3 Regulatory changes in prudential supervision

This chapter includes the most significant legal changes which, from a prudential supervision standpoint, were made in 2007 in the regulation of the activity of CIs and other financial intermediaries and auxiliaries subject to supervision by the Banco de España. The focus of this chapter on organisational and disciplinary rules sidelines other regulatory changes which, though they undoubtedly bear considerably on the day-to-day running of institutions, have a more technical and operational profile. Albeit only on an indicative basis, these rules include most notably, on one hand, those implementing the regulation of securities payment and settlement systems, including the Trans-European Automated Real-time Gross settlement Express Transfer (TARGET 2) system;[1] and, on the other, those updating and systematising various aspects relating to trading and dealing on the public debt market.[2]

3.1 Community provisions

Among the Community provisions promulgated in 2007, two have a particular bearing on the conceptual scope addressed by this chapter.

Directive 2007/44/EC of the European Parliament and of the Council of 5 September 2007 amending Council Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increases of holdings in the financial sector.[3]

This Directive introduces certain changes in the procedural rules and evaluation criteria applicable to acquisitions and increases of holdings in the financial sector, with the aim of harmonising those relating to insurance, credit and investment institutions. Its ultimate aim is to establish detailed criteria and precise application procedures, so as to avoid the distortions that would arise were group structures spanning several sectors of activity or several EU Member States to follow non-uniform procedures in evaluating the suitability of potential acquirers.

It is first stipulated that the voting rights which should be taken into consideration for these purposes are both those held directly (even when the exercise thereof is suspended), and those belonging to a third party when the exercise thereof is controlled discretionally. Nonetheless, special cases are foreseen in which specific voting rights shall be excluded from the overall calculation.

The thresholds for notifying the supervisor, both for initial acquisitions and for increases or reductions of holdings, are set at 20%, 30% (or one-third if this is the benchmark for other implementing regulations) and 50% of the institution's voting rights. However, the proposed harmonisation does not prevent the Member States from requiring that the competent authorities be informed of acquisitions below the thresholds envisaged in the Directive, provided that no more than one additional threshold of below 10% is imposed.

To ensure sound and prudent management of CIs, the Directive lays down detailed procedures for notification (terms and documents to be submitted), actions by the competent au-

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1. CBE 1/2007 of 26 January 2007 (BOE of 6 February 2007) on the information to be reported by SESPA (the company entrusted with managing the National Electronic Clearing System) and approval of its regulation; Guideline of the European Central Bank ECB/2007/2 of 26 April (OJEU of 8 September 2002); and Resolution of the Executive Commission of the Banco de España of 21 September 2007 (BOE of 14 November 2007). **2.** CBE 2/2007 of 26 January 2007 (BOE of 14 February 2007) on the Public Debt Book-Entry Market. **3.** OJEU of 21 September 2007.

thorities (including collaboration between them) and the aspects to be evaluated. These aspects are, namely: reputation and solvency of the acquirer, with particular attention to the effective supervision of the group into which the institution might be integrated; reputation and experience of the persons who are to manage it; and the presence of rational signs of risk of money laundering or financing of terrorism.

Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC.[4]

The ultimate aim of this Directive is to establish a legal framework for the provision of payment services and market access for the providers of such services, for the purpose of contributing to the creation of a *Single Euro Payments Area* (SEPA) and promoting its proper working, with particular attention to the safeguarding of consumers.

Thus, the Directive regulates firstly a new, singular type of institution, the so-called payment institutions, which may, along with CIs (including electronic money institutions) and post office giro institutions, provide payment services. This latter concept is also defined with particular precision. Along with these institutions, the ECB, the national central banks and other public authorities may also provide such services, when not acting in their capacity as such authorities.

The regulation of payment institutions shares many similarities with that of other financial intermediaries in terms of requirements, including most notably minimum initial capital (which varies depending on the range of services to be provided), internal control mechanisms, mechanisms for protecting users' funds and for preventing money laundering, the integrity and experience of directors and managers, and a business plan. Arrangements are also established for registration and supervision, and the carrying out of the service through agents or branches is provided for, acknowledging the right of freedom of establishment and freedom to provide services within the EU (subject simply to prior communication), except if the institution has availed itself of the regime for partial exemption from requirements envisaged for lenders that execute payment volumes of less than €3 million per month.

