital buffers

In accordance with the recommendations of the BCBS, the Directive establishes that, in addition to the Common Equity Tier 1 capital needed to meet the own funds requirements, credit institutions and certain investment firms[29] must hold certain capital buffers to ensure that they accumulate, during periods of economic growth, a sufficient capital base to absorb losses that may arise in periods of stress.

29 This requirement shall not apply to investment firms that are not authorised to provide certain investment services, defined in the Annexes to the Directive.

Accordingly, institutions shall be required to hold a *capital conservation buffer* of Common Equity Tier 1 capital equal to 2.5% of their total risk-weighted exposure amounts, established in Regulation (EU) No 575/2013 analysed above. Institutions that fail to meet that requirement shall be subject to the restrictions on distributions laid down in the Directive and shall thus be prohibited from taking certain steps, such as: making a distribution related to Common Equity Tier 1 capital; assuming an obligation to award variable remuneration or discretionary pension benefits, or to pay variable remuneration if the payment obligation was assumed at a time when the institution did not meet the combined buffer requirement; or making payments linked to Additional Tier 1 capital instruments.

Institutions shall also be required to hold an institution-specific *countercyclical capital buffer* of Common Equity Tier 1 capital equal to their total risk-weighted exposure amounts multiplied by the weighted average of the countercyclical buffer rates that apply in the countries where their credit exposures are located. These rates, which shall range from 0% to 2.5%, calibrated in fractions or multiples of 0.25 percentage points, shall be set and reviewed quarterly by the competent authority designated by each Member State. They may be set at a higher level where the authority deems appropriate.

Where the relevant authority of a third country has set and published a countercyclical buffer rate, institutions authorised to operate in that country may use a different buffer rate to calculate their respective institution-specific countercyclical capital buffer if they reasonably believe that the rate set by that authority provides insufficient protection for them against the risk of excessive credit growth in that country.

The countercyclical buffer is in addition to Common Equity Tier 1 capital and to the capital conservation buffer. Institutions that fail to comply with this buffer shall be subject to the same restrictions as in the case of failure to comply with the capital conservation buffer.

Lastly, Member States may determine that *systemic risk buffers* be created to prevent or mitigate long-term non-cyclical macroprudential or systemic risks; in other words, a risk of disruption of the financial system that could have serious adverse consequences for the financial system and for the real economy of a specific Member State.

In this respect, the Directive draws a distinction between global systemically important institutions (G-SIIs) and other systemically important institutions (O-SIIs), determining how the two categories are to be identified. Competent authorities may establish capital buffers, which shall be supplementary to Common Equity Tier 1 capital, for each category. Up to five sub-categories of buffers may be established for G-SIIs, according to their systemic importance. Each G-SII shall, on a consolidated basis, hold a buffer corresponding to the sub-category to which it is allocated; that buffer shall consist of and be supplementary to Common Equity Tier 1 capital and shall range from a minimum of 1%, increasing in amounts of 0.5% for each subcategory, to a maximum of 3.5% of the institution's total risk-weighted exposure amounts. For O-SIIs, competent authorities may establish a supplementary Common Equity Tier 1 capital buffer of up to 2% of their total risk-weighted exposure amounts.

Aside of the provisions of the preceding paragraph, Member States may establish a systemic risk buffer that entails supplementary Common Equity Tier 1 capital requirements equal to at least 1% of the total risk-weighted exposure amounts located in the Member State setting the buffer rate, which rate may also apply to exposures located in third countries. Up to 31 December 2014 this buffer rate may fluctuate up to 3%, and as from

1 January 2015 it may reach 5%; the competent authority shall be required to offer a detailed explanation, in the first case of the reasons for this fluctuation, and in the second of the reasons why it may have topped that rate.

Where a systemically important institution is subject to a G-SII buffer or an O-SII buffer, the higher of the two shall apply. Where an institution, on an individual or sub-consolidated basis, is subject to an O-SII buffer and a general systemic risk buffer, the higher of the two shall likewise apply. Lastly, where the systemic risk buffer applies to all exposures located in the Member State setting the buffer, but not to exposures outside that Member State, the systemic risk buffer shall be cumulative with the G-SII or O-SII buffers.

An institution that fails to meet its capital buffer requirements shall draw up a capital conservation plan and shall submit it to the competent authority within a period of no more than ten days. The latter shall assess the plan and shall only approve it if it considers that, when implemented, it would be reasonably likely to conserve or raise sufficient capital to enable the institution to meet its combined buffer requirements within a period that the competent authority considers appropriate. If this is not the case, the competent authority shall require the institution to increase its own funds to certain levels within specified periods, or it shall subject the institution to the restrictions on distributions of profits established in the Directive.

A Member State may, however, decide to exempt small and medium-sized investment firms from the capital buffer requirements if this does not threaten the stability of its financial system. The decision shall be fully reasoned and shall include an explanation as to why the exemption does not threaten the stability of its financial system and a precise definition of the small and medium-sized investment firms affected.

Lastly, a gradual implementation schedule is set for these measures, starting with a grace period in 2014 and 2015. In 2016 the capital conservation buffer shall consist of Common Equity Tier 1 capital equal to 0.625% of an institution's total risk-weighted exposure amounts, and the institution-specific countercyclical capital buffer shall not exceed 0.625% of those exposure amounts. Both figures shall rise to 1.25% in 2017, to 1.875% in 2018 and to 2.5% as from 1 January 2019.

The systemic risk buffer shall apply as from 2014, although a gradual implementation schedule is established up to 2018 for the specific G-SII and O-SII buffers.

However, Member States may set a shorter transitional period, in which case they shall inform the relevant parties, including the Commission, the European Systemic Risk Board (ESRB), the EBA and the corresponding supervisory college, accordingly.

Other aspects of the Directive

Among other measures, the Directive regulates the initial capital of investment firms, which is unchanged from the previous legislation: €125,000 for firms which do not deal in financial instruments for their own account or underwrite issues of financial instruments, but which simply perform certain services for clients; and €730,000 for all other investment firms.

Firms that are not authorised to hold client money or securities shall have one of the following forms of coverage: 1) initial capital of €50,000; or 2) professional indemnity insurance covering all of the European Union, or some other comparable guarantee against liability arising from professional negligence, covering at least €1 million per claim and a total of €1.5 million per annum for all claims; or 3) a combination of initial capital and professional indemnity insurance providing a similar level of coverage to that indicated above.

Banco de España: Electronic Register

Resolution of 18 June 2013 of the Executive Commission of the Banco de España (Official State Gazette of 24 June 2013), creating the Banco de España's Electronic Register, was published.

The purpose of the Resolution is to create and implement the Electronic Register, which is a new instrument to permit electronic filing of requests, documents and notices. In particular:

1) Receipt and sending, by electronic means, of requests, documents and notices (and attached documents) corresponding to the procedures and services that come under the remit of the Banco de España described in the Annex to the Resolution, where such requests, documents and notices need not be processed using specific applications; and annotation of entry or exit of such documents.

2) Recording and certification in the event of litigation, disagreements or doubts as to the receipt or sending of requests, documents or notices. Exceptionally, requests, documents or notices corresponding to procedures and services that do not come under the remit of the Banco de España shall be admitted where this is established by law.

The Electronic Register is a single register for all the bodies of the Banco de España and is included in the Single General Register system, together with the physical registers (the Central Register and the Auxiliary Registers), so that documents and requests filed with the Banco de España in any of these registers shall be equally valid. Nevertheless, in accordance with the powers conferred upon it by law, the Banco de España may determine that electronic filing is compulsory.

The Electronic Register will permit filing of documents, requests and notices 365 days a year, 24 hours a day, notwithstanding any service interruptions for technical or operational reasons, notice of which will be given in the Virtual Office as far as possible in advance.

Requests, documents or notices filed may be automatically rejected by the Electronic Register or by any of the specific electronic processing applications, informing the sender of the circumstances of the rejection, which are detailed in the Resolution.

The Resolution came into force on 25 June 2013.

Governance of credit institutions: assessment of suitability of persons directing their business

In Directive 2006/48/EC of the European Parliament and of the Council, of 14 June 2006, relating to the taking up and pursuit of the business of credit institutions, the EBA was asked to draw up a set of guidelines for the assessment of the suitability of persons who effectively direct the business of credit institutions. In response to that request, on 22 November 2012 the EBA issued its guidelines on the governance of credit institutions.

To enhance and adopt the guidelines set by the European authorities, Royal Decree 256/2013 of 12 April 2013 (Official State Gazette of 13 April 2013) transposing Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions was published on the assessment of the suitability of persons who effectively direct the business of credit institutions, incorporating the EBA's criteria of 22 November 2012 on the assessment of the suitability of members of the management body and key function holders.

The Royal Decree first sets out a comprehensive list of requirements as to good business and professional repute, appropriate knowledge and experience and, in the case of direc-

tors, a capacity to practice good governance, which requirements must be met by members of boards of directors, managing directors or similar officers and persons holding internal control functions or other key posts for the day-to-day running of the business of the institution and of its parent, as established by the Banco de España.

