Financial regulation: third quarter of 1999

1. INTRODUCTION

As in the second quarter of 1999, relatively few provisions of a financial nature were introduced in the third quarter.

In relation to the Banco de España, first the amendment of the general clauses applicable to monetary policy operations as regards the effects of breach of obligations arising under such general clauses is highlighted. Second, with regard to the Central Credit Register *(Central de Información de Riesgos,* CIR), the medium or vehicle whereby reporting entities may request the information they require from the CIR is specified.

As regards the securities markets, three provisions are mentioned, two of which affect the government debt market. First, arrangements have been made for the first issue of ten-year cancellable notes, in order to continue the policy of diversifying the range of instruments for financing the government in the long-term segment. Second, the legal regime for Spanish-government-debt market makers was changed in order to preserve debt-market liquidity, which had been drying up as a consequence of the concentration of the business of derivatives on European government debt. Finally, as regards private securities markets, the information of a public nature which must be reflected in relation to transactions on the official securities markets has been determined, in order to continue improving market transparency.

As for currency-exchange bureaux, certain procedures have been automated and some minor clarifications, which experience has shown to be necessary, have been introduced into the law regulating them.

Electronic signatures have been regulated, given the growing need for greater legal certainty and integrity in internet-based communications in which this new medium is used.

Finally, a new legal framework has been created for co-operatives, based on European directives. It incorporates numerous changes made to Spanish company law in recent years.

2. BANCO DE ESPAÑA: MONETARY POLICY OPERATIONS

The Resolution of 11 December 1998 (1) of the Executive Commission of the Banco de Es-

(1) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, pp. 78-82.

paña (BE) specified the general clauses applicable to monetary policy operations executed by the BE from 1 January 1999, in accordance with the guidelines set by the European Central Bank (ECB). This resolution has recently been amended by the *Resolution of 23 July 1999 of the Executive Commission of the BE* (BOE [Official State Gazette] of 7 August 1999), to revise the circumstances and effects of breach by the entities of their obligations arising under these general clauses.

In this respect, the Resolution of 11 December provided for financial penalties (ranging from 10,000 to 1,000,000 euro together, under certain circumstances, with the suspension or exclusion of the counterparty in breach from access to monetary policy operations) in certain cases of breach by the counterparty in connection with tenders, the contractual instruments which regulate open market operations, end-of-day procedures and the use of collateral, or of breach of the obligations arising under the regulations in force on minimum reserves.

The Resolution of 23 July amended the above-mentioned financial penalty. Its amount shall now be determined by applying the ESCB marginal lending rate plus 2.5 percentage points to the amount obtained by applying the rules laid down in the resolution according to the nature of the breach. Thus, in the event that the counterparty fails to provide sufficient eligible assets for the settlement of its obligations arising out of the tender procedures, only that part of the bid allotted to the said counterparty that is actually covered by the aforesaid eligible assets shall be settled. The grounds for imposition of the penalty shall be that the counterparty is not capable of providing sufficient collateral on the settlement date. Penalties shall be imposed on the difference between the amount allotted and the adjusted market value of the collateral.

The penalty applicable to the first and second breach committed by a counterparty within a 12-month period, running from the first breach, shall be equivalent to the result of applying the ESCB marginal lending rate plus 2.5 percentage points to the difference between the amount allotted at auction to the counterparty and the adjusted market value of the collateral. If the resulting amount is less than 500 euro no penalty will be imposed.

In the event of a third breach within the 12 months following the first such breach, in addition to the corresponding financial penalties, a further penalty shall be imposed in accordance with the rules laid down in the resolution, consisting of the suspension of the counterparty in breach.

In cases of serious breach, taking into account the amounts of the operations, the frequency of the breach and the specific circumstances of the same, the exclusion of the counterparty from access to open market operations may be considered. Finally, in cases of force majeure – i.e. breach for reasons beyond the control of the counterparty – no penalty will be imposed.