Secondly, the Directive implements the legal framework of payment services, paying particularly attention to the regime of consumer protection which could be extended, should the Member States so decide, to small and medium-sized enterprises. This regime, which draws on the concepts of transparency of conditions and sufficient information, is applicable to all payment services made in euro or in the currency of any Member State, provided the source and destination is in the EU.

To this end, the Directive specifies the information that has to be provided both before and after the payment operation, adjusting for whether what is involved is a one-off operation or whether it is under the auspices of a framework agreement.

Finally, the Directive regulates specific rights and obligations in respect both of payment service providers and users, including most notably conditions of use of payment instruments, distribution of charges[5] and execution time and availability of funds. It further urges Member States to establish both complaint procedures and out-of-court complaint and redress proce-

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4. OJEU of 5 December 2007. **5.** The Directive enshrines the principle of shared charges, by virtue of which the orderer and the beneficiary pay those relating to their own payment service providers (charges to the border).

dures for the settlement of disputes relating to the provision of payment services, along with an effective, proportionate and dissuasive regime of penalties for improper practices and those lacking in transparency.

3.2 National provisions

In the national regulatory setting, the year 2007 marked the start of the transposition to the Spanish legal framework of a series of far-reaching Community regulations which, while not entailing an overhaul of the financial sector, will undoubtedly have a most significant bearing both on what we might call the domestic dimension of financial activity, i.e. the organisation, financing and solvency of institutions, and the external facet of such activity, i.e. relations between institutions and their customers.

3.2.1 REGULATION OF DOMESTIC ACTIVITY AND OF CAPITAL

The main regulatory changes of a national scope bearing on the domestic dimension of financial activity include most notably:

Law 36/2007 of 16 November 2007 amending Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting requirements of financial intermediaries and other financial system rules.[6]

This Law, which partially transposes Directive 2006/48/EC of the European Parliament and of the Council, incorporates the so-called Basel II Accord into the national legal framework with the aim, among others, of ensuring an appropriate level of solvency and a level playing field for CIs, making the regulatory capital required more sensitive to actual risks and encouraging better risk management.

As regards the minimum own funds requirements for consolidated groups of CIs and for CIs not integrated into a consolidated group, the Law now details a series of risks which, in any event and without prejudice to others, should be covered. These risks are: for all activities, exchange rate risk, commodities-related risk and operational risk; for all activities except trading-book activities, credit risk and dilution risk; and for the trading book, position, settlement and counterparty risk.

Conversely, for weighting investments, operations and positions, and for determining potential surcharges on the basis of the risk profile, confidence continues to be placed in a subsequent regulatory implementation, introducing the possibility of using techniques for the reduction of credit risk. In determining these calculations, the use of external credit ratings is now permitted, albeit conditional upon prior recognition by the Banco de España of the company assigning the ratings. Also permitted are internal ratings and internal methods of measuring operational and market risk developed by the institutions themselves, subject to prior authorisation by the Banco de España.

In addition, CIs are required to establish sound, effective and comprehensive strategies and procedures providing for the appropriate evaluation, maintenance and distribution of a level of internal capital commensurate with the level of risks. In the case of consolidated groups, these mechanisms shall be consistent and well-integrated.

The powers of the Banco de España, in its capacity as the authority responsible for the supervision of CIs and its groups, include the following: authorising or demanding the exclusion of

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6. BOE of 17 November 2007. On 16 February 2008 the BOE published Royal Decree 216/2008 of 15 February 2008 on financial institutions' own funds. This legislation implements Law 36/2007, along with Law 47/2007 of 19 November 2007, referred to later, in respect of aspects relating to the solvency of investment services companies.

an institution of a consolidated group in specific cases; the review of capital evaluation and distribution strategies and systems; the assessment of the risks to which they may be subject; and the drafting and publication of guidelines with appropriate criteria or procedures for the proper assessment of such risks.