Good business and professional repute. The Banco de España is granted the power to assess that persons satisfy this requirement, taking into account a broad range of criteria focused essentially on three aspects: 1) their personal and professional track record as to fulfilment of the responsibilities of the post assessed, especially their history of personal creditworthiness, professional responsibility and professional conduct, if they have held positions of responsibility in credit institutions that have been subject to a restructuring or resolution process; 2) convictions or penalties for crimes, misdemeanours or administrative infringements (taking into account, as applicable, attenuating circumstances such as whether or not judgments are final, the severity of penalties or the time that has elapsed);[30] and 3) the existence of founded investigations relating to white-collar crimes.

Should any of these circumstances befall the persons assessed during the pursuit of their activity and this is significant for the assessment of their good repute, the credit institution shall notify the Banco de España accordingly within a period of 15 business days. Likewise, should any members of the board of directors, managing directors or similar officers or other employees holding internal control functions or key posts for the day-to-day running of the business of the institution become aware that they are subject to any such circumstances, they must inform the credit institution accordingly.

Appropriate knowledge and experience. The persons assessed must have a suitable level of training and profile, especially in banking and financial services, and practical experience acquired in their previous occupations over a sufficient period of time. For this purpose, account shall be taken of knowledge acquired in the academic sphere and of professional experience acquired in similar posts in other institutions or companies.

When assessing practical and professional experience, particular attention shall be paid to the nature and complexity of the posts held, the powers, decision-making powers and responsibilities held, the number of persons reporting to the persons assessed, their financial industry technical know-how and the risks managed. In any event, the level of experience shall be assessed taking into account the nature, scale and complexity of the business of each financial institution and the specific functions and responsibilities of the post held in the institution.

Secondly, and as a new development, the Royal Decree introduces the *assessment of the suitability of the members of the board of directors overall*, taking into account the different profiles of the board members, with a view to strengthening the independence and autonomy of the board as the top-level management body. In addition, board members must have the capacity to practice good governance. For that purpose, account shall be taken of: 1) any potential conflicts of interest that could lead to undue influence by third parties; and 2) the capacity of the board members to devote the time needed to perform the corresponding functions. Should any circumstance that might alter their capacity to practice good governance in the institution befall any of the directors during the pursuit of their activity, the credit institution shall notify the Banco de España accordingly within a period of 15 business days.

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30 For this purpose, the Banco de España may establish a committee of independent experts to report on the assessment files in cases of convictions for crimes or misdemeanours.

Moreover, credit institutions, in proportion to the nature, scale and complexity of their business, must have the appropriate *units and internal procedures* for selection and ongoing assessment of their directors and of persons holding internal control functions or key posts for the day-to-day running of the banking business. Once those key posts have been identified, an up-to-date list of the persons holding such posts and of the suitability assessment made by the institution, including the supporting documentation, must be made available to the Banco de España.

In addition to managing the Register of senior banking officers, the Banco de España shall be responsible for creating and managing a *Register of directors and managing directors* of parent institutions, other than credit institutions, investment services firms or insurance or reinsurance companies of Spanish banks, where all directors, managers and similar officers must necessarily be recorded. For these purposes, the persons concerned must notify their appointment within 15 business days following the date of acceptance of their post, indicating the personal and professional details to be established, in general, by the Banco de España, and expressly declaring, in the document evidencing their acceptance, that they satisfy the requirements as to good repute and, where applicable, professional profile and the capacity to practice good governance, and that they are not subject to any restrictions or incompatibilities that may be applicable.

Lastly, the Royal Decree extends these requirements as to good business repute and professional experience to most of the institutions supervised by the Banco de España, such as electronic money institutions, payment services institutions, appraisal companies, currency-exchange bureaux and mixed financial holding companies.

The Royal Decree came into force on 14 April 2013. However, two transitional periods are established for adaptation to the legislation: 1) three months from the date of entry into force, to set up the appropriate units and internal procedures for selection and ongoing assessment of the members of boards of directors, or governing councils in the case of credit cooperatives, managing directors or similar officers and persons holding internal control functions or key posts for the day-to-day running of the banking business, as established in the Royal Decree; and 2) six months from the date of entry into force, to replace any directors, managing directors or similar officers and other employees who do not satisfy the requirements as to good business and professional repute, who do not have the appropriate knowledge and experience to perform the corresponding functions or, in the case of directors, who do not have the capacity to practice good governance in the institution.

Hybrid capital and subordinated debt instrument management actions

Law 8/2013, 26 June 2013 (BOE of 27 June), on urban renewal, regeneration and rehabilitation, was published, the fifteenth final provision of which extends the period of application of hybrid capital and subordinated debt instrument management actions, as set out in Law 9/2012 of 14 November 2012[31] on restructuring and resolution of credit institutions,[32] from 30 June to 31 December.

The Law came into force on 28 June 2013.

31 See “Financial regulation: 2012 Q4,” Economic Bulletin, January 2013, Banco de España, pp. 36-40.

32 Chapter VII of Law 9/2012 established that credit institution restructuring and resolution plans should include actions regarding the management of the hybrid capital instruments and subordinated debt of credit institutions affected by such plans so as to ensure an appropriate distribution of the costs of restructuring or resolution of the institution in accordance with European Union rules on State aid and the objectives and principles laid down in the Law, in particular, to safeguard financial stability and minimise the use of public funds.

Central Credit Register: changes to the regulations

The regulations of the of the Central Credit Register (CCR) have been updated to enhance its content, primarily by expanding the range of data reporting entities are required to submit and the interconnections within it, and so as to comply with the requirements of the Memorandum of Understanding on Financial Sector Policy, 23 July 2012. Implementing this reform necessitated a number of changes to Law 44/2002 of 22 November 2002[33] on financial system reform measures, Chapter IV of which regulates the CCR. These were incorporated into the first additional provision of Royal Decree-Law 6/2013 of 22 March 2013 (BOE of 23 March 2013) on the protection of the holders of certain savings and investment products and other financial measures.

The changes in this Law are basically intended to establish a clear distinction between the data reported to the CCR for forwarding to other reporting entities for them to use in the course of their business, and the information (including data based on financial institutions' own forecasts) required by the CCR exclusively for compliance with the reporting requirements established by the Banco de España in the exercise of its supervision and inspection functions, and other functions assigned to it by law.

These changes were implemented with the publication of *Ministerial Order ECC/747/2013 of 25 April 2013* (BOE of 6 May), amending Ministerial Order ECO/697/2004 of 11 March 2004 and *CBE 1/2013, 24 May 2013* (BOE of 31 May), on the CCR, repealing CBE 3/1995 of 25 September 1995 and amending CBE 4/2004 of 22 December 2004 on public and confidential financial reporting rules and formats, which introduced some significant changes in the way the CCR operates.

The Ministerial Order came into force on 7 May and the Circular will come into force on 31 December of this year. A transitional regime has been established, which is applicable until March 2015, such that compliance with the obligations to report certain "information modules" will be phased in over this period (although in certain exceptional cases, the deadline is not until 31 December 2015).

Table 3 summarises the most important changes with respect to the previous regulations, in particular the creation of information modules to link operations with the counterparties involved, and transaction-by-transaction reporting, with no general minimum reporting threshold.

CHANGES TO EXPOSURE REPORTING

In order to allow better identification of the characteristics and risks of the various types of transactions, a more detailed breakdown of the main product type is envisaged than that is currently reported. Under the new rules data will be reported using information modules so as to facilitate data transmission and adapt reporting to the different nature and complexity of the various activities conducted by reporting entities.

In order to minimise the administrative burden this substantial increase in the amount of information to be reported to the CCR entails, the data have been subdivided into basic and dynamic data. The basic data are those which only need to be reported once, unless they are subsequently amended, as they do not normally change over time, whereas the dynamic data have to be reported periodically (i.e. monthly, quarterly or half-yearly, depending on their nature).

This system links transactions to their counterparties through its modules, indicating the nature of their involvement (direct exposure counterparty, guarantor, party subsidising