3. CENTRAL CREDIT REGISTER

The Central Credit Register, organised by the BE in accordance with the provisions of Legislative Decree 18/1962 of 7 June 1962 on nationalisation and reorganisation of the Banco de España, began to operate in December 1963. Since then a number of reforms have been made. Specifically, the amendments of BE Circular 7/1989 of 24 February 1989 (now repealed) and BE Circular 3/1995 of 25 September 1995 (2) basically consisted in a widening of the reporting entities and the borrowers and credits reported, adapting the CIR to the changes which had occurred in the financial system. The last amendment was made by BE Circular 6/1998, of 29 May 1998 (3). It modified the amendment of 1995 to redefine certain concepts and introduce some reforms in order to improve the information provided by the CIR.

Recently, *BE Circular 8/1999 of 27 July 1999* (BOE of 7 August 1999), due to be effective as of 1 November 1999, filled a gap in BE Circular 3/1995, which had failed to specify the medium or vehicle for applying for the information which the reporting entities require from the CIR. In this respect, BE Circular 8/1999 specifies that such applications shall be made in accordance with the format set out in the Annex to the Circular, in a magnetic medium or by computer links, given that the increase in their numbers has made it advisable to restrict the use of paper (4). Finally, the applications shall be accompanied by an express declaration by the applicant that it has the authorisation of the borrowers as required by such Circular.

4. GOVERNMENT DEBT: ISSUANCE OF CANCELLABLE 10-YEAR NOTES

Pursuant to the powers granted by the Budget Law, the consolidated text of which was ap-

(2) See "Regulación financiera: cuarto trimestre de 1995", in *Boletín económico,* Banco de España, January 1996, p. 82.

(3) See "Financial regulation: second quarter of 1998", in *Economic bulletin,* Banco de España, July 1998, p. 84.

(4) Only applications relating to more than five holders will be admitted on paper.

proved by Royal Legislative Decree 1091/1988 of 23 September 1988, the Ministry of Economy and Finance has in recent years been expanding and modifying the range of instruments and techniques used by the Directorate General of the Treasury and Financial Policy ("the Treasury") in order to improve and boost the government debt market and at the same time, to facilitate its funding policy in the market. It is also empowered to issue or redeem debt, to establish its representation, maturity, interest rate and other features, as well as, where applicable, to execute such operations. These powers are delegated to the Treasury by a Ministerial Order of 27 January 1999 (5), which makes arrangements for the creation of government debt during 1999 and January 2000.

Making use of this prerogative and in order to diversify the range of government funding instruments in the long-term segment, the *Resolution of 9 August 1999* (BOE of 11 August 1999) was published. This arranged for the first issue of euro-denominated ten-year cancellable notes ("the notes"), with a face value of 500 million euro, to be made on 10 August 1999.

The maturity date of the notes is 10 August 2009, they have a nominal interest rate of 4.78 % per annum and coupons are payable annually in arrears (the first payable on 10 August 2000). Investors shall be entitled to redeem their securities early, on 10 August 2003, 2005 and 2007, with repayment at less than face value (96.1 %, 96.4 % and 98.03 % respectively). To do so they will have to give notice of their desire to redeem them ten business days (according to the "TARGET calendar") prior to the respective redemption date. Finally, a minimum trading amount of 1,000 euro is established.

5. GOVERNMENT DEBT: CHANGES TO THE REGULATION OF "MARKET MAKERS"

The Ministerial Order of 10 February 1999, implemented by the Resolution of 11 February 1999 of the Directorate General of the Treasury and Financial Policy (DGTPF) (6), established the basic principles, as well as the rights and obligations of Spanish government-debt market makers.

Fulfilment by market makers of their commitments has enabled the debt market to remain highly liquid in the new environment defined by the EU. However, in recent months there has been a considerable loss of liquidity in the Spanish government-debt futures market as a consequence of the concentration of the European government-debt derivatives business.

The substitution of national-bond futures by a contract on another bond poses problems for its use as a hedging instrument in the national spot market. This situation warrants the search for ways of recovering the natural hedging of Spanish bonds (the Spanish-bond future), since lack of liquidity reduces the interest of members which, in turn, leads to further losses of liquidity.

To this end, the *Resolution of 23 July 1999* of the DGTPF (BOE of 28 July 1999), which amends that of 11 February 1999, has been published. The new resolution releases market makers with permanent establishments in Spain from the obligation of quoting one of the two benchmark bonds with residual maturity of over eight years.