Supervisory powers on a consolidated Community basis are also specified when this falls within the remit of the Banco de España. Among other responsibilities, the Banco de España shall coordinate the collection and dissemination of information, it shall plan and coordinate all supervision activities both in normal and emergency situations, and it shall cooperate in the granting of authorisation for the use of internal credit ratings or internal operational risk measurement methods for their application in Spanish groups of CIs.[7]

Furthermore, the Law introduces new requirements for reporting and dissemination to the public by CIs. It establishes the obligation to publish, at least once a year, a document called *information of prudential relevance.* This will include specific information on their activities and financial position, so that the market and other interested parties may assess institutions' risks, their strategies, their control mechanisms and their solvency. Although the minimum content of this document shall be determined by the Banco de España, each institution should set a formal information dissemination policy, compliance with which shall be overseen by the Banco de España.[8]

Moreover, new executive powers have been granted to the Banco de España for the exercise of its discipline-related functions regarding compliance by CIs with solvency obligations. Accordingly, the Banco de España may: oblige institutions and their groups to hold additional own funds, in certain circumstances, to the minimum amount required; require CIs to reinforce the procedures, mechanisms and strategies adopted for compliance with these requirements; demand the application of specific risk-reduction policies; restrict or limit institutions' business, operations or network.

Finally, for reasons of prudent valuation, it is established that the requirements for minimum own funds resulting from the application of ratings or of internal risk measurement methods may not be less, during the first year the Law is in force, than 90% of those that would result from applying the previous legislation. This lower limit stands at 80% for the second year.

Law 41/2007 of 7 December 2007 amending Law 2/1981 of 25 March 1981 on mortgage market regulation and other mortgage and financial system rules, on the regulation of reverse mortgages and dependency insurance, and establishing a specific tax regulation.[9]

Although the scope of application of this Law is multi-faceted and varied, insofar as it has a bearing on practically all aspects of the mortgage market, from the standpoint of this Report there are two essential amendments: first, the introduction of technical improvements in the instruments for financing mortgage activity; and second, the amendment of the supervisory regime for appraisal companies.

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7. As a result of these changes, Royal Legislative Decree 1298/1986 of 28 June 1986 on the adaptation of current legislation on credit institutions to that of the European Communities has also been amended, in order to accommodate the regulations governing information exchange between competent authorities in respect of supervision on a consolidated basis. **8.** These obligations are also reflected in Law 26/1988 of 29 July 1988 on the disciplining and intervention of credit institutions, into which the related types of infringements have been introduced along with the obligation to have an appropriate organisational structure, with clearly defined, transparent and consistent reporting lines which, in the case of credit institutions providing investment services, shall observe the organisational requirements laid down in Law 24/1988 of 28 July 1988 on the Securities Market. **9.** BOE of 8 December 2007.

Along with these changes, the Law introduces others ranging from the regulation of institutions' relations with their customers (transparency in the taking out of mortgage loans, compensatory arrangements for early repayment, reverse mortgages and dependency insurance policies) to the introduction of technical improvements in the mortgage-related legal framework. These measures are analysed in section 3.2.2 below.

Refinancing mechanisms

With regard to the technical improvements introduced into CIs' refinancing mechanisms, it is firstly permitted that any real estate mortgage loan, irrespective of its end-purpose and of where the property is located within the EU, may act as a guarantee for the issuance of mortgage bonds. In compensation, and so as to improve the quality of the collateral instruments, the loan-to-value ratio is reduced from 70% to 60%, except for housing loans, in which the current ratio of 80% is retained. However, both ceilings may rise respectively to 80% and 95% if there are appropriate and sufficient additional guarantees.

To promote transparency of the collateral portfolio, provision is made for the creation of a special register that shall separately include all mortgage loans and credits forming collateral for covered bonds (identifying those that meet the requirements established in the Law) and all those assigned to mortgage bond issues. Further, certain clarifications are made regarding the order of priority of holders of mortgage-backed securities in the event of the initiation of insolvency proceedings, while the insolvency administration body is authorised to conduct whatsoever operations might be necessary so that, in the event of time lags in the insolvent party's revenues, these holders may be paid.