33 See "Financial regulation: 2002 Q4," Economic Bulletin, January 2003, Banco de España, pp. 95-96.

CHANGES TO THE REGULATIONS OF THE CENTRAL CREDIT REGISTER

TABLE 3

CBE 3/1995, 25 SEPTEMBER	CBE 1/2013, 24 MAY
Statement of exposures and purpose	
The purpose of the statement is both to provide data to reporting entities and to support supervision and inspection functions.	As well as reporting data for forwarding to other entities, data are to be reported for exclusive use in the Banco de España's supervision, inspection and other functions.
The exposure on the transactions existing at the end of each month is to be reported.	A monthly statement – broken down into principal, ordinary interest, interest on arrears, and claimable expenses – is also required, explaining why loan exposures have decreased (such as cash payments, refinancing, foreclosure of assets, etc.) and, where applicable, the amount of the reduction.
The purpose of this statement is to provide reporting entities with information for them to use in their business activities.	They must also furnish the mandatory information decided by the Banco de España in the exercise of its supervision, inspection and other legally mandated functions, including data based on entities' own forecasts.
Exposures reportable to the CCR	
Reportable risks are classified into two categories, according to the manner in which the counterparties are involved: 1) direct exposures with the first obligor; and 2) indirect exposures with guarantors and other persons liable for the risk in the event of a default by the direct exposure counterparty.	Each direct exposure will be linked to the indirect exposures affecting it, and the collateral guaranteeing fulfilment of the obligations arising from the direct exposures reported.
Reporting is on an aggregate basis by transaction type, with a threshold of €6,000 for resident counterparties and €300,000 for non-residents.	Exposures are to be reported on an individualised, transaction-by-transaction basis, and there is no general minimum reporting threshold. Aggregate data may only be submitted in the case of counterparties belonging to the "households", "non-financial corporations" and "non-profit institutions serving households" sectors, and only when certain requirements are met. These requirements include the cumulative risk being less than €6,000, and that the products concerned are current account overdrafts, credit card debt, pension or salary advances, other call loans, or consumer finance loans with an original amount of less than €3,000 and repayment period of less than 12 months.
Use and transfer of CCR data	
Each month the CCR will send each reporting entity consolidated information from the whole system on its borrowers that have a cumulative exposure with another reporting entity of €6,000 or more.	This threshold is raised to €9,000 in the case of monthly returns and ad hoc requests from reporting entities.
The CCR will supply a report with the data from the most recent monthly statement.	For ad hoc report requests by reporting entities, another report with the statement returned six months previously will be submitted.
The counterparties for an exposure reportable to the CCR may access all the information provided to reporting entities and their risk report, broken down by reporting entities.	Counterparties for an exposure reportable to the CCR may access all the information concerning them, except in the case of data submitted to the Banco de España solely for the exercise of its supervision and inspection functions and other functions assigned to it by law. In this case, the risk report will only state the name of the entity reporting the exposures, so that interested parties can exercise their rights directly with the reporting entity.

SOURCES: BOE and Banco de España.

the principal or interest, etc.). To facilitate data control and management, all transactions will be identified with a code, which will remain unchanged throughout their lifetime. In exceptional cases where the entity needs to change a transaction's code, the old and new codes will be linked using a specific module intended for this purpose.

The addition of a code-linking module is particularly significant as it enables transactions to be linked in the case of transactions such as refinancing, rollovers, subrogations, assets deriving from off-balance-sheet transactions, transferred transactions, and financial guarantees received. Moreover, transactions secured by other CCR reporting entities are to be linked to transactions reported by the guarantor. Additionally, the beneficiary of the guarantee is to supply the guarantor with the details of the guaranteed transactions through the CCR.

The information required on assets received as collateral is particularly exhaustive in the case of real estate, and includes itemised valuations. This information is to be linked to the transactions the collateral secures in the relevant module. To meet supervisory needs, as required by the accounting circular, detailed information also has to be reported on assets foreclosed or received in lieu of payment of debts. This report has been designed to take into account the fact that an asset may be used as collateral for more than one transaction, that a transaction can be secured by more than one asset, and that assets' value may change over time.

Applying the principle of proportionality, supervised entities are only required to report data concerning guarantees received, securities, derivative instruments, and assets foreclosed or received in lieu of payment of debts when the cumulative value of each activity is €10 million or more. However, entities must keep the relevant information on their databases, regardless of this limit, where it is to be made available to the Banco de España if so required.

As well as the exposures on transactions existing at the end of each month, credit institutions are required to state each month the reasons why loan exposures have decreased (such as cash payments, refinancing, foreclosure of assets, etc.) and, where applicable, the amount of the reduction. This information is to be broken down into principal, ordinary interest, interest on arrears, and claimable expenses.

Restructured, refinanced, renegotiated, subrogated and segregated transactions have to be identified. Any links they may have to any originating transactions for which details were previously reported to the CCR must also be stated.

Transactions secured by other CCR reporting entities are to be linked to transactions reported by the guarantor. Additionally, when the guarantor is also a reporting entity, the beneficiary of the guarantee is to furnish the guarantor with the details of the guaranteed transactions through the CCR.

In the case of the transfer of loans to third parties in which management is retained, the transferring entity is to continue reporting transferred exposures as previously, but must also identify the assignee, and both the exposure they continue to assume and that taken on by the assignee.

Additionally, accounting and own funds information are to be submitted for each transaction in which the institution continues to assume risks, stating the credit rating, specific provisions, risk-weighted exposure, probability of default, etc.

EXPOSURES REPORTABLE TO THE CCR

One of the most important changes is the obligation to report exposures on an individualised, transaction-by-transaction basis, with no general minimum reporting threshold. Previously, reporting was on an aggregate basis by transaction type, with a threshold of €6,000 for resident counterparties and €300,000 for non-residents. As of the new legislation's coming into force, aggregate data may only be submitted, on a quarterly basis, in the case of counterparties belonging to the "households", "non-financial corporations" and "non-profit institutions serving households" sectors, and only when certain requirements are met. These requirements include the cumulative exposure being less than €6,000, and that the products concerned are current account overdrafts, credit card debt, pension or salary advances, other call loans, or consumer finance loans with an original amount of less than €3,000 and repayment period of less than 12 months.

Exceptionally, the Fondo de Garantía de Depósitos de Entidades de Crédito (Credit Institution Deposit Guarantee Fund) will not report the guarantees it gives other entities as a result of asset protection schemes included in action or restructuring plans, or other measures to support credit institutions adopted in accordance with the regulations governing its operation. For their part, reguarantee companies will not report to the CCR transactions in which they refinance financial guarantees given and bonds and non-financial guarantees, warranties and indemnities provided.

Exposures reportable to the CCR are those arising from transactions in the form of: 1) loans, classed as business credit; financial credit; finance leases, and reverse repurchase agreements; 2) debt securities, such as bonds and other securities creating or representing a debt for their issuer and issued either in the form of certificates or book entries; 3) financial guarantees requiring that the issuer make specific payments to reimburse the creditor for the loss incurred when the debtor defaults on their payment obligation, regardless of the legal form; 4) irrevocable commitments to grant loans under predetermined terms and conditions; 5) other commitments entailing credit risk;[34] and 6) loan of securities, in which the reporting entity grants the borrower full title to the securities with the commitment to return other securities of the same class as those received, without any disbursement being made, other than the payment of commission.

As under the previous legislation, reportable exposures are classified in two categories depending on the manner of the counterparties' involvement: 1) direct exposures with the first counterparty; and 2) indirect exposures with guarantors and other persons liable for the risk in the event of a default by the direct exposure counterparty.

The amount of the direct exposure is the sum of the drawdowns (principal, interest and commissions due, interest on arrears, and claimable expenses) plus any undrawn amounts (immediately and conditionally available). The indirect exposure is calculated as the maximum exposure guaranteed by the counterparty for the transactions in which the latter intervenes solely as guarantor, or because its signature is committed in trade portfolio transactions or financing bills.

USE AND TRANSFER OF CCR DATA

The CCR will send reporting entities monthly consolidated information from the system as a whole on those of their borrowers with a cumulative exposure with another reporting entity of €9,000 or more (this threshold was previously set at €6,000). Consequently, data on counterparties whose cumulative exposure with an entity is less than this amount will not be provided to reporting entities as they are only submitted to the CCR for the purposes of compliance with the reporting obligations laid down by the Banco de España in the exercise of its supervision and inspection role and other functions assigned to it by law.

As regards the information supplied to reporting entities, as of the entry into force of the legislation, when reporting entities request data on a potential customer, the CCR will provide two reports: one with the data from the most recent monthly report, and as a new feature, a report with the data reported six months previously. It is also stipulated that reporting entities may only process the information supplied to them by the CCR for the purposes of assessing the risk associated with the transactions motivating the application for the report. Thus the data may not be used for any other purposes.

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34 Specifically, guarantees and bonds that do not match the definition of a financial guarantee, and irrevocable documentary credits, those available under other commitments (multipurpose credit facilities, guarantee lines, documentary credit facilities and credit through drawdowns).

The Credit Institution Deposit Guarantee Fund and reguarantee companies may ask the CCR to send them exposure reports on the counterparties of transactions in which they are listed as indirect exposure counterparties.

The new legislation also makes certain changes to counterparties' right of access to information. Thus, any natural or legal person listed as a counterparty for an exposure reportable to the CCR may access all the information concerning them, except in the case of data submitted to the Banco de España solely for the exercise of its supervision and inspection functions and other functions assigned to it by law. In this case, the risk report will only state the names of the entity reporting the exposures, so that interested parties can exercise their rights with them directly.

In all other cases, the CCR will furnish the counterparties with two risk reports referring to the latest date for which data are available. One of these will include the same information as is given to reporting entities at the end of each monthly process, and in the other the information will be broken down transaction by transaction, indicating the name of the reporting entity and stating the amounts.

AMENDMENTS TO THE RULES ON PUBLIC AND CONFIDENTIAL FINANCIAL INFORMATION

Circular CBE 4/2004 has been amended to modify certain existing statements and add new ones, and to update the special accounting register of mortgage loans/transactions and the minimum sectorisation scheme in the database. Specifically, new statements have been added to provide transaction-by-transaction data on derivative instruments, equity instruments, and assets received in foreclosures or in lieu of debt payments, together with certain supplementary data on debt securities reported to the CCR. Applying the principle of proportionality, it is envisaged that information need not be sent on these activities when the cumulative amount of each is less than €10 million. Entities that have been submitting some of the aforementioned statements must continue to do so even if the cumulative amount of their transactions drops below the reporting threshold, until the Banco de España notifies them in writing that it is no longer necessary for them to do so.

