Financial regulation: second quarter of 1999

1. INTRODUCTION

New financial provisions were relatively sparse in the second quarter of 1999, although some of them are of great importance.

In the area of the Banco de España, two circulars were published in relation to the *Sistema Nacional de Compensación Electrónica* (National Electronic Clearing System, SNCE). The first incorporates, within the current-account cheques and promissory notes general subsystem, documents subject to a protest before a notary public, since the extension of the period for protest means that protests can now be processed in the system by computer. The second, basically attempts to update various Banco de España circulars relating to the SNCE which had become obsolete, adapting them to current legislation.

With respect to credit institutions, the provisions of Directive 97/5/EC of 27 January 1997 (1) of the European Parliament and of the Council on cross-border credit transfers have been partially incorporated into Spanish law. As in the Directive, it is intended that transfers carried out through a credit institution from one place to another within the European Union (EU) should be rapid, reliable and cheap, and the customer information the institutions are required to ensure and the minimum obligations the institutions must assume to execute such transfers are established. Also, the table of official benchmark rates for mortgages has been adjusted, incorporating a new one-year interbank benchmark rate linked to the Euribor index.

Most of the provisions enacted during this period relate to the securities market. In the primary market, the liberalising regime introduced by Law 24/1988 of 28 July 1988 (2) has been extended to include issues of securities previously banned or subject to prior authorisation, modifying their administrative treatment. At the same time, the new legal regime for issuance in the securities markets established in Royal Decree 2590/1998 of 7 December 1998 (3) has been partially implemented: the National Securities Market Commission (CNMV) has been authorised to determine the content of short-form programme prospectuses (a new form of short-form prospectus) and to modify certain

(1) See "Regulación financiera: primer trimestre de 1997", in *Boletín económico,* Banco de España, April 1997, p. 117.

(2) See "Regulación financiera: tercer trimestre de 1988", in *Boletín económico,* Banco de España, October 1988, pp. 61 and 62.

(3) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, pp. 90-98.

types of prospectus currently regulated to adapt them to the special characteristics of the issuers, in order to make it easier for them to place securities in the primary market.

In the area of Portfolio Investment Institutions, three provisions worth mentioning are discussed: first, the agreements for the promotion of asset securitisation funds, which have made it possible to set up funds ("FTPymes") which, with a state guarantee, will specialise in the securitisation of loans to productive firms; second, the amendment of the co-operation agreements relating to FONDTESOROs (mutual funds which invest in government securities), state-guaranteed assets issued by "FTPymes", and to trade derivative instruments that are not traded on organised secondary markets; and, finally, the legal and tax regime for real-estate investment institutions, which implements the provisions of Law 20/1998 of 1 July 1998 (4). In particular, their investment policy has been made more flexible and they have been granted greater tax incentives.

With regard to other financial institutions the new legal regime for risk-capital institutions contained in Law 1/1999 of 5 January 1999 (5) has been implemented. The CNMV has been authorised to issue provisions in relation to the procedure for the authorisation of new institutions, and to establish their accounting rules and the formats for their annual accounts, as well as the information deriving from the financial supervision to which they are subject.

Turning to other areas, a new regulation has been issued on foreign investment, combining in one single piece of legislation the regulation of foreign investment in Spain and that of Spanish investment abroad, both of which are fully liberalised, in accordance with the principles laid down in this respect by the Treaty on European Union (the Maastricht treaty).

The publication of the statute of the Official Credit Institute should also be mentioned. This adapts its legal and financial regime to Law 6/1997 of 14 April 1997 on the organisation and operation of the general state administration, as was required by the provisions of the latter.

Finally, a set of urgent liberalisation and competition-enhancing measures have been introduced, to stimulate competition in markets for goods, services and productive factors, and also to avoid inflationary pressures emerging in certain sectors less exposed to foreign competition.

(4) See "Financial regulation: second quarter of 1998", in *Economic bulletin,* Banco de España, July 1999, pp. 89-90.

(5) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, pp. 100-101.

2. NATIONAL ELECTRONIC CLEARING SYSTEM: INCORPORATION OF NEW DOCUMENTS AND UPDATING OF CERTAIN ASPECTS

Royal Decree 1369/1987 of 18 September 1987 (6), the Ministerial Order of 29 February 1988 (7) and Banco de España Circular 8/1988 of 14 June 1988 (8) regulated the structure and operation of the SNCE, which is made up of the *Sistema Nacional de Intercambios* (National Exchange System) and the *Sistema Nacional de Liquidación* (National Settlement System). Later, Banco de España Circular 11/1990 of 6 November 1990 (9) laid down the operating rules for the current-account cheques and promissory notes general subsystem regulated in Rule SNCE-04 and integrated within the National Exchange System. Subsequently, said Circular was amended by Banco de España Circular 5/1991 of 26 July 1991 (10), Banco de España Circular 1/1995 of 30 June 1995 (11), Banco de España Circular 2/1998 of 27 January 1998 (12) and Banco de España Circular 9/1998 of 30 October 1998, in order to incorporate the clearing of new documents and payment instruments into that subsystem.

In the past, the regulation of Rule SNCE-04 excluded certain documents subject to one or more exceptions from its scope of application, including those subject to a protest before a notary public, since the period for its execution meant that they could not be processed through the subsystem.

Recently, under Law 19/1985 of 16 July 1985 on bills of exchange and cheques, amended by Law 37/1998 of 16 November

(6) See "Regulación financiera: cuarto trimestre de 1987", in *Boletín económico,* Banco de España, January 1988, p. 51.

(7) See "Regulación financiera: primer trimestre de 1988", in *Boletín económico,* Banco de España, April 1988, p. 65.

(8) See "Regulación financiera: segundo trimestre de 1988", in *Boletín económico,* Banco de España, July-August 1988, p. 79.