At the same time, it requires them to continue to quote the 10-year notional MEFF bond during 60 % of the market session with a maximum bid-offer spread of 10 ticks (i.e. ten basis points) and a minimum of forty contracts for each position. Breach of this obligation for six consecutive months shall be a ground for withdrawal of market-maker status, in accordance with the Resolution of 11 February 1999.

6. CURRENCY-EXCHANGE BUREAUX

Law 13/1996 of 30 December 1996 (7) on fiscal, administrative and social measures, which accompanied the 1997 Budget Law, established, inter alia, the sanctioning regime applicable to the owners of currency-exchange bureaux, other than credit institutions, as well as to their directors and managers, similar to the legislation in other European countries. Subsequently, Royal Decree 2660/1998 of 14 December 1998 (8) implemented the law through regulations and modified the legal regime of these bureaux, making important changes to the powers of the BE, which had until then been regulated in BE Circular 8/1992 of 24 April 1992 (9).

(5) See "Financial regulation: first quarter of 1999", in *Economic bulletin,* Banco de España, April 1999, p. 63.

(6) See "Financial regulation: first quarter of 1999", in *Economic bulletin,* Banco de España, April 1999, pp. 60-62.

(7) See "Regulación financiera: cuarto trimestre de 1996", in *Boletín económico,* Banco de España, January 1997, p. 115.

(8) See "Financial regulation: fourth quarter of 1998", in *Economic bulletin,* Banco de España, January 1999, pp. 99 and 100.

(9) See "Regulación financiera: segundo trimestre de 1992", in *Boletín económico,* Banco de España, July-August 1992, p. 91.

Later, the BE Resolution of 6 April 1999 published Internal Circular 1/1999 of 6 April 199 on currency-exchange bureaux, which developed, inter alia, the obligations of the authorused entities to submit information to the BE, as well as the responsabilities of the various internal departments of the BE in the area. Likewise, it delegated powers to authorise new entities to the branches of the BE.

Recently, the BE *Resolution of 27 Septem - ber 1999* (BOE of 4 October 1999) published Internal Circular 4/1999 of 27 September 1999 on currency-exchange bureaux, which makes certain changes to the previous Internal Circular in order to adapt the computer application "ROC" *(Registro de Oficinas de Cambio de Moneda)* to the new requirements of Royal Decree 2660/1998. This has automated certain procedures that were previously carried out manually and permits the branches of the BE to manage most of the data of the owners.

7. RULES ON TRANSPARENCY IN THE OPERATIONS OF OFFICIAL SECURITIES MARKETS

Royal Decree 629/1993 of 3 May 1993 (10) on rules for acting in the securities markets and compulsory registrations, implemented by the Ministerial Order of 25 October 1995 (11) and CNMV Circular 1/1996 de 27 March 1996 (12), laid down certain minimum rules of conduct for all persons operating on securities markets, based on EU recommendations and directives, which involved a significant step towards securing the transparency of all participants in such markets.

Subsequently, Law 37/1998 of 16 November 1998 (13) reformed the Securities Market Law 24/1988 of 28 July 1988 (14) in order to incorporate Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field into Spanish law. In order to secure market transparency, it provides that the National Securities Market Commission (CNMV), the Banco de España or the market regulatory bodies shall determine, within such limits as may be established by regulations, the information of a public nature on market operations which it shall be compulsory to disclose.

Pending its implementation in regulations, the CNMV has promulgated *CNMV Circular 3/1999 of 22 September 1999* on the transparency of operations on official securities markets (BOE of 1 October 1999), since it is essential to determine the minimum information that must be published on operations carried out on official securities markets (15), in accordance with the minimum requirements laid down in the Directive 93/22/EEC.

The Circular regulates the information of a public nature that stock markets, official futures and options markets and the AIAF fixed-income market must disclose on (both ordinary and extraordinary) market operations, as well as, where applicable, the orders made on the same.

The *stock market regulatory companies* shall publish, in daily turnover bulletins or through other appropriate media, certain information which is set out in the Circular, according to the type of operation to be carried out. The Circular thus regulates the information which must be published on ordinary operations (both on orders made and operations executed); on equity operations carried out through floor trading; on operations carried out on the electronic fixed-income market; on special stock market operations and on extraordinary operations.