Secondly, certain administrative formalities in place to date in the issuance of mortgage bonds have been removed in order to achieve a more neutral administrative treatment of such bonds as compared with covered bonds. To this end, the need to include a marginal note in the Property Register for each of the mortgages assigned is dispensed with and the previously compulsory setting-up of a bondholders' syndicate becomes optional. As with covered bonds, these issues continue to be backed by the issuer's unlimited liability in the event the specific collateral does not cover the amount of the debt.

Thirdly, and with a view to enhancing the quality of the collateral portfolio, the limit on the issuance of covered bonds is lowered from 90% to 80% of the outstanding mortgage loan balance. To compensate for this reduction and, above all, to reduce liquidity and interest-rate risk, the Law provides for the possibility of including specific liquid and low-risk assets in the pool of collateral covering the bond (up to 10% of the principal issued) or covered bond (up to 5%) issues.

Appraisal companies

With regard to appraisal companies, the Law acts in three areas, under the basic principle of preserving and strengthening the professionalism and independence of these companies. First, it establishes that, in certain cases[10], appraisal companies must have in place appropriate mechanisms to underpin their independence and avoid conflicts of interest. Also, the CIs by which they are controlled shall set up a *technical committee* to verify compliance with the independence requirements contained in the aforementioned mechanisms. This committee shall draft a report every year and send it to the board of directors or equivalent body of the institution and to the Banco de España.

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10. Specifically, when they provide services to credit institutions in their group, or when at least 25% of their total income in the regulatorily specified time period arises from their relationship with a credit institution or institutions in the same group, provided that one or more of these credit institutions has issued mortgage bonds that are in circulation.

Second, the sanctioning regime of appraisal companies is amended. New infringements derived from the new obligations contained in the Law are defined and the existing infringements are revised and updated.

Third, in order to ensure the appropriate management of appraisal companies, a regime of significant holdings[11] is established, similar to that envisaged for CIs. The direct or indirect acquisition of a significant holding in an appraisal company will entail the obligation to inform beforehand the Banco de España, which will have a term of three months to oppose, if appropriate, the proposed acquisition.

3.2.2 REGULATION OF RELATIONS WITH CUSTOMERS

The regulatory changes which, at the national level, address mainly relations between institutions and their customers, include most notably:

Law 22/2007 of 11 July 2007 on the distance marketing of consumer financial services.[12]

This Law establishes the specific regime to be applied to contracts with consumers of financial services[13] entered into at a distance (without a simultaneous physical presence), either directly or through an intermediary, by institutions established in Spain, in other EU Member States or in countries from the European economic area (EEA), in this latter instance when the recipient of the services resides in Spain and any of the following are the case: publicity of collective investment institutions (CIIs), direct insurance, operations with consumers, arrangements involving the choice by the parties of the legislation applicable to the contract, permissibility of communications and real estate located in Spain.

The essential purpose of this Law is none other than to protect consumers, given their potential greater vulnerability to distance marketing. To ensure this protection, the Law expressly provides for the invalidity of the waiver by consumers of the rights conferred on them by law, and the invalidity of acts carried out to evade this Law. It likewise set in place a rigorous, detailed regime governing the information to be furnished to consumers prior to their entering into the contract or to assuming their obligations. This information should refer to the service provider, to the financial service itself, to the contract and to the means of lodging complaints and claiming compensation at a distance, and it should be clear, comprehensible and adapted to the communication technique used.

The Law also regulates the right of withdrawal, whereby the customer shall have a period of 14 calendar days (30 calendar days in contracts relating to life insurance) to withdraw from the contract without being penalised and without giving any reason. However, this right may not be exercised in contracts whose price depends on market fluctuations beyond the supplier's control, or in those services whose contractual conditions require special legal certainty, as is the case, among others, of mortgage loans, certain insurance policies, contracts performed in full by the parties thereto at the express request of the consumer, and pension schemes. The consumer exercising the right of withdrawal shall only be obliged to pay, at most, for the financial service actually provided by the supplier up to the time of withdrawal, without any penalty.