(9) See "Regulación financiera: cuarto trimestre de 1990", in *Boletín económico,* Banco de España, January 1991, pp. 31 and 32.

(10) See "Regulación financiera: tercer trimestre de 1991", in *Boletín económico,* Banco de España, October 1991, pp. 53 and 54.

(11) See "Regulación financiera: segundo trimestre de 1995", in *Boletín económico,* Banco de España, July-August 1995, p. 107.

(12) See "Financial regulation: first quarter of 1998", in *Economic bulletin,* Banco de España, April 1998, pp.104 and 105.

1998 (13) on the reform of the securities market, the period for making protests was extended from five to eight business days. This has made it possible for these documents to be brought within the scope of application of Rule SNCE-04. The Banco de España has carried out this incorporation through Banco de España Circular 5/1999 of 28 May 1999 (BOE [Official State Gazette] of 16 June 1999).

The following documents, among others, remain excluded from the subsystem: cheques with a payment date the same as or after the clearing date; cheques with a payment date more than 15 calendar days before the clearing date; cheques made out to a named payee with an issue date more than 45 calendar days prior to the clearing date; current-account promissory notes with maturity subsequent to the clearing date; and current-account promissory notes with maturity date more than ninety calendar days prior to the clearing date.

Banco de España Circular 6/1999 of 28 May 1999 (BOE of 16 June 1999), which amends various Banco de España circulars dedicated to the regulation of the SNCE, has been published. Its purpose is to update and homogenise their content, since some aspects thereof have been modified by higher ranking provisions, by the development of the SNCE itself, or by the publication of subsequent circulars.

3. BANK TRANSFERS

Directive 97/5/EC of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers laid down the basic rules for individuals and firms (in particular, small and medium-sized firms) to be able to make transfers through a credit institution from one place to another within the EU rapidly, reliably and cheaply, establishing both the customer information that the institutions must ensure and the minimum obligations of the institutions when executing such transfers in accordance with the customers' instructions.

The EU Member States were required to incorporate the provisions of this Directive into their domestic law by 14 August 1999.

Law 9/1999 of 12 April 1999 (BOE of 13 April 1999), which regulates the legal regime for cross-border transfers within the EU, has been published in order to comply with this requirement. This law partially introduces into Spanish law those provisions of Directive 97/5/EC that need to be enacted through a Law. The rest of the provisions of the Directive, which do not require such status, will be incorporated into Spanish law through the subsequent implementation of the Law.

The main novelty consists in the establishment, on one hand, of a number of minimum obligations of institutions in respect of the execution of cross-border transfers within the EU and, on the other, the legal consequences of breach of such obligations.

The scope of application of the Law includes any cross-border transfer made within the EU of an amount of up to EUR 50,000 (14) (approximately ESP 8.3 million pesetas) (excluding transfers not to be paid into an account), ordered by natural or legal persons (15), either through a credit institution or the branch of such an institution, or through so-called currency-exchange bureaux which manage transfers received from abroad or sent abroad through credit institutions. Likewise, intermediary institutions may participate in transfers between Member States. These may be credit institutions, other than the credit institutions of the originator and the beneficiary, acting as the correspondent of any of the above-mentioned entities.

With respect to the *minimum obligations* of the institutions, the latter shall execute transfers in accordance with the specific instructions of the customer, as regards both the time limit for execution and the total amount to be transferred. To this end, they shall comply with certain minimum requirements as to speed and reliability.

Both the institution of the originator and that of the beneficiary shall credit funds and make them available, respectively, within the time limit agreed with their customers. Where such time limit is not complied with or, in the absence of any such time limit, where, at the end of the fifth banking business day following the date of acceptance of the transfer order, the funds have not been credited to the beneficiary's account, the originator's institution shall compensate the latter in the terms laid down in the Law (16).

(13) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, pp. 90-98.

(14) The same amount as established in Directive 97/5/EC.

(15) The originator must be a natural or legal person other than a credit institution, currency-exchange bureau, insurance company, portfolio investment institution or investment services company.

(16) The compensation shall consist of interest on the amount of the transfer calculated at the legally established rate (4.25 % this year) multiplied by 1.25, for the period running from the end of the time limit indicated to the date on which the funds are credited into the account of the beneficiary entity.

The beneficiary's institution shall compensate the beneficiary, in similar terms, where the agreed time limit has not been complied with or, in the absence of any such time limit, where, at the end of the banking day following the day on which the funds have been credited to the account of the beneficiary's institution, they have not been credited to the beneficiary's account.

In the absence of any order to the contrary, the transfer must be executed free of charges for the beneficiary, unless the originator has specified that the charges for the transfer are to be wholly or partly borne by the beneficiary. Such instructions shall be notified to the beneficiary entity and to the intermediary institutions, if any. Otherwise, any amount unduly deducted shall be transferred or paid to the relevant party, the costs of such deductions being assumed by the party responsible.

The most serious case of breach consists of failure to execute a transfer, once it has been accepted by the originator's institution. In this case, the institution is obliged to refund the amount of the transfer plus the costs incurred by the originator and compensation – like that laid down in the Directive – up to a total of EUR 12,500 (approximately ESP 2.1 million).

Notwithstanding the foregoing, the Law provides that all the obligations mentioned are discharged in any situation of force majeure, namely abnormal and unforeseeable circumstances beyond the control of the person pleading force majeure, the consequences of which would have been unavoidable despite all efforts to the contrary.