The *regulatory companies of official futures and options markets* shall publish, in real time and for each contract and open maturity and series, where applicable, the cumulative volume for each of the three best bid and offer proposals. As regards operations executed, the price, volume and time of execution of all operations carried out during the session shall be indicated and, as regards open positions, the volume thereof.

Finally, with regard to operations executed in the AIAF fixed-income market, the volume contracted in each issue traded, the latest price and IRR shall be reported in real time, except for short-term assets (promissory notes) for which only the latest volume contracted and IRR shall be published.

(10) See "Regulación financiera: segundo trimestre de 1993", in *Boletín económico,* Banco de España, July-August 1993, p. 91.

(11) See "Regulación financiera: cuarto trimestre de 1995", in *Boletín económico,* Banco de España, January 1996, pp. 85 and 86.

(12) See "Regulación financiera: primer trimestre de 1996", in *Boletín económico,* Banco de España, April 1996, pp. 130 and 131.

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

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

(15) This Circular is not applicable to operations in the government-debt market.

8. ELECTRONIC SIGNATURE

Given the progress in telecommunications in recent years and the increase in so-called electronic business, there has been a growing demand for the regulation of electronic signatures, in order to give the use of this new medium greater legal certainty and completeness. A draft directive to establish a common framework for electronic signatures is being debated in the European Union and Spain is a very active participant in this debate.

Respecting the content and the common position of the aforementioned directive, and anticipating its promulgation, *Royal Legislative Decree 14/1999 of 17 September 1999* (BOE of 18 September 1999) on electronic signatures has been published. It establishes a clear regulation of the latter, giving them legal effectiveness, and it specifies the regime applicable to certification service providers. It also determines the register in which certification service providers will have to be registered and the regime for administrative inspection of their activity, it regulates the issuance and loss of efficacy of the certificates and it defines the infringements and sanctions that are provided for to secure its performance.

An electronic signature is defined as data in electronic form attached to, or logically associated with, other electronic data, which serves as a means of formally identifying the author or authors of the document in which it is contained. An electronic signatures is "advanced" if it is capable of identifying the signatory (16), has been created using means that the signatory can maintain under his sole control and is linked to the data to which it relates in such a manner that any subsequent change of the data is detectable.

As to their legal effects, advanced electronic signatures, provided that they are based on a qualified certificate (17) and that they have been created by a secure signature creation device, shall have the same legal effects as a hand-written signature in relation to paper-based data and shall be admissible as evidence in legal proceedings, being valued according to the consideration criteria established in procedural rules.

An advanced electronic signature shall be presumed to fulfil the conditions necessary to produce the effects indicated, when the qualified certificate on which it is based has been issued by an accredited certification service provider (18) and when the secure signature creation device is certified.

The provision of certification services is not subject to prior authorisation and is carried out under a freely competitive regime. No restrictions may be placed on certification services originating in another EU Member State.

The creation of the Register of Certification Service Providers ("the Register") at the Ministry of Justice should be highlighted. All such providers established in Spain shall have to apply, prior to the commencement of their activity, for registration, which will be regulated in the appropriate regulations. The Registry shall be public and shall keep permanently up to date and available to the public, a list of the entities registered, their names or business names, their internet page or e-mail address and, where applicable, their accredited status or capacity to issue qualified certificates. It will be possible to consult the data entered in the register on-line or through the appropriate register certificate.

Another section of the decree establishes the obligations that must be fulfilled by certification service providers in general, and providers issuing qualified certificates in particular. The latter shall, among other obligations, ensure speed and security in the provision of the service and, specifically, they must use trustworthy systems and products which are protected against modification and they must ensure the technical and, where applicable, cryptographic security of the certification processes supported by them.

As regards supervision and control, the Ministry of Public Works, through the Secretary General for Communications, shall oversee the performance of the obligations of the certification service providers. The latter must provide to the said Secretary General all such information and means necessary for it to exercise its functions. The infringements which service providers may commit are defined, being classified as very serious, serious and minor, as are the related sanctions, which may amount to a ban on performance of the activity in Spain for a maximum period of two years.

(16) The signatory is the natural person who holds a signature creation device and acts either on their own behalf or on behalf of the natural or legal person they represent.