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11. For the purposes of this Law, a significant holding in an appraisal company is defined as a direct or indirect interest of at least 15% of the capital or voting rights of the company, or one which, although not reaching this percentage, enables significant influence to be exercised in the company. **12.** BOE of 12 July 2007. **13.** For the purpose of the Law, 'financial service' means any credit or payment banking services, investment services, private insurance operations, pension plans and the activity of insurance intermediation.

The Law provides further protection to consumers, such as the possibility of demanding the immediate cancellation of charges arising as a result of fraudulent use of payment cards, and the prohibition of providing and charging for unrequested or tacitly renewed services.

Additionally, the Law regulates injunctions as a means of protection for consumers and promotes the use of out-of-court procedures. In any event, the burden of proof in respect of compliance with obligations under this Law shall be borne by the supplier.

Finally, the Law establishes a sanctioning regime which, in the case of supervised companies, shall defer to their specific regulatory regime and, in the case of other institutions, to that laid down in consumer regulations. By default, the provisions of Law 34/2002 on information Society services and electronic commerce shall be applied.

Law 41/2007 of 7 December 2007 amending Law 2/1981 of 25 March 1981 on mortgage market regulation and other mortgage and financial system rules, on the regulation of reverse mortgages and dependency insurance, and establishing a specific tax regulation.[14]

This section covers the external influence of this Law, whose organisational and financial provisions have already been analysed in section 3.2.1 above.

Relations with customers

Mindful both of the importance of transparency in the taking out of mortgage loans and of its attendant regulatory technicalities, the Law extends the reporting obligations in force to all types of mortgages on dwellings, while it empowers the Ministry of Economy and Finance to determine the minimum information that CIs have to furnish to their customers before any contract is signed. This information shall enable customers to ascertain the key characteristics of the products available and to assess whether they are suited to their needs and financial situation.

Aware, too, of the importance, as a competition-boosting factor, that the possibility of early debt repayment has for customers, the Law establishes a new compensation regime for early repayment for new mortgages on a dwelling in which the borrower is a natural person or a legal person subject to the small-companies regime under corporate income tax. Under this regime, the fee for total or partial early repayment shall be replaced by compensation for withdrawal that may not exceed 0.25% of the principal repaid (0.5% if the repayment takes place within the first five years of life of the credit or loan). In addition, the institution may receive compensation for interest rate risk provided that the repayment: (i) does not take place in an interest-rate-revision period whose agreed duration is equal to or less than twelve months, and (ii) it does not generate a capital gain in the institution's favour.[15]

Along with this new regime, the Law not only retains the tax benefits of mortgage subrogations and novations, in particular the exemption from transfer tax and stamp tax, but it also extends the cases in which mortgages may be amended without forgoing these benefits. In addition to the interest rate (ordinary or default) and/or the term, the amount, financial conditions (includ-

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14. BOE of 8 December 2007. **15.** A capital gain arising from exposure to interest-rate risk is defined as the positive difference between the principal outstanding at the time of prepayment and the market value of the loan or credit. This shall be calculated as the sum of the present value of the outstanding payments up to the next interest rate adjustment and the present value of the outstanding principal that will remain at the adjustment date if the loan were not repaid early. When the difference is negative, a capital loss for the creditor institution is deemed to exist.

ing the method of repayment) and personal guarantees may also be changed, without such changes entailing any alteration to or loss of priority of the registered mortgage.[16]

Additionally, in calculating the notary fees for subrogation, modifying novation and settlement of mortgage loans, the rates for loan documents with no stated amount shall be charged, while in the calculation of registry fees the rates for registrations shall be applied, taking as a basis the amount of outstanding principal reduced by 90%.