4. CREDIT INSTITUTIONS: THE "EURIBOR" INDEX AS A NEW BENCHMARK RATE FOR MORTGAGES

Banco de España Circular 8/1990 of 7 September 1990 (17) on the transparency of operations and the protection of customers implemented the Ministerial Order of 12 December 1989 (18), which extended to credit institutions rules that were initially only applicable to deposit money institutions. This Circular has been updated since to reflect the changes that have occurred in the Spanish financial system, which have had a particular impact on the operations of credit institutions with their customers, as well as to adapt Spanish law to the EU law in this area. In particular, the latest amendments to Banco de España Circular 8/1990 were introduced by Banco de España Circular 4/1998 of 27 January 1998 (19), which incorporated the provisions of the Recommendation of the European Commission of 30 July 1997 concerning transactions by electronic payment instruments, and by Banco de España Circular 3/1999 of 24 March 1999 (20), which introduced some of the rules contained in Law 46/1998 of 17 December 1998 (21) on the introduction of the euro, as well as the recommendations of the European Commission of 23 April 1998 (22) concerning "banking charges for conversion to the euro" and concerning "dual display of prices and other monetary amounts", during the transitional period (from 1 January 1999 to 31 December 2001).

Banco de España Circular 8/1990 has recently been amended again, by *Banco de España Circular 7/1999 of 29 June 1999* (BOE of 9 July 1999). The table of official benchmark rates for mortgages has been extended to incorporate a new benchmark index linked to the euro-area interbank market. This index has been created by the European Banking Federation on the basis of the information provided by a broad set of banks of the area on their one-year interbank operations. This new one-year interbank benchmark rate, called EURIBOR, is defined as the simple arithmetic mean of the values of the spot rate published by the European Banking Federation for one-year euro deposit transactions, calculated from the offering rates of the above-mentioned banks.

5. MODIFICATION OF THE RULES ON SECURITIES ISSUANCE

Law 24/1988 of 28 July 1988 on the securities market established the general principle of freedom of issuance on the Spanish market, although, at the same time, it empowered the Ministry of Economy and Finance to ban certain issues or make them subject to prior authorisation. The Ministerial Order of 14 November

(17) See "Regulación financiera: tercer trimestre de 1990", in *Boletín económico,* Banco de España, October 1990, pp. 76 and 77.

(18) See "Regulación financiera: cuarto trimestre de 1989", in *Boletín económico,* Banco de España, January 1990, p. 35.

(19) See "Financial regulation: first quarter of 1998", in *Economic bulletin,* Banco de España, April 1998, pp. 105-106.

(20) See "Financial regulation: first quarter of 1999", in *Economic bulletin,* Banco de España, April 1999, pp. 58-60.

(21) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, pp. 83-90.

(22) See "Financial regulation: second quarter of 1998" in *Economic bulletin,* Banco de España, July 1998, pp. 92-93.

1989 (23), exercising this power, banned issues of securities where the principal or interest may be revised in accordance with the movements in some general index, and made three types of issue subject to prior authorisation: issues denominated in foreign currency made on the domestic market; issues by non-residents made on the domestic market; and issues with a maturity of more than 18 months when certain circumstances apply. Subsequently, the Ministerial Order of 18 December 1992 (24) dispensed with the need for prior authorisation in the first two cases (foreign-currency-denominated issues and issues by non-residents), without prejudice to the requirement for issues by non-residents in the Spanish market to be notified in advance to the Treasury.

The *Ministerial Order of 28 May 1999* (BOE of 4 June 1999) has recently extended the liberalising regime to the other cases mentioned, changing their administrative treatment.

Thus, the only case of a ban, namely issues of securities where the principal or interest may be revised in accordance with some general price index or with the price of some good or service or indices linked to the latter, is now subject to *prior authorisation.* However, this regime does not affect issues whose interest rate may be revised in accordance with the change in another interest rate which serves as a benchmark rate, or those whose yield is determined by the change in stock market indices or the indices of other secondary securities markets which, as in the past, remain liberalised.

The need for prior authorisation is lifted in the only case in which it was provided for, i.e. for issues with maturity of more than 18 months with any of the following characteristics:

1. No explicit return (e.g. zero-coupon bonds).

2. A mixed return, provided that the actual explicit annual return is less than the benchmark rate in force for each issue.

3. An explicit return (coupons) payable at intervals of more than one year.

When these types of issues are made and there is an obligation to register the prospectus with the CNMV, the latter shall send a copy of the same to the tax authorities. The CNMV shall also inform the tax authorities of the result of the allotment procedure and the dispersion of the placement, as well as of any changes in the characteristics of the securities already issued.

6. PROSPECTUSES FOR USE IN ISSUES OR PUBLIC OFFERINGS OF SECURITIES

Royal Decree 2590/1998 of 7 December 1998 (25) on changes to the legal regime for the securities markets made important changes to the regulation of issues and public offerings of securities. Among the changes, in relation to the primary market, one of the most important concerns prospectuses. A new form of short-form prospectus, called a *short-form programme prospectus,* was introduced and the minimum content of prospectuses established. The latter may vary according to the type of securities to be issued, the characteristics of the issuing entity, the amount of the issue and any other circumstances that justify a difference. In both cases, the CNMV was authorised to adapt the content of these prospectuses to the special characteristics of the issuer, in order to facilitate the placement of securities on the primary market on comparable conditions to those in other EU countries.

The CNMV, exercising this power, has published *Circular 2/1999 of 22 April 1999* (BOE of 30 April 1999), which implements the new abridged programme prospectus and modifies certain types of prospectus currently regulated to adapt them to the special characteristics of the issues.

One notable change is the possibility that the CNMV may require, in certain circumstances, and for all forms of prospectus provided for in this provision, an introductory chapter (Chapter 0), to highlight the most important circumstances and the specific risks of the issuer offering securities. Also, a new format is introduced for Chapter 1, relating to the persons who assume the responsibility for the content of the prospectus and the relevant supervisory bodies, applicable to all forms of prospectus which issuers of equities, fixed income or warrants envisaged in this Circular may use.

As an alternative to the traditional short-form prospectus (designed for a specific issue) the short-form programme prospectus can cover the plan for issues or offerings – generally, issues of private fixed income – which a single

(23) See "Regulación financiera: cuarto trimestre de 1989", in *Boletín económico,* Banco de España, January 1990, p. 39.