Additionally, some of the statements envisaged in CBE 4/2004 have been modified in order to collect the information needed to prepare balance of payments statistics in accordance with Economic and Monetary Union statistical requirements, and new statements have also been added, including in particular information on the cost of funding raised in the month corresponding to business in Spain.

Collective investment institutions: key investor information document and prospectus

CNMV Circular 2/2012, 9 May 2013 (BOE 24 June), on the collective investment institution (CII) prospectus and key investor information document was published, replacing CNMV Circular 3/2006, 26 October 2006, on CII information prospectuses, to adapt their content to Community legislation. The Circular came into force on 25 May 2013.

This Circular completes the process of implementing European legislation on certain Undertakings for Collective Investment in Transferable Securities (UCITS) in national law.[35]

35 See Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), which came into force on 1 July 2011, implemented by Commission Regulation (EU) No 583/2010 of 1 July 2010 establishing the provisions for the application of Directive 2009/65/EC, as regards key investor information and conditions to be met when providing key investor information or the prospectus in a durable medium other than paper or by means of a website. Under these new regulations, the document of key investor information replaces the previous simplified prospectus, thus harmonising the document with the key information investors need to know about CIIs in order to make properly founded investment decisions at European level in a brief, concise and clear format.

This process began with the publication of Law 31/2011 of 4 October 2011, which amended Law 35/2003 of 4 November 2003 on collective investment institutions, and the publication of Royal Decree 1082/2012, 13 July 2012, approving the Regulation implementing Law 35/2003 of 4 November 2003.[36]

The Circular pursues three main objectives: 1) to regulate the document containing the key investor information, establishing the special requirements for real estate CIIS and hedge funds; 2) establish the standard formats of the CIIs document and prospectus; and 3) adapt the content of the Circular to recent legislative amendments concerning, among other things, the situations in which unit holders are entitled to leave the fund.

MAIN FEATURES OF THE KEY INVESTOR INFORMATION DOCUMENT AND PROSPECTUS

This document must be impartial, clear and not give rise to confusion. It must provide information in such a form that investors are able to distinguish it from that from other sources, and be written in concise and non-technical language that is comprehensible to the average investor. The aim is to ensure that investors can reasonably be expected to be in a position to be able to understand the essential characteristics, nature and risks of the investment product being offered and to take properly founded investment decisions without needing to resort to other documents.

The CNMV may require non-harmonised CIIs (i.e. those not complying with the requirements of Directive 2009/65/EC) or their managers and trustees, include in this document any additional information, warnings or explanations it sees fit for appropriate investor information and protection and market transparency.

Both the key investor information document and the prospectus must be updated when there are any changes in their key features, as described in the circular. The Circular also specifies the cases in which the aforementioned communications must state unit holders' right to leave the fund. This right gives them the possibility, within 30 calendar days of the communication being sent, of opting for a total or partial reimbursement or transfer of their units, at the corresponding settlement value on the date of the last day of the information period, without the deduction of a redemption fee or any other expense.

In specific cases in which unit holders are to be allowed to leave the fund of given prior information in the case of guaranteed funds, it must be expressly stated in the notification that the reimbursements are not guaranteed, and the settlement value of the fund and losses that would be incurred, with respect to the guaranteed minimum, are to be stated.

Finally, the cases in which the CNMV may update certain sections of these two documents ex officio, in particular, when necessary to adapt them to the regulations in force or to include warnings to enhance the information offered to investors.

SPECIFIC FEATURES OF THE KEY INVESTOR INFORMATION DOCUMENT AND PROSPECTUS IN CERTAIN CASES

The Circular establishes certain special features of the document of key investor information and prospectus applicable in the case of non-financial CIIs, hedge funds, and funds of hedge funds, affecting their scope, the information on the CII's track record, and determination of the risk profile of these funds. It also establishes special features for CIIs aiming to

36 The Circular implements the authority granted to the CNMV by Royal Decree 1082/2012 of 13 July 2012 to decide upon the content and form of presentation of the key investor information document, and establishes the special requirements for non-harmonised CIIs, according to the class, type or category to which they belong. It also authorised the CNMV to determine the content and form of presentation of the prospectus, and the special requirements applicable, and may require that any additional information, warnings or explanations it sees fit for appropriate investor information and protection and market transparency be included.

implement an investment policy that replicates or reproduces a particular stock-market or fixed-income index, or takes this index as its benchmark, and for quoted investment funds and open-ended collective investment schemes (SICAVs). In these cases, further additional content is described referring to efficient portfolio management techniques and financial derivative instruments, and to the management of guarantees in relation to these operations. Thus, among other points, CIIs must include a detailed description of the risks deriving from these activities, particularly counterparty risk and possible conflicts of interest, and their impact on returns. These techniques and instruments must be used in the best interests of the CII.

FORM AND CONTENT OF THE KEY INVESTOR INFORMATION DOCUMENT AND PROSPECTUS

The form and content of these two documents must conform to the standard models included in the annexes of the Circular. However, the CNMV may require that CIIs, or, where applicable, their managers and trustees, include any additional information, warnings or explanations it sees fit to adapt the information and ensure investor protection and market transparency.

Finally, certain aspects of CNMV Circular 5/2007, 27 December 2007, on significant events affecting CIIs; CNMV Circular 4/2008 of 11 September 2008 on the content of quarterly, half-yearly and annual reports of CIIs and of the statement of position; and CNMV Circular 6/2010 of 21 December 2010 on transactions in derivatives of collective investment institutions (CIIs) have been updated.

Investment services: customer information requirements regarding the financial instrument suitability assessment

CNMV Circular 3/2013 of 12 June 2013 (BOE of 19 June) was published, implementing certain obligations to provide information to investment services clients, in relation to the assessment of the suitability of financial instruments.

The Circular, which comes into force on 19 August, implements the powers granted to the CNMV by Law 24/1988 of 28 July 1988 on the Stock Market, amended by Law 9/2012 of 14 November 2012 on restructuring and resolution of credit institutions,[37] and is applicable to entities offering investment services (hereinafter, the Entities).[38]

The main changes are set out below.

OBLIGATION TO INFORM CUSTOMERS ABOUT THE SUITABILITY ASSESSMENT

To assess their customers in relation to investments, institutions are to give their customers a description in writing or any other durable form of how their recommendation matches the investor's characteristics and objectives. The recommendation must be consistent with all the characteristics of the customer evaluated and the description must refer, at least, to the terms in which the investment product or service has been classified from the point of view of market, credit and liquidity risk, and its complexity, and the customer suitability test. In the case of professional investors the institution may omit this explanation as regards knowledge and experience, and their financial situation. A short form of the description may be given when repeated recommendations are made regarding products of the same type or family.[39]

37 Law 24/1998 authorised the CNMV to require that the information given to investors prior to their purchasing a product include all the warnings it sees fit regarding the financial instrument, and in particular, warnings that it is a not a suitable product for non-professional investors, in view of its complexity. It may also require these warnings to be included in advertising material.

38 The following are considered to be investment firms: 1) securities dealers and brokers; 2) portfolio management companies; and 3) financial advisory firms. Duly authorised credit institutions and fund management companies may also provide certain investment services and ancillary services.

39 A product is considered to be of the same type or belong to the same family of products when the complexity of their characteristics and the nature of their risks are similar, bearing in mind market, liquidity and credit risks.

OBLIGATION TO INFORM CUSTOMERS ABOUT THE APPROPRIATENESS ASSESSMENT

Entities that assess the knowledge and experience of their customers when providing them with investment services other than advice on investments or portfolio management, must supply the customer with a copy of the document with the results of the test. The assessment must be consistent with all the information available to the entity or provided by the customer and used in the test. This document must be delivered each time a customer evaluation for a particular type or family of products is carried out.

The entity must demonstrate compliance with this information obligation. For this purpose, a signed copy of the information given to the customer stating the date on which it was delivered, a record of the information's being sent to the customer by electronic means, or any other reliable means will be sufficient.

When the assessment cannot be performed because the customer does not provide sufficient information, or the entity considers the service or product not to be appropriate for them, it must advise the customer that it is unsuitable for them given their lack of the necessary knowledge or experience to understand the nature and risks of the financial instrument used in the intended transactions.

When the transaction involves a complex instrument, the entity must obtain the customer's signature on the standard text for the case where the test could not be carried out, together with a handwritten statement that the product is complex and that it has not been possible to evaluate its appropriateness for the customer due to the lack of information. Similarly, when the entity provides a service relating to complex instruments other than advice on investments or portfolio management and wishes to include a statement to the effect that no advisory services have been given in this transaction with the documentation the investor is to sign, it must obtain the customer's signature together with a handwritten statement that they have not been given advice regarding this transaction.

UPDATED REGISTER OF ASSESSED CUSTOMERS AND UNSUITABLE PRODUCTS

In order to facilitate the supervisory activity of both the CNMV and the internal oversight bodies, entities are to keep an up-to-date register of assessed customers and unsuitable products which will reflect, for each customer, the products that have been evaluated previously with negative results. This is without prejudice to the fact that entities may conduct as many customer assessments as they see fit.