New products

In order to allow households to draw on home equity, without this impairing their standard of living, the Law regulates the so-called reverse mortgage. This instrument involves a mortgage loan or credit taking the form of a mortgage on real property that is the habitual dwelling of the applicant, provided that the following requirements are met: a) the applicant and any beneficiaries designated by him/her must be 65 years old or more or in a situation of severe or considerable dependency; b) the mortgagor must draw the loan amount in periodic withdrawals or as a lump sum; c) the debt must only be claimable by the creditor and the security interest enforceable upon the death of the borrower or, if so stipulated in the contract, upon the death of the last of the beneficiaries;[17] and d) the mortgaged residence must have been appraised and insured against damage.

The reverse mortgage envisaged in this Law may only be granted by CIs and by insurance companies authorised to operate in Spain, without prejudice to the limits, requirements and conditions imposed on insurers by their sectoral regulations. On granting these mortgages, institutions are obliged to provide independent advice to applicants. The public deeds documenting these transactions will enjoy the same tax benefits envisaged for mortgage subrogations and novations, along with the same regime for the calculation of notary and registry fees.

Finally, the Law regulates the coverage of dependency either under an insurance contract entered into with insurers, including social welfare mutual societies, or through pension schemes. Insurance contracts shall be taken out with insurers that are authorised to pursue insurance activity in the life and sickness branches, and they may be in the form of individual or collective policies.

Law 47/2007 of 19 December 2007 amending Law 24/1988 of 28 July 1988 on the securities market.[18]

This is a wide-ranging Law which, in transposing Directives 2004/39/EC and 2006/49/EC, both of the European Parliament and of the Council, regulates numerous aspects relating to: (i) the solvency and supervision of investment services companies; (ii) organisational requirements for institutions providing investment services; (iii) the conditions under which such services shall be provided; and (iv) the requirements made of regulated markets, of multilateral trading facilities and of systematic internalisation, the latter two instruments having been newly created.

It is true that major changes have been introduced into the securities market (the definition of financial instruments, the new regulation of official secondary securities markets and the intro-

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16. Nonetheless, if the mortgage liability figure were to increase or the loan term to extend due to this increase or extension, acceptance by the holders of a lower priority for their registered claims would be necessary. **17.** It should be borne in mind, however, that the maximum amount drawable by the mortgagor shall be determined as a percentage of the appraisal value on the date of the constitution of the contract. If this percentage is reached, the elderly person or dependent shall cease to draw income and the debtor shall continue to generate interest. Upon the death of the owner or of the last of the beneficiaries, the heirs will have to settle the debt, which may be done by enforcement of the mortgage. **18.** BOE of 20 December 2007.

duction of new alternative forms of trading, the creation of new investment service companies and of new investment services, the laying down of new rules of conduct and the updating of the solvency and supervisory regime). But for the purposes of this chapter the focus here will be solely on the amendments relating to the Public Debt Book-Entry Market, whose operation is overseen by the Banco de España, and on those relating to the organisational requirements for institutions providing investment services (among which CIs are the most significant in quantitative terms) and to the conditions under which they should provide such services.

Public debt market

The new Law on the Public Debt Book-Entry Market no longer solely addresses the trading of fixed-income securities represented by book entries issued by public agencies or entities. Now, other financial instruments can be traded on it provided they comply with the applicable regulations and with its technical specifications.

Although the Banco de España continues to be considered as the governing agency of the market, it is foreseen that its replacement will be as established generally for the other official secondary markets. Further, the Public Debt Book-Entry Market Advisory Committee, which supplied information on the general provisions proposed on market-related matters, among other functions, has ceased to exist.

Access to market-member status, and the revocation thereof, had hitherto required authorisation by the Ministry of Economy and Finance at the proposal of the Banco de España, further to a report from the CNMV. The procedure will now be the same as for any other market. Likewise, access to management-company status, which was also subject to date to an authorisation procedure, will now depend solely on compliance with the provisions of the market regulation.

Finally, the Banco de España is authorised so that, in the event of a Public Debt Book-Entry Market management company being declared insolvent, it may immediately arrange, and at no cost to the investor, for the transfer of the book-entry securities held on behalf of third parties to other managing companies. And this without prejudice to the rights of securities-holders to request their transfer to another managing company on their own account.