(24) See "Regulación financiera: cuarto trimestre de 1992" in *Boletín económico,* Banco de España, January 1993, p. 75.

(25) See note 3.

entity intends to make during the following 12 months. Thus, each time the entity decides to make an issue envisaged in the plan, it will not have to publish a new short-form prospectus, but simply to file supplementary information with the CNMV at the time of the issue. The CNMV has introduced two kinds of programme prospectus for fixed-income issues: one for non-convertible and non-exchangeable fixed-income securities (simple fixed income) and the other for warrants.

The Circular also modifies other types of prospectus to adapt them to the special circumstances of simple fixed-income issues, and it clarifies the type and content of other forms of prospectus applicable both to equities and fixed-income securities in general.

In particular, as regards the forms of prospectus for simple fixed income, the following are provided for:

a) An extended prospectus specifically for fixed income, the content of which is more limited and less extensive than that of the incomplete prospectus regulated in the Ministerial Order of 12 July 1993, which can only be used by issuers who issue exclusively fixed-income securities.

b) An extended prospectus specially for public-sector entities (which may be used by domestic or foreign public-sector bodies, international agencies of a public nature and foreign states) which are not exempt from the legal requirement to prepare and file a prospectus.

c) A short-form prospectus for the issue or offering of simple fixed income securities which modifies the short-form prospectus used until now for this kind of issuer and extends the benefits of the reform to those who because they issue sporadically cannot take advantage of the programme prospectus system.

d) A short-form programme prospectus for simple fixed-income securities and a short-form programme prospectus for warrants.

Thus, besides clarifying the type and content of the forms of prospectus for the issue and public offering of both fixed-income and equity securities, the CNMV has established a new regime for the issuance of fixed-income securities, which is much more rapid and efficient than the one currently in force, in order to help increase the financing possibilities for numerous firms in the Spanish market.

7. PORTFOLIO INVESTMENT INSTITUTIONS: CHANGES TO "FONDTESOROS"

The Ministerial Order of 7 June 1990 (26), amended by the Ministerial Order of 25th January 1994 (27), authorised the Ministry of Economy and Finance, through the Directorate General of the Treasury and Financial Policy, to enter into standard-form co-operation agreements with the Management Companies of Portfolio Investment Institutions for the creation of Securities Funds and Money-Market Funds to invest in public debt (hereafter "FONDTESOROs"). Also, the Treasury undertook to grant, during the term of the agreements, use of the trademark "FONDTESORO" and of its logotypes, in order to facilitate the marketing of the funds.

The Ministerial Order of 10 June 1997 (28) on the financial operations of Portfolio Investment Institutions in financial derivatives, opened up the possibility for such institutions to enter into contracts for derivatives not traded on any organised secondary market. Recently, the Ministerial Order of 28 May 1999 on agreements for the promotion of asset securitisation funds (commented on below) provides for the creation of funds which, under the trade name "FT-Pyme", will specialise in the securitisation of loans to productive firms, with part of their liabilities (within the principal tranche of fixed-income securities) enjoying a state guarantee.

In order for FONDTESOROs to be able to benefit from the use of such instruments for the management of their portfolios, the *Ministerial Order of 28 May 1999* has been published. It partially amends the Ministerial Order of 7 June 1990 on co-operation agreements relating to FONDTESOROs, enabling these mutual funds to invest in that part of the assets issued by "FTPymes" covered by the state guarantee and, also, to enter into contracts for derivative instruments not traded on any organised secondary market.

Likewise, and in order to widen the range of financial assets in which they can invest their funds, it has been considered appropriate to permit a percentage of their portfolio to be invested in other fixed-income assets, provided that they enjoy a high credit rating. Finally, in the

(26) See "Regulación financiera: segundo trimestre de 1990" in *Boletín económico,* Banco de España, July-August 1990, pp. 80 and 81.

(27) See "Regulación financiera: primer trimestre de 1994" in *Boletín económico,* Banco de España, April 1994, p. 93.

(28) See "Regulación financiera: segundo trimestre de 1997" in *Boletín económico,* Banco de España, July-August 1997, pp. 111-113.

case of newly created FONDTESOROs, this Order authorises investment of up to a certain percentage of their portfolio in equity securities.

Thus, the Order in question makes three new investment possibilities available both to newly created FONDTESOROs and those others which, having an agreement in force, wish to modify their investment policy in order to extend the variety of financial instruments in which they can invest their funds. They are the following:

— *FONDTESORO RENTA FIM:* whose portfolio must be invested (save for the part to cover the liquidity ratio), principally, in government debt, in any of its forms, or in bonds issued by FTPymes which enjoy a state guarantee. These investments must account for no less than 70 % of the assets of the fund. Likewise, at least 50 % of their assets shall be invested outright in government bonds, or the like, with an original maturity of more than one year, and they may invest a maximum of 20 % of their total assets in other fixed-income securities (other than government debt) that are traded on a Spanish organised secondary market and have a high credit rating. Finally, they may trade on forward markets or markets for financial derivatives solely in order to hedge the financial risks of their portfolios.

— *FONDTESORO PLUS FIM:* whose portfolio must have the same composition as above, except for the final percentage. Thus, this type of FONDTESORO may invest a maximum of 20 % of its total assets in the equity securities on which the IBEX-35 index is based and in other fixed-income securities (other than government debt) that are traded on a Spanish organised secondary market and have a high credit rating. They may also trade on forward markets and markets for financial derivatives solely in order to hedge the financial risks of their portfolios.