In compliance with the obligation to keep customers informed at all times, on request, entities must furnish customers with the information on their particular circumstances held on this register free of charge.

OTHER CHANGES

The obligations to assess suitability shall not be applicable to the FROB's decisions to execute hybrid capital instrument and subordinated debt management actions, as envisaged in Law 9/2012 of 14 November 2012 on restructuring and resolution of credit institutions, in view of the binding nature of the FROB's decision and the fact that investors' prior consent is not necessary.

When such hybrid capital instrument and subordinated debt management actions are carried out at the behest of the issuing institution and investor participation is voluntary, the entity may propose to the CNMV that the content of the warning and the handwritten text referred to above may be adapted to the special circumstances of the operation offered to investors.

Remuneration of directors of listed companies and savings banks that issue traded securities

CNMV Circular 4/2013 12 June 2013 (BOE of 24 June) establishing the standard forms for the annual report on remuneration of the directors of listed companies and of the members of the boards of directors and oversight committees of savings banks issuing securities admitted to trading on official securities markets was published.

This Circular implements the powers granted to the CNMV by Ministerial Order ECC/461/2013 of 20 March 2013 (BOE of 23 March 2013) setting out the content and structure of the annual corporate governance report, the annual compensation report, and other information mechanisms for listed companies, savings banks and other entities issuing securities admitted to trading on official securities markets. In particular, it authorises the CNMV to define the content and structure of the compensation reports, to which end it may establish models or forms in accordance with which the various entities are to publish these reports.

Under these powers, the standard models with which the format, content and structure of the annual compensation reports of listed companies and savings banks issuing securities admitted to trading on official securities markets are to comply are included in the annexes to the Circular.

These reports are also to be submitted to the CNMV electronic registry for their publication as a significant event.

The Circular came into force on 25 June 2013, and will be applicable to compensation reports subject to voting, on a consultative basis as a separate point on the agenda, at ordinary general shareholders' meetings or ordinary general assemblies held as of 1 January 2014.

Annual corporate governance report by listed companies, savings banks and other entities issuing traded securities

CNMV Circular 5/2013 12 June 2013 (BOE of 24 June) establishing the standard forms for the annual corporate governance report of listed companies and savings banks issuing securities admitted to trading on official securities markets was published.

As in the case of the preceding Circular, in this Circular the CNMV implements the powers granted by Ministerial Order ECC/461/2013 of 20 March 2013 to describe the content and structure of the annual corporate governance report of listed companies, savings banks and other entities issuing securities admitted to trading, authorising it to establish the relevant standard models or forms.

These models are included in the annexes to the Circular, and entities are required to adhere to them when submitting and disseminating their annual corporate governance reports.

These reports are also to be submitted to the CNMV electronic registry for their publication as a significant event.

The Circular came into force on 25 June and will be applicable to the annual corporate governance reports entities are due to submit as of 1 January 2014.

Amendment to the Regulations on credit rating agencies

Regulation (EU) No 462/2013 of the European Parliament and of the Council of 21 May 2013 (OJEU of 31 May) amending Regulation (EC) No 1060/2009 on credit rating agencies was published. The objectives of this Regulation include: 1) reinforcing the independence of credit rating agencies; 2) improving transparency and promote sound credit rating processes and methodologies; and 4) reducing the over-reliance of market participants on credit ratings.

The Regulation came into force on 20 June 2013, but envisages transitional arrangements whereby application of certain points will be phased in by stages between now and June 2018.

The main changes are set out below.

REINFORCING CREDIT RATING AGENCIES' INDEPENDENCE

The conditions of independence applying to credit rating agencies (CRAs) are reinforced in order to increase the level of credibility of credit ratings issued under this model. Regulation (EC) No 1060/2009, already required credit rating agencies to apply a rotation mechanism providing for gradual changes in teams of analysts and credit rating committees so that the independence of the rating analysts and persons approving credit ratings would not be compromised. This mechanism has now been extended to credit rating agencies in relation to re-securitisations,[40] limiting the period during which an agency may provide ratings on new re-securitisations with the same underlying assets from the same originator on a continual basis to four years. This rotation mechanism does not apply to smaller credit rating agencies, i.e. those that have fewer than 50 employees at group level involved in the provision of credit rating activities, or that have an annual turnover generated from credit rating activities of less than €10 million at group level.

The Regulation also requires a strict separation of the outgoing agency from the incoming credit rating agency in the case of rotation as well as between the two credit rating agencies providing credit rating services in parallel to the same issuer. The credit rating agencies concerned must not be linked to each other by control or belong to the same group of credit rating agencies. Likewise, agencies may not be shareholders or members of, or be able to exercise voting rights in, any of the other credit rating agencies, or have the power to appoint members of the administrative or supervisory boards of any of the other credit rating agencies.

Other measures to guarantee agencies' independence include stricter regulation of cases of conflicts of interest, which now also extend to agencies' shareholders or members. Credit rating agencies should therefore abstain from issuing credit ratings, or should disclose that the credit rating may be affected, where a shareholder or member holding 10% of the voting rights of that agency is also a member of the administrative or supervisory board of the rated entity or has invested in the rated entity when the investment reaches a certain size. Similarly, the fact that a shareholder or member holding at least 5% of the voting rights of that credit rating agency has invested in the rated entity or is a member of the administrative or supervisory board of the rated entity should be disclosed to the public, at least if the investment reaches a certain size. Moreover, where a shareholder or member is in a position to exercise significant influence over the business activity of the credit rating agency, that person should not provide consultancy or advisory services to the rated entity or a related third party regarding its corporate or legal structure, assets, liabilities or activities.

Finally, shareholders or members of credit rating agencies may not simultaneously hold a stake of 5% or more in more than one credit rating agency or exercise a dominant influence on any other agency, unless the credit rating agencies concerned belong to the same group.

GREATER TRANSPARENCY AND BETTER CREDIT RATING AGENCY METHODS AND PROCESSES

The regulation provides that the European Securities and Markets Authority (ESMA) is to set up a European rating platform on its website. This will include credit ratings and credit rating

40 A re-securitisation is understood to mean a securitisation in which at least one of its underlying exposures is itself a securitisation.

outlooks[41] issued by credit rating agencies and will be accessible to issuers, investors and other interested parties. The European rating platform will also incorporate the ESMA's central repository to which ratings agencies report information on historical performance data.

As regards credit rating procedures and methods, rating agencies are to establish, maintain, enforce and document an effective internal control structure governing the implementation of policies and procedures to prevent and mitigate possible conflicts of interest and to ensure the independence of credit ratings. Credit rating agencies are to establish standard operating procedures (SOPs) with regard to corporate governance, organisation, and the management of conflicts of interest. These SOPs should be periodically reviewed and checked to evaluate their effectiveness and assess whether they need to be updated.

When a credit rating agency intends to use new rating methodologies, models or key rating assumptions (or make a material change to existing ones) which could have an impact on a credit rating, it is required to inform the ESMA and publish the proposed changes on its website, inviting stakeholders to submit comments for a period of one month and give a detailed explanation of the reasons for and the implications of the proposed material changes or proposed new rating methodologies.

RULES CONCERNING SOVEREIGN RATINGS

Credit rating agencies are to issue sovereign ratings in a manner which ensures that the individual specificity of a particular Member State has been analysed. Credit rating agencies should explain the key elements underlying those credit ratings in their press releases or reports. A statement announcing revision of a given group of countries is prohibited unless accompanied by individual country reports. These reports must be made publicly available.

Credit rating agencies are to publish a calendar setting a maximum of three dates (which are to fall on a Friday) for the publication of solicited and unsolicited sovereign ratings and related rating outlooks of Member States on their websites and submit this calendar to ESMA annually. Finally, credit rating agencies are to refrain from making direct or indirect recommendations regarding sovereign entities' policies.

REDUCING THE OVER-RELIANCE ON CREDIT RATINGS

Over-reliance on credit ratings needs to be reduced and all the automatic effects deriving from credit ratings should be gradually eliminated. Financial institutions that use credit rating agencies ratings for regulatory purposes[42] must make their own assessment of the risk and not depend exclusively or automatically on rating agencies.

To this same end, certain measures have been introduced concerning the rating of structured finance instruments. Thus, the issuer, the originator and the sponsor of a structured finance instrument established in the European Union are to jointly publish on the European rating platform information on the credit quality and performance of the underlying assets of the structured finance instrument, the structure of the securitisation transaction, the cash flows and any collateral supporting a securitisation exposure as well as any information that is necessary to conduct comprehensive and well-informed stress tests on the cash flows and collateral values supporting the underlying exposures.

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41 The Regulation introduces the concept of "rating outlooks," which are opinions regarding the likely direction of a credit rating over the short term, the medium term or both. The relevance of rating outlooks for investors and issuers are comparable to that of credit ratings. They are therefore also required to be accurate, transparent and free from conflicts of interest.

42 Specifically, Credit institutions, investment firms, insurance undertakings, reinsurance undertakings, institutions for occupational retirement provision, management companies, investment companies, alternative investment fund managers and central counterparties.

Furthermore, where an issuer or a related third party intends to solicit a credit rating of a structured finance instrument, it is to appoint at least two credit rating agencies to provide credit ratings independently of one another. To ensure they give independent ratings, the appointed credit rating agencies must not belong to the same group of credit rating agencies nor be linked by relationships of control through their shareholders or members. This is intended to reduce reliance on a single rating.