(17) The certificate is the electronic attestation which links a signature verification data to a signatory and confirms their identity. The certificate is qualified if it is issued by a certification service provider.

(18) The certification service provider is the natural or legal person who issues certificates. They are also able to provide other services related to electronic signatures.

One section of the decree refers to the equivalence of certificates across countries. Certificates issued by providers in countries that are not EU Member States may be equivalent to those issued in Spain if they fulfil a number of requirements set out in the decree.

Other noteworthy aspects of the Royal Legislative Decree are the requirements that must be met by qualified certificates, as well as the period of effectiveness and the loss of efficacy of the certificates.

9. NEW CO-OPERATIVES LAW

The General Co-operatives Law 3/1987 of 2 April 1987 adapted the legal regime for co-operative companies to the requirements of the system of regional (autonomous) government. Even so, it has been necessary to create a new legal framework which, drawing on Community commercial and fiscal directives, reflects the numerous changes made to Spanish company law in recent years. This has been possible through publication of the *Co-operatives Law 27/1999 of 16 July 1999* (BOE of 17 July 1999), which reinforces the basic principles of the co-operative spirit and confronts the major economic and business challenges posed to it by Spanish membership of the Economic and Monetary Union.

In accordance with the powers transferred to the Regional (autonomous) governments, the scope of application of the law relating to co-operative companies which carry on their activity within the territory of several regional (autonomous) governments (except when it is mainly carried on in one of them) and to co-operative companies which mainly carry on their activity in the towns of Ceuta and Melilla has been redefined.

The Law provides a broad flexible framework within which co-operatives can regulate themselves, and establishes the basic principles that must generally be applied in the pursuit of their activity. One objective of the law is to reinforce business consolidation among co-operatives. For this purpose it has been necessary to make their financial and corporate regime more flexible, as well as to introduce certain changes relating to corporate financing. Thus, access to new ways of raising own funds is permitted, through the issuance of *special shares (participaciones especiales)* with a maturity of at least five years, which may be freely transferable. Also, the possibility is envisaged of issuing *non-voting equity units (títulos participativos),* remunerated according to the co-operative's profits.

With regard to their incorporation, the minimum number of members for a grade one co-operative is reduced from five to three, which will facilitate the creation of this kind of company. To the same end, it is established that co-operatives are incorporated by means of the simultaneous appearance of all three promoter members, with the incorporation meeting being abolished, so that the process is speeded up. Also, the concept of a "sponsoring member" *(socio colaborador)* is developed to substitute the so-called "associate" *(asociado)* of the previous Law, thereby increasing participation possibilities.

At the same time, new regulations have been established to govern the right of withdrawal of contributions, with greater protection for members and reinforcement of the co-operative "open-door" principle.

Another group of changes relate to the forms of financial collaboration between co-operatives. Thus, the concept of "special merger" has been created, whereby a co-operative company can be merged with any kind of civil partnership or commercial company, and the concept of the change of status of a co-operative company to another civil partnership or commercial company is regulated, without it being necessary to wind up the co-operative and create a new one. At the same time, new activities are included within the different classes of co-operatives such as social initiative, integral and so-called "mixed" co-operatives, in the regulation of which elements specific to co-operatives exist alongside others specific to commercial companies. In other respects, the forms of association of co-operative companies (unions, federations and confederations) have been maintained in order to promote the co-operative movement at the state level so as to defend and promote its interests, and the powers of inspection and sanctioning of the Ministry of Work and Social Affairs remain in place.

Finally, as regards credit co-operatives, they will continue to be governed by their specific legislation and by the provisions implementing the same (19). The general provisions regulating the activity of credit institutions will also apply to them and the Co-operatives Law will only be of supplementary effect.

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(19) The rules regulating credit co-operatives are contained in Law 13/1989 of 26 May 1989, which laid down the foundations of their legal system taking into account the dual nature of these institutions, which arises because besides being credit institutions they preserve their nature as co-operative promoting institutions. This law was implemented by Royal Decree 84/1993 of 22 January 1993, which besides adapting certain aspects of the legal framework for credit co-operatives to that of other credit institutions, incorporated the provisions of Community law applicable to them.