— *FONDTESORO RENTA FIAMM:* whose portfolio must be invested (save for the part to cover the liquidity ratio), principally, in government debt, in any of its forms, or in bonds issued by FTPymes which enjoy a state guarantee. These investments must account for no less than 80 % of the assets of the fund. Likewise, at least 60 % of their assets shall be invested in government debt in any of its forms with a residual maturity not exceeding the limits laid down in current legislation (at the moment, eighteen months), and they may invest a maximum of 10 % of their total assets in other fixed-income securities (other than government debt) that are traded on a Spanish organised secondary market, have a high credit rating and have a residual maturity not exceeding the limits established in current legislation. Finally, they may also trade on forward markets or markets for financial derivatives, for the sole purpose of hedging the financial risks of their portfolio.

8. ASSET SECURITISATION FUNDS: PROMOTIONAL AGREEMENTS (FTPYMES)

Royal Legislative Decree 3/1993 of 26 February 1993 (29) on urgent budgetary, tax, financial and employment measures and additional provision five of Law 3/1994 of 14 April 1994, whereby the Second Banking Co-ordination Directive was introduced into Spanish law, authorised the government to extend the regime established in Law 19/1992 of 7 July 1992 (30) for mortgage securitisation funds, with suitable adaptations, to the securitisation of other loans and creditors' rights, including those arising under leasing transactions, and those relating to the activities of small and medium-sized firms, to be known as asset securitisation funds. The government, exercising this power, issued Royal Decree 926/1998 of 14 May 1998 regulating asset securitisation funds and their management companies, establishing the reference framework for asset securitisation in Spain.

Recently, Law 49/1998 of 30 December 1998 (31) on the 1999 State Budget, has empowered the Ministry of Economy and Finance to give guarantees for fixed-income securities issued by asset securitisation funds set up under the agreements which would be entered into by the said Ministry with their management companies and, at the same time, to establish rules and requirements for such agreements.

The *Ministerial Order of 28 May 1999* (BOE 4 June 1999) has been published to execute this provision. It establishes the regime for and content of the promotional agreements which the Ministry of Economy and Finance (through the Directorate General of the Treasury and Financial Policy (DGTPF) may enter into with the management companies of asset securitisation funds. The purpose of such agreements is to

(29) See "Regulación financiera: primer trimestre de 1993" in *Boletín económico,* Banco de España, April 1993, p. 96.

(30) See "Regulación financiera: segundo trimestre de 1992" in *Boletín económico,* Banco de España, July-August 1992, pp. 93 and 94.

(31) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, p. 109.

promote the creation of asset securitisation funds which, under the trade name "FTPyme", may benefit from state guarantees for the fixed-income securities they issue, in order to support the financing of business.

Management companies seeking to enter into such agreements shall file an application with the DGTPF, submitting a report explaining their plans to set up an FTPyme. This step shall be carried out quite separately from the formalities subsequently required by the CNMV under current regulations. To this end, in addition to observing the general provisions of the relevant legislation, they shall fulfil the following requirements:

1. As regards their assets, loans or credits granted by credit institutions which have signed the agreement executed with the Ministry of Economy and Finance may be securitised. Such loans or credits must fulfil the conditions stipulated in that agreement.

2. As for liabilities, the percentages of the nominal value of each series or class of fixed-income securities issued by asset securitisation funds which may be guaranteed are specified in the annex to the Order.

3. There must be a credit improvement which reduces the risk of the guaranteed securities, so that they are granted a minimum credit rating by a credit rating agency recognised by the CNMV. This rating must be obtained prior to the final grant of the guarantee.

4. Finally, all the securities issued by the asset securitisation funds belonging to the series or classes guaranteed by the state must be traded, even when the guarantee only covers a proportion of the series or class, on an official Spanish secondary securities market.

Lastly, the Order's annexes contain details of the standard co-operation agreement for the creation of FTPymes to be entered into by the DGTPF and the management companies, as well as of the framework co-operation agreement between the Ministry of Economy and Finance and credit institutions, determining which credits may be assigned to FTPymes, set up to support the financing of business.

9. REAL-ESTATE INVESTMENT INSTITUTIONS

The basic regulation of Portfolio Investment Institutions is contained in Law 46/1984 of 26 December 1984 (32), and in its implementing regulations, i.e. Royal Decree 1393/1990 of 2 November 1990 (33). Subsequently, both pieces of legislation were amended, by Law 19/1992 of 7 July 1992 (34) and Royal Decree 686/1993 of 7 May 1993 (35), respectively, to incorporate the regulation of real-estate investment institutions (real-estate investment companies and mutual funds), establishing their financial characteristics, and the tax and sanctioning regimes applicable to them. Later, the Ministerial Order of 24 September 1993 (36) completed the legislation regulating these institutions, and specified the significant role to be performed by management and appraisal companies and the custodian in their affairs.

The precautionary measures established in these provisions involved certain rigidities that made these instruments unattractive compared to other forms of portfolio investment. These limitations were overcome by Law 20/1998 of 1 July 1998 (37) on reform of the legal and tax regime for real-estate investment institutions and on the assignment of certain creditors' rights of central government, which amended Law 46/1984, introducing greater flexibility into their investment policy and greater tax incentives.

It was then necessary to amend Royal Decree 1393/1990, to adapt the regulations to the provisions of Law 20/1998, and this has now been done through *Royal Decree 845/1999 of 21 May 1999* (BOE of 4 June 1999).

Of the main changes introduced, it is worth highlighting the new investment options available to real-estate investment institutions. Until now real-estate investment institutions could only invest in completed buildings for rental, or in separate parts of them, to be used for housing, offices, car parks or commercial premises. Now, under this Law, they may also invest in buildings under construction, purchase options and commitments to purchase buildings by in-

(32) See "Regulación financiero: cuarto trimestre de 1984", in *Boletín económico,* Banco de España, January 1985, pp. 41-43.

(33) See "Regulación financiera: cuarto trimestre de 1990", in *Boletín económico,* Banco de España, January 1991, pp. 30 and 31.

(34) See note 23.

(35) See "Regulación financiera: segundo trimestre de 1993", in *Boletín económico,* Banco de España, July-August 1993, pp. 104 and 105.