The sectoral competent authorities in charge of supervising these entities are to monitor the adequacy of agencies' credit risk assessment processes, assess the use of contractual references to credit ratings and, where appropriate, encourage them to mitigate the impact of such references, with a view to reducing reliance on credit ratings, in line with specific sectoral legislation.

The Commission will continue to review whether references to credit ratings in European Union law trigger or have the potential to trigger sole or mechanistic reliance on credit ratings by the competent authorities or other financial market participants with a view to deleting all references to credit ratings in European Union law for regulatory purposes by 1 January 2020, provided that appropriate alternatives to credit risk assessment have been identified and implemented.

Finally, the Regulation governs credit rating agencies' civil liability regarding the credit ratings they issue. Thus, where a credit rating agency has committed, intentionally or with gross negligence, any of the infringements listed the Regulation, an investor or issuer may claim damages from it.

Community directive amending prudential requirements regarding certain financial institutions' risk management

Directive 2013/14/EU of the European Parliament and of the Council of 21 May 2013 (OJEU of 31 May) amending Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision, Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) and Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Funds Managers in respect of over-reliance on credit ratings, was published.

The Directive establishes that the competent authorities for institutions for occupational retirement provision (IORPs), UCITS and AIFMs (alternative investment fund managers) are to monitor the use of references to credit ratings in these institutions' investment policies, and where appropriate, encourage mitigation of the impact of such references, with a view to reducing exclusive and mechanistic reliance on such credit ratings.

Member States are to bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 21 December 2014.

The Directive came into force on 20 June 2013.

European venture capital funds

Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 (OJEU on 25 April) on European venture capital funds has been published, coming into force on 15 May and applicable as of 22 July 2013.

The Regulation establishes a series of requirements and uniform conditions for the marketing of qualifying European venture capital funds (EuVECAs) throughout the Union, as

well as rules on their portfolio composition, investment instruments and techniques, and the organisation, conduct and transparency of alternative investment fund (AIF) managers marketing EuVECAs.

CHARACTERISTICS OF EuVECAs

EuVECAs are AIFs that must be established in a Member State and invest at least 70% of their total aggregate capital contributions and uncalled committed capital in qualifying investment assets.

Qualifying investments may be: 1) capital or quasi-capital instruments issued by qualifying portfolio undertakings (as defined below) or issued by a company with a majority holding in such companies, and which have been acquired by the EuVECA in exchange for a capital instrument issued by it; 2) loans granted by EuVECAs to qualifying portfolio undertakings, provided that these loans do not use more than 30% of the total aggregate capital contributions and uncalled committed capital in the qualifying venture capital fund; 3) shares of qualifying portfolio undertakings bought from the undertaking's existing shareholders; and 4) units or shares in one or more other EuVECAs, provided that these EuVECAs have not invested more than 10% of their total aggregate capital contributions and uncalled committed capital in other EuVECAs.

A qualifying portfolio undertaking is one that, at the time of an investment by the qualifying venture capital fund: 1) is not admitted to trading on a regulated market or on a multilateral trading facility (MTF); 2) employs fewer than 250 persons; 3) has an annual turnover not exceeding €50 million or an annual balance sheet total not exceeding €43 million; 4) is not itself an AIF, credit institution, investment firm, insurance undertaking or financial holding company.

These companies may be registered in a Member State or non-EU country, provided that the latter is not listed as Non-Cooperative Country and Territory by the Financial Action Task Force on anti-money laundering and terrorist financing, and has signed an agreement with the Member State of origin of the EuVECA's manager and each Member State in which the latter intends to market the EuVECA's shares or units.

REQUIREMENTS UPON MANAGERS MARKETING EUVECAS

Managers of qualifying venture capital funds (EuVECAs) are to guarantee that they do not use more than 30% of the total aggregate capital contributions and uncalled committed capital[43] to purchase assets other than qualifying investments.

EuVECA managers may not employ any method by which the exposure of the fund is increased beyond the level of its committed capital, whether through borrowing of cash or securities, holding positions in derivatives or by any other means. They may only borrow, issue debt obligations or provide guarantees at the level of the EuVECA where such borrowings, debt obligations or guarantees are covered by uncalled commitments.

Managers of EuVECAs may market the units and shares of qualifying venture capital funds solely to investors considered to be professional clients or to other investors that: 1) commit to investing a minimum of €100,000; and 2) state in writing, in a separate document from the contract to be concluded for the commitment to invest, that they are aware of the risks associated with the envisaged commitment or investment.

43 The 30% threshold will be calculated on the basis of amounts investible after the deduction of all relevant costs (i.e. fees, charges and expenses borne by investors and which are agreed between the manager of an EuVECA and its investors). Holdings in cash and cash equivalents will not be taken into account in the calculation of this threshold as they are not considered investments.

They must also: 1) act honestly, fairly and with due skill, care and diligence in conducting their activities; 2) apply appropriate policies and procedures for preventing malpractices that can reasonably be expected to affect the interests of the investors and the qualifying portfolio undertakings; 3) conduct their business activities in such a way as to promote the best interests of the qualifying venture capital funds they manage, the investors therein and the integrity of the market; 4) possess adequate knowledge and understanding of the qualifying portfolio undertakings in which they invest; 5) treat their investors fairly; and 6) ensure that no investor obtains preferential treatment, unless such preferential treatment is disclosed in the rules or instruments of incorporation of the EuVECA.

Where a manager of an EuVECA delegates functions to third parties, the manager's liability towards the EuVECA or its investors shall remain unaffected. Any delegation of functions shall not undermine the effectiveness of supervision of the EuVECA manager and, in particular, prevent that manager from acting, or the EuVECA from being managed, in the best interests of its investors.

Managers of EuVECAs must identify and avoid conflicts of interest and, where they cannot be avoided, manage and monitor and disclose promptly those conflicts of interest in order to prevent them from adversely affecting the interests of the EuVECAs and their investors.

At all times, managers of EuVECAs must have sufficient own funds and use adequate and appropriate human and technical resources as necessary for the proper management of the EuVECA.

TRANSPARENCY REQUIREMENTS

Managers of EuVECAs are to make an annual report available to the competent authority of the home Member State for each EuVECA they manage within six months of the end of the financial year. This report will describe the composition of the portfolio of the EuVECA and the activities of the previous year. It must also disclose the profits earned by the qualifying venture capital fund at the end of its life and, where applicable, the profits distributed during its life. It must also contain the EuVECA's audited financial accounts.

Managers of EuVECAs must inform their investors, prior to their investment decision, in a clear and understandable manner, of at least the following: 1) the identity of the manager and any other service providers contracted by that manager in relation to their management of the EuVECAs, and a description of their duties; 2) the amount of own funds available to that manager and a detailed statement as to why that manager considers that amount to be sufficient to maintain the adequate human and technical resources necessary for the proper management of its qualifying venture capital funds; and 3) a description of the investment strategy and objectives of the EuVECA, including, *inter alia*, a description of the risk profile of the qualifying venture capital fund and any risks associated with the assets in which the fund may invest or investment techniques that may be employed.

SUPERVISION AND ADMINISTRATIVE COOPERATION

Managers of EuVECAs are to inform the competent authority of their home Member State of the following: 1) the identity of the persons who effectively conduct the business of managing qualifying venture capital funds; 2) the identity of the qualifying venture capital funds, the units or shares of which are to be marketed and their investment strategies; 3) a list of Member States where the manager of an EuVECA intends to market each qualifying venture capital fund; and 4) a list of Member States where the manager of a qualifying venture capital fund has established, or intends to establish, EuVECAs.

The competent authority of the home Member State will only register the manager of an EuVECA if the following conditions are met: 1) the persons who effectively conduct the business of managing EuVECAs are of sufficiently good repute and are also sufficiently experienced in relation to the investment strategies pursued by the manager of a qualifying venture capital fund; 2) the information mentioned has been furnished; 3) all the requirements have been met; and 4) the EuVECAs being managed meet the requirements laid down in the Regulation.

Registration shall be valid in all Member States and shall allow managers of EuVECAs to market qualifying venture capital funds under the designation 'EuVECA' throughout the European Union.

The competent authority of the home Member State is responsible for supervising compliance with the requirements laid down in this Regulation. Where there are clear and demonstrable grounds for the competent authority of the host Member State to believe that the manager of an EuVECA is in breach of this Regulation within its territory, it shall promptly inform the competent authority of the home Member State accordingly. The competent authority of the home Member State will then take appropriate measures.

Competent authorities will, in accordance with national law, have all supervisory and investigatory powers that are necessary for the exercise of their functions. They will, in particular, have the power to 1) request access to any document in any form, and to receive or take a copy thereof; 2) require the manager of a qualifying venture capital fund to provide information without delay; 3) require information from any person related to the activities of the manager of a qualifying venture capital fund; 4) carry out on-site inspections with or without prior announcement; 5) take appropriate measures to ensure that a manager of a qualifying venture capital fund continues to comply with the Regulation; and 6) issue an order to ensure that a manager complies with the Regulation and desists from a repetition of any conduct that may represent a breach of this Regulation.