Organisational requirements of institutions providing investment services

The Law introduces the obligation for institutions providing investment services to define appropriate policies and procedures for ensuring compliance with the Securities Market legislation. To this end, they should have an organisational structure suited to the services they provide; a regulatory compliance unit; a reporting system that ensures knowledge of obligations, risks and responsibilities; appropriate organisational measures in order, first, to monitor the operations conducted personally by their managers and employees, and further, to prevent potential conflicts of interest from harming their customers; appropriate records of operations; and measures to protect the financial instruments in which customers have placed their trust.

In addition, and under the supervision of the Banco de España in the case of CIs, companies providing investment services should have suitable administrative and accounting procedures; effective internal control mechanisms and risk assessment techniques, including a compliance verification body; business continuity arrangements; appropriate measures for protecting customers' funds (which in the case of entities other than credit institutions entail the prohibition of their use on own account); and operational risk control procedures.

Rules of conduct

One of the main purposes of the reform is the effective protection of investment services customers. To this end, the Law distinguishes between three possible categories of investor to

which it grants different degrees of protection: retail customers, professional customers (those with experience, knowledge and the necessary skill to take their own investment decisions and to correctly assess their risks) and eligible counterparties (regulated professional customers and public agencies). The greatest degree of protection is granted to the first category.

Furthermore, the Law stipulates that customers should be given appropriate and comprehensible information on the company, on its financial instruments and investment strategies, on its execution venues and associated charges, and on the risks of the service offered. This information should be provided not only to current customers but also to potential ones, when it may be part of an advertising campaign.

When providing investment advice or portfolio management, the company should bear in mind both the knowledge and experience of retail customers and their financial situation and investment objectives, while for other services it is only necessary to request knowledge and experience in the investment field relevant to the specific type of product or service offered or demanded. However, when the service provided involves the execution or the reception and transmission of orders on the customer's initiative, it will suffice to comply with specific organisational and reporting conditions.

As an additional means of protection, the Law provides that any accrual by investment services companies of profits or incentives that are not in keeping with the provisions in the Law and its regulatory implementation will mean that the conduct of these companies will not be considered diligent.

3.2.3 OTHER RULES

As part of the regulatory framework this chapter addresses, particular attention should be paid to other securities market reforms, including most notably that introduced by *Law 6/2007 of 12 April 2007 reforming Law 24/1988 on the securities market, for the amendment of the regime governing initial public offerings and the transparency of issuers;* and by Royal Decrees 1066/2007 of 27 July 2007, and 1362/2007 of 19 October 2007, which implement it.

However, from the standpoint of the prudential supervision by the Banco de España of CIs and other intermediaries or financial auxiliaries, these amendments are of limited interest in that, first, they only affect listed companies or securities issuers; and further, they come under the remit of the CNMV. A straightforward listing of the key aspects these rules regulate will therefore suffice here.

Further to Law 6/2007 and the subsequent implementation thereof, the obligation to formulate an initial public offering (IPO) turns on the concept of control, a position assumed to be when a physical or legal person attains, either individually or in concert with others, and directly or indirectly, a percentage of voting rights equal to or over 30%; or when, with a lower share, this person designates over 50% of the company's board members. Nonetheless, the CNMV may dispense with this obligation when an equivalent procedure ensures protection of the legitimate interests of shareholders and of holders of securities carrying rights to subscribe to the shares. The IPO should be for 100% of the shares (the concept of a partial IPO has ceased to exist) at a fair price (the highest price paid by the offeror for the same securities in the 12 months prior to the announcement of the offering). However, the CNMV may alter this price in specific circumstances and provisions are laid down for cases where there have been no prior acquisitions. In any event, the IPO may be voluntary.

Provisions are also in place for mandatory bids (which may be invoked both by the offeror and by the shareholders if, as a result of an IPO, 90% of the capital is acquired), and rules cover

the obligations of the board of directors of the offeree company, whose actions contrary to the bid must be authorised by the general meeting of shareholders.

The Law also amends the regime governing the regular publication and dissemination of relevant information by securities issuers, including that relating to their own shares.