(36) See "Regulación financiera: tercer trimestre de 1993", in *Boletín económico,* Banco de España, October 1993, pp. 77-79.

(37) See "Financial regulation: second quarter of 1998", in *Economic bulletin,* Banco de España, July 1998, pp. 89-90.

stalments, provided that their maturity does not exceed two years, title to administrative licences which allow buildings to be rented, as well as buildings to be used as residences for students and the elderly. In all cases, these types of business shall be exploited through rental.

As against the current regime of a complete ban on transactions with shareholders and group companies, some are permitted, subject to certain limits and conditions. Thus, real-estate investment institutions' shareholders and group companies may be lessees or hold rights, other than those arising from their shareholder status, with respect to the property which makes up the assets of the institutions, provided that no conflict of interests arises therefrom, and that arm's-length prices and conditions apply to the relevant contracts. The same provisos shall be applicable to any purchase or sale of property where the other party is a shareholder. These provisions shall also apply in the case of persons or entities having links with shareholders, and property rented to such persons or entities may not, under any circumstances, exceed 25 % of the assets of real-estate investment institutions. As regards the contributions of shareholders to the capital or net worth, these may take the form of, besides cash, real estate or securities.

Real-estate investment institutions may also finance the acquisition of property and its refurbishment through mortgages, provided that the outstanding balance of borrowing does not exceed 50 % of the assets of the institution. Finally, they may acquire property from entities of the same group, or which belong to the group of their management company, provided that they are newly built and that certain other requirements are fulfilled.

As regards the rules governing their investments, real-estate investment companies shall invest at least 90 % of the annual average of the monthly balances of their assets in real estate with the above-mentioned characteristics. The rest may be invested in fixed-income securities traded on organised secondary markets, as well as in such equities as may be determined by the Ministry of Economy and Finance. Real-estate investment funds shall invest at least 70 % of the annual average of the monthly balances of their assets in real estate. Also, they shall maintain a liquidity coefficient of at least 10 % of the total assets of the previous month, in the form of cash, deposits, sight accounts or assets with a residual majority of less than 18 months. Of this coefficient, up to 5 % of total assets may take the form of such equities as may be determined by the Ministry of Economy and Finance. The remaining percentage of the assets may be invested in fixed-income securities traded on organised secondary markets. In both cases, these institutions may not acquire any single asset representing more than 35 % of their total assets.

As regards the tax regime for these institutions, that provided for in Law 20/1998 is introduced. Thus, corporate income tax shall be levied at a rate of 1 %, provided that investments in any type of urban property for rental account, during the tax period as a whole, for at least 50 % of their assets (investments in housing and residences for students and the elderly count for these purposes). In the case of property under construction, it must be registered in the Property Registry. Finally, the minimum period for which properties must be held by the institutions is reduced from four to three years, save where, exceptionally, the institution has the express authorisation of the CNMV.

The Royal Decree in question also amends Royal Decree 1343/1992 of 6 November 1992 (38), implementing Law 13/1992 of 1 June 1992 (39) on shareholders' equity and supervision on a consolidated basis of financial institutions. Thus, as regards the weighting of risk elements for the calculation of the solvency coefficient, the mortgage market fixed-income securities envisaged in Law 2/1981 of 25 March1981 on the mortgage market are introduced with a weighting of no less than 10 % (previously 50 %). Finally, certain changes are made to Royal Decree 1732/1998 of 31 July 1998 (40) on the fees applicable to the activities and services provided by the CNMV.

10. RISK-CAPITAL INSTITUTIONS: AUTHORISATION OF NEW INSTITUTIONS, ACCOUNTING RULES AND INFORMATION OBLIGATIONS

Certain amendments have been made to the legal regime for risk-capital institutions, initially contained in Royal Legislative Decree 1/1986 of 14 March 1986 (41) on urgent administrative, financial, tax and employment measures, to

(38) See "Regulación financiera: cuarto trimestre de 1992, in *Boletín económico,* Banco de España, January 1993, pp. 65-71.

(39) See "Regulación financiera: segundo trimestre de 1992", in *Boletín económico,* Banco de España, July-August 1992, pp. 82-86.

(40) See "Financial regulation: third quater of 1998" in *Economic bulletin,* Banco de España, October 1998, pp. 79-80.

(41) See "Regulación financiera: primer trimestre de 1986", in *Boletín económico,* Banco de España, April 1986, pp. 31 and 32

adapt its provisions to current circumstances. Law 1/1999 of 5 January 1999 (42) established a stable and complete legal framework for these institutions, laying the foundations for them to continue promoting and fostering small and medium-sized non-financial firms, which engage in activities relating to technological innovation or others through the acquisition of temporary holdings in their capital.

This Law authorises the Ministry of Economy and Finance to determine, for each type of risk-capital institution (according to their specialities), the requirements and forms to apply for authorisation, as well as the documents which must accompany such applications. It is also authorised to establish and modify the accounting rules and the information which both the risk-capital institutions and their management companies must provide to the CNMV.

The *Ministerial Order of 17 June 1999* (BOE of 30 June 1999) has been published pursuant to this power. It partially amends Law 1/1999, authorising the CNMV to issue provisions in relation to the procedure for the authorisation of new institutions, and to determine the accounting rules and the formats for the annual accounts, in order to adapt them to the prolonged period of maturity of the investments which they make, incorporating a specific section containing information on the fulfilment of coefficients and information deriving from the financial supervision to which they are subject. It is also authorised to determine the content, frequency and scope of the information (in particular, on activities, investments, funds, net-worth, financial statements, shareholders and the economic/financial situation) which these institutions and their management companies must supply to the said Commission.