Member States will lay down the rules on administrative penalties and other measures applicable to breaches of the provisions of the Regulation and will take all measures necessary to ensure that they are implemented. The administrative penalties and other measures provided for must be effective, proportionate and dissuasive.

Competent authorities and the European Securities and Markets Authority (ESMA) will cooperate with each other for the purpose of carrying out their supervision functions and will exchange all information and documentation necessary to carry out their respective duties under this Regulation.

Measures to strengthen the protection of mortgage debtors, debt restructuring and rented social housing

Law 1/2013 of 14 May 2013 (BOE of 15 May) on measures to strengthen the protection of mortgagors, debt restructuring, and rented social housing, was published, coming into force on 15 May 2013, and partially amended by Law 8/2013, 26 June 2013 (BOE of 27 June), on urban renewal, regeneration and rehabilitation, which came into force on 28 June 2013.

CHANGES IN THE PROTECTION OF MORTGAGORS

An immediate two-year moratorium on evictions of families considered to be especially vulnerable has been enacted. This exceptional temporary measure will affect any mortgage foreclosure proceedings or extrajudicial sale granting the property to the creditor affecting the principal residence of persons included in certain groups.

Special vulnerability is defined here in similar terms as in Royal Decree-Law 27/2012 of 15 November 2012 (BOE of 16 November 2012), on urgent measures to strengthen the protection of mortgage debtors. Namely it applies to: 1) large families; 2) one-parent families with two dependent children; 3) families with a child aged under three years; 4) families with a member with a recognised level of disability of more than 33%, requiring long-term care, or suffering from illness accredited as permanently preventing them from working; 5) families in which the mortgagor is unemployed and has exhausted their unemployment benefits; 6) families living together in which one or more persons related to the mortgagor or their spouse by a family tie of up to the third degree of kinship is disabled, requires long-term care, or suffers from a serious illness accredited as permanently preventing them from working; and 7) families in which there is a victim of domestic violence, provided the dwelling subject to repossession is their principal residence.

As well as being in one of the situations above, the following economic circumstances must also apply:

1) That the household's total income[44] is not more than three times the public multipurpose income indicator (IPREM). This limit will be four times the public multipurpose income indicator in cases 4 and 6 above, and five times this indicator when the person being evicted has cerebral palsy, mental illness or disability, with a recognised level of disability in excess of 33%, or has a physical or sensory disability, with a recognised level of disability of 65% or more, and in cases of serious illness accredited as permanently preventing them or their carer from working.

2) That during the four years prior to the application, the financial effort the mortgage burden represents as a share of household income has multiplied by a factor or at least 1.5.

3) That the mortgage payments are more than 50% of the household's combined net income.

4) That the mortgage loan is secured by the debtor's sole property and that it was granted to enable the purchase thereof.

Also, *Royal Decree-Law 6/2012 of 9 March 2012* on urgent measures to protect mortgage debtors with no means of support[45] has been amended to expand its scope of application, such that it applies to mortgage guarantors for the main debtor as well as loan contracts secured with a property mortgage for which the debtor is on the exclusion threshold. The application to guarantors will be under the same conditions as established for the mortgage borrower.

The cases and circumstances in which a debtor is considered to be on the exclusion threshold have also been updated. These are basically the following: 1) that the family's total income is not more than three times the public multi-purpose income indicator

44 The household comprises the debtor, his or her spouse (not legally separated) or registered cohabiting partner, and the children, irrespective of age, who live in the home, including those linked by a relationship of guardianship, custody or fostering.

45 Royal Decree-Law 6/2012 aimed to establish measures to enable the restructuring of mortgage debt for borrowers facing extreme difficulties keeping up with payments. The model of protection devised pivots on the drafting of a code of good practice for the viable restructuring of mortgage debt on the principal residence, backed up with a series of tax measures, and certain mechanisms to make foreclosure proceedings more flexible.

(IPREM) or four times this indicator if the household includes a disabled person; and 2) that during the four preceding years the household has suffered a significant alteration in its financial circumstances, in terms of its ability to afford housing, or the circumstances making the household especially vulnerable, as defined here, have arisen.

Certain protective measures have also been introduced for mortgage guarantors below the exclusion threshold. They can therefore require that the entity exhaust the main debtor's assets first, without prejudice to the application to the latter of the measures envisaged in the code of good practice, before claiming the guaranteed debt, even if they have expressly waived the benefit of discussion in the contract.

In relation to the code of good practice, the rule revises its scope of application, in particular, in the case of municipalities of up to 100,000 inhabitants where the purchase price of dwellings inhabited by one or two people has been increased from €120,000 to €150,000, with an additional €30,000 for each dependant up to a maximum of three.

It also specifies that member entities are to inform their customers appropriately about the possibility of their being covered by the provisions of the code. In particular, entities signing up to the code must inform customers in writing of its existence, giving a detailed description of its contents, and the possibility of customers failing to meet any of their mortgage payments or having any other difficulty meeting their mortgage payments might have of being covered by the code.

The number of members of the oversight committee entrusted with supervising and ensuring compliance with the code of good practice has been increased from four to eleven.[46] Similarly, the committee may examine and put to the government proposals relating to the protection of mortgage debtors. Another new feature is the penalty system, in which member entities breaching the code will be liable to the penalties laid down in Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions, and breach of the obligations arising from it will be considered a serious infringement and penalised as laid down in the Law.

Finally, the default interest rates applicable to all mortgage lending contracts as of the time the debtor accredits to the entity that they are on the exclusion threshold has been lowered from 2.5% to 2% of the outstanding loan principal.

CHANGES TO MORTGAGE MARKET LEGISLATION

Improvements have been made to the mortgage market with the amendment of the consolidated text of the Mortgage Law, promulgated by Decree on 8 February 1946; Law 2/1981 of 25 March 1981 on mortgage market regulation; and Law 41/2007 of 7 December 2007, amending Law 2/1981 of 25 March 1981 on mortgage market regulation and other rules of the mortgage and financial system, regulating reverse mortgages and long-term care insurance and establishing certain tax rules.

The *deed of mortgage* on the property must state whether the mortgaged property is intended as the principal residence or not. Unless proven otherwise, at the time of foreclo-

46 One appointed by the Ministry of Economic Affairs and Competitiveness, having at least the rank of Director General, who will chair the committee and have the casting vote; one appointed by the Banco de España, who will serve as the secretary; one appointed by the CNMV; a judge appointed by the General Council of the Judiciary; a clerk of court appointed by the Ministry of Justice; a notary appointed by the General Council of Notaries; a member appointed by the National Statistics Institute; one appointed by the Spanish Mortgage Association; one appointed by the Consumers' and Users' Council; two appointed by non-governmental organisations, providing placement services, selected by the Ministry of Health, Social Services and Equality.

sure it will be deemed that the property is the principal residence if so stated in the deed. The deed will also be required to include, together with the customer's signature, a handwritten statement, with the wording to be determined by the Banco de España, to the effect that the borrower has been adequately warned of the possible risks arising out of the contract. This will apply, in particular, in the following cases: 1) when limitations are placed on the variability of the interest rate, in the form of floor and ceiling clauses, in which the limit on downward variations is less than that on upward variations; 2) when the contract incorporates an interest rate hedging instrument, or 3) when the loan is in one or more foreign currencies.

In the case of mortgages on the principal residence, the *interest on arrears* that credit institutions may demand will be limited to three times the legal interest rate and may only accrue on the outstanding principal. Capitalisation of this interest is also expressly prohibited, and if foreclosure is insufficient to cover the whole of the secured debt, the sum raised will be applied to interest on arrears last, so as to reduce the principal on which interest accrues to the maximum possible extent.

Moreover, the repayment period of the mortgage or secured loan used to finance the purchase, construction or renovation of the principal residence may not exceed 30 years when seeking to refinance it by issuing securities pursuant to Law 2/1981 of 25 March 1981 on mortgage market regulation.

The Mortgage Law has also been strengthened as regards the arrangements for *extrajudicial sales of mortgaged property*, provided that this has been agreed in the mortgage deed in the event of a default on payment of principal or interest on the guaranteed amount.

Extrajudicial sale is to be witnessed by a notary and must comply with certain requirements and formalities. These include the following: 1) the valuation the interested parties assign to the property as the reference price for the auction may not differ from that which would have been set in direct judicial foreclosure proceedings and may in no case be less than 75% of the value indicated in the appraisal performed according to the provisions of Law 2/1981 of 25 March 1981; 2) the sale will be effected in a single electronic auction to be held on the online auctions portal managed by the Agencia Estatal del Boletín Oficial del Estado [State Agency for the Official State Bulletin]; and 3) when the notary considers that any of the clauses of the mortgage loan constituting the basis for the extrajudicial sale – or which may have determined the amount claimable – to be unfair, he or she shall notify the parties. The notary will suspend the extrajudicial sale in all cases where either of the parties accredits that they have applied to the competent judicial body for a resolution decreeing the unlawfulness of the sale, due to the existence of unfair contract terms in the mortgage contract, or for it to continue without the application of these terms.