11. THE NEW LEGAL REGIME FOR CAPITAL MOVEMENTS AND FOREIGN INVESTMENT

Directive 88/361/EC of 24 June 1988 liberalised capital movements between residents in Community states, establishing a transitional period of application for Spain, which ended on 31 December 1992. However, the Spanish economic situation and the growing internationalisation of economic activity made it possible to bring forward the full liberalisation of cross-border transactions and transfers to February 1992, through Royal Decree 1816/1991 of 20 December 1991 (43). That royal decree was subsequently adapted to the new liberalised context by means of Law 18/1992 of 1 July 1992 (44), its implementing regulations being issued by Royal Decree 671/1992 of 2 July 1992 (45) on foreign investment in Spain and Royal Decree 672/1992 of 2 July 1992 (46) on Spanish investment abroad.

The Treaty on European Union, signed by Spain on 7 February 1992 (47), established full freedom of movement of capital. However, it authorised the Member States to impose or maintain administrative requirements for the liberalised transactions, for two basic reasons: to allow administrative, statistical or economic monitoring of such operations and to allow the adoption of measures justified by reasons of public order and security.

The purpose of the above-mentioned royal decrees was to incorporate the provisions of Directive 88/361 into Spanish law. However, this directive was subsequently superseded by the provisions of the Maastricht Treaty on the freedom of capital movements, which translated into a system characterised by the absence of administrative controls of a prior nature, unless, pursuant to the safeguard clauses, they affected national interests.

Royal Decree 664/1999 of 23 April 1999 (BOE of 4 May 1999) on foreign investment has now been published to ensure that Spanish law is fully adjusted to the provisions of the Maastricht Treaty. This establishes, generally, the freedom of both incoming and outgoing capital movements.

The Royal Decree combines in a single piece of legislation the regulation of foreign investment in Spain and Spanish investment abroad, both being fully liberalised, at the same time as it repeals the above-mentioned Royal Decrees 671/1992 of 2nd July 1992 and 672/1992 of the same date. All this is without prejudice to the special regimes affecting foreign investment in Spain that are contained in specific sectoral legislation.

(42) See "Financial regulation: fourth quarter of 1998" in *Economic bulletin,* Banco de España, January 1999, pp. 100 and 101

(43) See "Regulación financiera: cuarto trimestre de 1991", in *Boletín económico,* Banco de España, January 1992, pp. 58-60.

(44) See "Regulación financiera: segundo trimestre de 1992" in *Boletín económico,* Banco de España, July-August 1992, pp. 87-89.

(45) See previous note.

(46) See "Regulación financiera: segundo trimestre de 1992", in *Boletín económico,* Banco de España, July-August 1992, pp. 89 and 90.

(47) See "Regulación financiera: cuarto trimestre de 1992", in *Boletín económico,* Banco de España, January 1993, p. 72.

The main change introduced by the Royal Decree is the establishment of an ex-post administrative step consisting of a general declaration of investments for administrative, economic and statistical purposes, while the prior verification and authorisation procedures required until now are dispensed with. However, in certain cases of investment made from territories or countries classified by current Spanish law as *tax havens,* a prior declaration is required in addition to the declaration mentioned above.

With respect to *foreign investment in Spain,* it is worth mentioning that the traditional categories into which investment used to be classified (direct, portfolio, real-estate, and other forms of investment) are replaced by a specific list of operations considered to be foreign investment:

1. The taking of holdings in Spanish firms.

2. Establishing and increasing capital endowments of branches.

3. The subscription for and acquisition of marketable debt securities issued by residents.

4. The acquisition of shares in mutual funds registered with the CNMV.

5. The acquisition of property situated in Spain, for a total amount exceeding ESP 250 million (or the euro equivalent), or when, irrespective of the amount, it comes from a tax haven.

6. The creation, execution or participation in joint ventures, foundations, economic interest groupings, co-operatives and co-ownership, when the total value of the share of the foreign investors exceeds ESP 500 million (or the euro equivalent), or when, irrespective of the amount, it comes from a tax haven.

As regards its declaration, generally the investment shall be declared by the non-resident investor after it has been made, merely for administrative, statistical or economic purposes. Non-resident investors shall send to the Investment Registry of the Ministry of Economy and Finance information on such operations within such period and with such content as may be established by the rules implementing this decree. As an exception to the general rule, in the case of investments made from tax havens, investors must also make a declaration prior to making the investment.

Marketable securities (issued or offered publicly and traded on a secondary market) are a special case. Here, the *financial institutions* whose activity is the custody or administration of securities represented by means of book-entries that are the object of the investment, or the firms whose intervention is necessary for the subscription or transfer of securities, in accordance with the rules applicable, are obliged to make the declaration. In the event that the investment is in securities that are not traded on secondary markets, but the parties have deposited or registered such securities voluntarily, the entity obliged to make the declaration shall be the entity which is the custodian or administrator of the same, unless a firm, securities agency or credit institution has intervened in the transaction, in which case it shall be responsible for making the declaration. In the case of bearer shares, the person obliged to declare shall be the Spanish firm in which the investment is made, and finally, investments in mutual funds shall be declared by the management company of the fund.

As regards the *regime for Spanish investment abroad,* it is somewhat similar to the above regime. Thus, the following operations are considered Spanish investment abroad:

1. The taking of holdings in foreign companies.

2. Establishing and increasing capital endowments of branches.

3. The subscription for and acquisition of marketable debt securities issued by non-residents.

4. The acquisition of shares in foreign mutual funds.

5. The acquisition of property situated abroad, for a total amount exceeding ESP 250 million (or the euro equivalent), or when, irrespective of the amount, the investment is in a tax haven.

6 The creation, execution or participation in joint ventures, foundations, economic interest groupings, co-operatives and co-ownership, when the total value of the share of the resident investors exceeds ESP 250 million (or the euro equivalent), or when, irrespective of the amount, the investment is in a tax haven.

Likewise, Spanish investments abroad shall be declared, generally by the resident investor after the investment has been made, for the same administrative, statistical or economic purpose. As an exception to the foregoing, only in the case of investment where the host is a

tax haven is a declaration also required prior to the making of the investment.