The measures to encourage the independence of *appraisal companies* from credit institutions have also been strengthened, in particular in the case of those which derive 10% of their business from a credit institution or group of credit institutions (previously this figure was 25%). They will also be required to have internal rules of conduct establishing what roles their managers and directors are barred from exercising as a result of incompatibilities. These measures shall also apply to credit institutions' appraisal departments. It is also provided that the Consejo de Consumidores y Usuarios [Consumers' and Users' Council] may initiate penalty proceedings when it considers appraisal services to have been found to have been provided in an irregular manner. As of the entry into force of these rules, appraisal companies must undergo account audits, pursuant to the rules governing account auditing.

The requirement for prior notification of the Banco de España in the case of the acquisition of *significant shareholdings*[47] in appraisal companies remains in effect, and credit institutions are expressly prohibited from acquiring or maintaining such shareholdings. Natural or legal persons associated with the marketing, ownership, exploitation or financing of property valued by them are similarly barred.

CHANGES TO THE CIVIL PROCEDURE LAW

Various amendments have been made to Law 1/2000 of 7 January 2000 on Civil procedure in order to ensure that mortgage foreclosure proceedings take place in a way that protects the rights and interests of mortgagors appropriately, and overall, to streamline foreclosure proceedings and make them more flexible. In particular, the legal costs that may be claimed from the foreclosed debtor may in no case exceed 5% of the amount demanded in the foreclosure order.

The possibility of *a reduction in the outstanding debt* has been provided for, such that when part of the debt remains unpaid after mortgage foreclosure of the debtor's principal residence, the debtor may be released from it if certain conditions are satisfied. These are, settlement of 65% of the remainder within five years, together with interest at the legal rate, or if that is not possible, 80% over a period of ten years.

The debtor is also entitled to a share of any possible future revaluation of the foreclosed property. Specifically, if the foreclosed property is sold in the following ten years, the outstanding debt for which the debtor is liable will be reduced by 50% of the capital gain obtained from the sale.

If, during the periods indicated above, the property is realised for a sum greater than that for which the debtor is liable, the latter will be released under the above rules and be entitled to the remainder of the proceeds. If these periods expire in 2013 they will be extended until 1 January 2014.

Additionally, access to *auctions* has been made easier for bidders and the requirements imposed on them reduced, such that, for example, the guarantee necessary to bid has been reduced from 20% to 5% of the appraisal value of the property. The time a successful bidder is given to obtain the price at which the property was sold at auction has been doubled from 20 to 40 days.

Certain improvements have been made to auction procedures, such as establishing that the appraisal value for the auction may not be less than 75% of the appraisal value when the loan was granted (previously no reserve price was set).

If there are no bidders at the auction, the creditor may request that the *property be awarded* as follows. In the case of a principal residence, at 70% of the auction starting price (previously 60%), or at 60% if the total debt including all items is less than 70%. If the property is not the debtor's principal residence, at 50% of the starting price, or the amount owed for all items.

Enforcement procedures have also been amended such that either ex officio or on request by one of the parties, the competent judicial body may assess the existence of *unfair terms* in the contract giving rise to enforcement or determining the amount claimed

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47 A significant shareholding in an appraisal company is understood to be one that reaches at least 10% of the company's capital of voting rights, directly or indirectly. It also includes smaller shareholdings that nevertheless permit considerable influence to be exerted over the company.

and, consequently, order the foreclosure to be unlawful, or that it continue without application of the terms considered to be unfair.

Finally, in cases of default on loan repayments, as of the entry into force of this legislation, the creditor may initiate a claim for the capital owing together with interest once the debtor has defaulted on his or her obligation to pay an equivalent of at least three months' instalments and this pact is stated in the mortgage deed (no such period had previously been set).

OTHER CHANGES

The consolidated text of the Law regulating pensions schemes and pension funds, enacted by Legislative Royal Decree 1/2002 of 29 November 2002, has been amended to allow mortgagors to draw on their pension plans when facing foreclosure of their principal residence. Thus, for a period of two years as of the entry into force of this law, members of pension plans may realise their vested rights on request in the event of proceedings to evict them from their principal residence, provided certain requirements are met.

The terms and conditions under which these vested rights may be realised may be defined in the specific regulations, but at least the following minimum conditions must be met: 1) the pension plan member is in judicial or administrative foreclosure proceedings or in the process of an extrajudicial sale to meet their obligations, in which the sale of their principal residence has been ordered; 2) the pension plan member does not have other assets, rights or income that are sufficient to meet the totality of the debt subject to foreclosure proceedings and thereby avoid sale of the property; and 3) the net amount of their consolidated rights in the pension plan is sufficient to avoid the sale of the property.

The reimbursement of the vested pension rights will be made at the member's request in the form of a single payment of the amount necessary to avoid sale of the property, and shall be subject to the tax treatment applicable to pension plan benefits. The reimbursement must be made within seven working days of the member's submitting the necessary supporting documentation.

This provision will also be applicable to persons insured by assured savings plans, company insurance schemes, mutual provident schemes, and collective insurance in general that provides for pension commitments in which the rights arising from the premiums paid by the company have been transferred to the insured persons, together with the rights corresponding to the premiums paid by the latter.

Lastly, the government has been authorised to take the necessary steps to foster, jointly with the financial sector, the constitution of a stock of social housing to meet the needs of people who have been evicted from their principal residence as a result of their defaulting on their mortgage when the circumstances envisaged in this law apply.

Measures to support entrepreneurs and stimulate growth and job creation

Royal Decree-Law 4/2013 of 22 February 2013 (BOE of 23 February) on measures to support entrepreneurs and stimulate growth and job creation, was published, coming into force on 23 February 2013.

The main changes from the financial and fiscal standpoint are highlighted below.

CHANGES AFFECTING THE FINANCIAL SECTOR

The measures to promote business finance include an amendment to the Regulations on the organisation and supervision of private insurance, enacted by Royal Decree 2486/1998 of 20 November 1998, to allow insurance undertakings to invest in shares admitted to

trading on the alternative stock market (MAB)[48] or any other multilateral trading facility,[49] and in venture capital funds, and that these investments be eligible as part of their technical provisions. Similarly, the regulations on pension schemes and pension funds, enacted by Royal Decree 304/2004 of 20 February 2004, have been amended to allow pension funds to invest in these securities.

In both cases, a specific maximum limit of 3% of insurance undertakings' total technical provisions, or of the pension funds' total assets, in the securities of a single entity is established. This ceiling rises to 6% when they are issued or backed by entities belonging to the same group.

Another measure to encourage non-bank finance of share capital companies is the elimination of the limit set in the Law on Share Capital Companies.[50] This relaxation of the rules will only be applicable in the case of issues aimed at institutional investors, to ensure adequate protection of retail investors. Specifically, it applies in the following cases: 1) when aimed solely at qualified investors; or 2) investors purchasing securities of a minimum value of €100,000 in each issue; or 3) when offering securities with a nominal unit value of at least €100,000.

CHANGES IN TAX LEGISLATION

In order to stimulate business creation and reduce the tax burden on new firms in their first few years of operation, a more favourable tax framework has been created for self-employed persons starting a business. Thus, new businesses starting after 1 January 2013 will pay corporate income tax in the first tax year in which the company's taxable earnings are positive and in the subsequent tax year at a rate of 15% on the first €300,000 of taxable income, and 20% on the remainder.

In line with the above, a new reduction of 20% on net business and professional earnings has been established in personal income tax for persons starting a business or professional activity, applicable to the first tax year in which their earnings are positive and in the subsequent tax year. The current limit on the exemption for unemployment benefits received as a single payment has also been eliminated (this exemption was previously set at €15,500).

MEASURES COMBATING LATE PAYMENT IN COMMERCIAL TRANSACTIONS

The period in which debtors are to settle payment (unless stipulated otherwise in the contract) has been shortened from 60 to 30 calendar days after the receipt of the goods or provision of services, even if the invoice or demand for payment is received previously. This limit can be extended to 60 calendar days by agreement between the parties in exceptional cases.

It is stipulated that, if the parties have agreed a deferred payment timetable, and either of them fails to meet payment on the agreed date, the interest on arrears will be calculated only on the overdue amounts.

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48 This is a securities market supervised by the CNMV dedicated to small capitalisation companies that aim to expand, with regulations specially tailored to them, and costs and processes suited to their characteristics.

49 Multilateral trading facilities are managed by an investment firm or governing company of an official secondary market, making it possible to bring together different interests in buying and selling multiple financial instruments in the system according to its non-discretionary rules to enable contracts, i.e. a system in which transactions to buy and sell financial instruments are matched.

50 Article 405 of Legislative Royal Decree 1/2010 of 2 July 2010, enacting the consolidated text of the Law on Share Capital Companies, establishes that the total amount of issues by share capital companies may not exceed the value of their paid-up share capital plus their reserves as stated on the most recent approved balance sheet.

The legal interest rate the debtor is liable to pay in the event of late payment has been increased, such that it is now the interest rate applied by the ECB in its most recent main refinancing operation, plus eight percentage points.

Late payment incurs a fixed charge of €40 that the creditor is entitled to collect from the debtor, which will be added to the principal without the need for an express demand. All duly substantiated costs of collection caused by the default will be added to this amount. As regards these costs, the legislation states that any agreement between the parties excluding compensation will be presumed to be an unfair contract term and thus null and void.

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