Investments in marketable securities made through investment services companies, credit institutions or any other resident entities engaging in any of the activities of the former, which act for the account and at the risk of the investor as the intermediary holder of such securities shall be declared to the Investment Registry by such entities.

As an exception to the liberalising regime, the Royal Decree establishes those cases in which prior clearance of the investment is necessary. Investments which by their nature affect or may affect – even occasionally – activities relating to the exercise of public power or activities which affect or may affect public order, security, and public health, require prior administrative authorisation by the Council of Ministers, upon the proposal of the Ministry of the Economy and Finance and the department affected.

Similarly, foreign investment in Spain in activities directly relating to national defence, and those in the production or distribution of arms, munitions, explosives or war material, also requires the prior authorisation of the Council of Ministers, upon the proposal of the Ministry of Defence. In the case of listed companies engaging in such activities, only acquisitions by non-residents of more than 5 % of the share capital of the Spanish company, or of holdings which, although smaller, entitle the investor to direct or indirect representation on the board of directors, shall require authorisation.

12. MODIFICATION OF THE LEGAL REGIME OF THE OFFICIAL CREDIT INSTITUTE

State-capital credit institutions (formerly, official credit institutions) and the Official Credit Institute have undergone notable legal and operational changes in recent years. In 1991, pursuant to Royal Legislative Decree 3/1991 of 3 May 1991 (48) and Law 25/1991 of 21 November 1991, overhaul of the whole model of official Spanish credit was undertaken, in order to expand lending activity and to eliminate certain barriers limiting the potential to compete on the single European financial market. Corporación Bancaria de España, S.A., a state-owned institution with 100 % state capital – today known as Argentaria – was set up. Subsequently, it brought under one umbrella the official credit institutions, the Caja Postal de Ahorros and Banco Exterior. As part of this process the status of the Official Credit Institute was changed to that of a state-owned public limited company and credit institution, attached to the Ministry of Economy and Finance, and considered to be a State Financial Agency.

Subsequently, Royal Legislative Decree 12/1995 of 28 December 1995 (49) on urgent budgetary, tax and financial measures developed the legal and financial regime of the Official Credit Institute, in order to clarify and rationalise state official credit activity. This decree provided that one aspect of its legal regime that would have to be adapted was its statute, and it granted the government powers for such purpose.

Later, Law 6/1997 of 14 April 1997 on the organisation and operation of the general state administration established the aim of rationalising the institutional structure of state administration, with adaptation of the autonomous agencies and other public-law entities to such structure.

Royal Decree 706/1999 of 30 April 1999 (BOE of 13 May 1999) on the adaptation of the Official Credit Institute to the Law on the organisation and operation of the general state administration and approval of its statute has been published to comply with the legal requirements of the above-mentioned legislation. This decree contains the rules for adapting to Law 6/1997 and the text of the statute of the Official Credit Institute, as established by Royal Legislative Decree 12/1995, giving it the status of a public-sector business entity (it was formally considered to be a state-owned public limited company). It remains a credit institution, attached to the Ministry of Economy and Finance, and is still considered to be a State Financial Agency.

13. URGENT LIBERALISATION AND COMPETITION ENHANCEMENT MEASURES

The buoyancy of domestic demand as the driving force of economic growth has highlighted significant increases in the prices of certain sectors, especially those less exposed to foreign competition, obliging urgent measures to

(48) See "Regulación financiera: segundo trimestre de 1991", in *Boletín económico,* Banco de España, July-August 1991, pp. 60 and 61.

(49) See "Regulación financiera: cuarto trimestre de 1995", in *Boletín económico,* Banco de España, January 1996, p. 85.

be taken to avoid the emergence of inflationary pressures. In consequence, *Royal Legislative Decree 6/1999 of 16 April 1999* (BOE of 17 April 1999) has been published. It seeks to stimulate competition in the markets for goods, services and productive factors, and to contribute to the stability of the economy by improving resource allocation and making the opportunities of agents in these markets more equal.

First, with respect to the protection of competition, precautionary measures have been taken to prevent processes of modification of market structures resulting in an excessive increase in the degree of business concentration. For this purpose, a number of instruments have been introduced to improve the monitoring of business concentration operations and its efficacy. Specifically, notification to the *Servicio de Defensa de la Competencia* (Protection of Competition Service) – attached to the Ministry of Economy and Finance – has been made compulsory for those projects or operations where:

a) A share of 25 % or more of the domestic market, or a defined geographical market therein, for a particular product or service is acquired or increased.

b) The total sales in Spain of all the participants in the last accounting year exceeded ESP 40 billion, provided that at least two of the participants individually have a turnover of more than ESP 10 billion in Spain.

The Protection of Competition Service shall be notified prior to the operation or within one month of the date of conclusion of the concentration agreement. In transactions for the acquisition of listed shares, when a takeover bid is necessary the notification obligation shall be subject to a specific procedure to be determined in regulations.

As regards measures relating to attestation of documents, the fees of notaries public and land registrars are reduced for mortgages and house purchases. Also, the costs of registering companies in mercantile registries are reduced.

To make further headway in the deregulation of the gas sector, due to be fully deregulated in 2008, the levels of consumption required to gain access to the status of a wholesale consumer are reduced. Also, in view of the development of the natural gas sector and the desirability of promoting the entry of new distributors and stimulating competition, the period of exclusivity in a specific geographical area granted to the current authorised distributors is reduced.

In relation to the electricity sector, the far-reaching deregulation of the market, together with the decline in interest rates, the rise in electricity demand and the increase in competition, enable a further reduction to be made in the electricity tariff, which will particularly affect domestic consumers.

Finally, the prices of other basic products and services, such as medicines, the tariffs paid by toll-motorway users and telecommunications services, have been moderated and a number of measures have been introduced to stimulate competition in mobile telephony.

21.7.1999.