REPORT ON BANKING SUPERVISION IN SPAIN

2001

BANCO DE ESPAÑA

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PREFACE

This Report is the first to be published by the Banco de España on its supervisory tasks. It is primarily intended to report on the central bank's supervisory conduct, as is clearly incumbent upon it given the powers and degree of autonomy conferred under Spanish regulations. Further, by means of the information provided, it seeks to heighten awareness and understanding of supervisory regulations and conduct.

These aims, moreover, are part of a broader picture. Undeniably, this exercise in accountability is in response, in turn, to an increasingly pressing social demand for greater transparency in the management of public affairs, especially when a high degree of autonomy, as is the case here, is granted to bring this about. The second aim is no less important. Better knowledge and general understanding of the mandate given to the Banco de España in respect of supervision, the rules governing it, the criteria and priorities with which it is applied, the specific procedures it follows and the actions arising as a consequence complement the supervisory mission and allow it to be more efficient. This is because supervision may then count on the active contribution of all those called on to participate in achieving greater solvency and stability for our financial system, ranging from depositors and other investors to the directors and senior managers of financial institutions.

This approach is all the more necessary insofar as the links between the financial sphere and the real economy are increasingly close and complex, thereby strengthening the key role a country's financial system plays in economic growth and stability. In such circumstances, the priority and central objective of banking supervision must still be to bolster confidence in the system, seeking to prevent potential banking crises and their effects and, hence, protect depositors. Furthermore, at a time financial systems are evolving at great speed, owing to globalisation, deregulation, financial innovation, competition and concentration processes, banking supervision cannot and should not act as a brake on development. On the contrary, it should establish a supervisory framework to encourage best banking and risk management practices, so that the proper, efficient and stable functioning of the financial system may assist the country's development. And it should do so by providing its services with the quality and integrity that society demands.

In this new financial framework, the qualitative aspects of banking are becoming increasingly important. These include the quality of corporate governance, control mechanisms, risk management culture and structures, and transparency to the markets, among others. All these aspects are scarcely perceptible in the figures of a balance sheet. That means supervision, while not overlooking watchfulness of financial institutions' capital and soundness, will have to pay increasing attention to evaluating their human and organisational capital.

In order to discharge its responsibilities appropriately, supervision must perceive all these changes, identify the underlying trends and, on the basis of this, review in an ongoing fashion the validity of its approach, duly updating its working methods and perfecting, stimulating and reallocating the means at its disposal. Reporting on this dynamic and involving both the finance industry and society as a whole therein is not only a part of supervisory responsibilities, but also a vital means for addressing them with a reasonable prospect of success.

In providing greater transparency in respect of the various supervisory actions of the Banco de España, this Report complements others, including the Annual Report, that are already published on a regular basis. These cover, inter alia, the Public Debt Book-Entry System, the Balance of Payments, the Central Balance Sheet Data Office and the Complaints Service. In addition, in seeking to draw support so that banking supervision may better attain its objectives, the Report builds on the work of the Banco de España's new line of publications under the self-explanatory title of "Financial Stability", which act as an open forum for discussing initiatives related to this area.

In sum, this Report is intended to be the first of a series. In publishing it, the Banco de España wishes to contribute to a better understanding of its supervisory activity, which will result in a more effective and transparent exercise of its powers in this area.

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ANNEXES

ABBREVIATIONS

€ m	Millions of euro
1BCD	First Banking Co-ordination Directive
2BCD	Second Banking Co-ordination Directive
ACs	Appraisal companies
AIAF	Association of Securities Dealers
ATA	Average total assets
ATM	Automated teller machine
BAC	Banking Advisory Committee
BCBS	Basel Committee on Banking Supervision
BE	Banco de España
BIS	Bank for International Settlements
BOE	Official State Gazette
bp	Basis points
BSC	Banking Supervision Committee of the ESCB
CBE	Circular of the Banco de España
CCR	Central Credit Register of the Banco de España
CECA	Spanish confederation of savings banks
CERSA	Spanish state-owned reinsurance company
CGs	Consolidated groups of CIs, DIs, etc.
CIs	Credit institutions (DIs, SCIs and the ICO)
CNMV	National Securities Market Commission
DGF	Deposit Guarantee Fund
DGS	Directorate General of Insurance
DGTPF	Directorate General of the Treasury and Financial Policy
DIs	Deposit Institutions
EAR	Equivalent annual rate
EC	European Commission
ECB	European Central Bank
EEA	European Economic Area
EMU	Economic and Monetary Union
ESCB	European System of Central Banks
EU	European Union
FESCO	Forum of European Securities Commissions
FMC	Financial Markets Committee
GdC	Groupe de Contact

GDP	Gross domestic product
GTIAD	Working Group on the Interpretation and Application of the Banking Directives
IAIS	International Association of Insurance Supervisors
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICO	Official Credit Institute
IFAC	International Federation of Accountants
IOSCO	International Organisation of Securities Commissions
IPO	Initial public offering
LABE	Law on the autonomy of the Banco de España (Law 13/1994)
LDI	Law on the discipline and intervention of credit institutions (Law 26/1988)
LSM	Law on the securities market (Law 24/1988)
MGCs	Mutual guarantee companies
MO	Ministerial Order
MTG	Mixed Technical Group
OCC	US Office of the Comptroller of the Currency
OECD	Organisation for Economic Co-operation and Development
OJ L	Official Journal of the European Communities – legislation series
pp	percentage points
RD	Royal Decree
RDL	Royal Decree Law
RGs	Regional (autonomous) governments
ROA	Return on assets (profit after tax as percentage of ATA)
ROE	Return on equity (profit after tax as percentage of own funds)
SABER	Risk-based approach to banking supervision
SCIs	Specialised credit institutions
SEPBLAC	Commission for the Prevention of Money Laundering and Monetary Offences
SLBE	Banco de España Settlement Service
SNCE	National Electronic Clearing System
TSG	Technical Sub-Group
US	United States

I

STRUCTURE AND EVOLUTION OF THE CREDIT SYSTEM

As in other developed countries, the Spanish credit system has, since the onset of the 1990s, seen a significant increase in the concentration of activity in an increasingly smaller number of institutions and groups. This has essentially come about further to the process of mergers which, between 1998 and 2000, gave rise to the two biggest Spanish financial groups. Nonetheless, this process has not had appreciable effects on the degree of competition between institutions in the system and, moreover, it has slowed in 2001 in respect both of the reduction in the number of institutions and of the degree of concentration.

However, the process has not been accompanied by a reduction in the number of offices or in the numbers of staff employed. Both have held stable thanks basically to the growth in savings banks and credit co-operatives, which have been much less affected than banks by the above-mentioned developments.

Banking activity in general, and credit activity in particular, have grown strongly over the past four years, in step with the upturn of the Spanish economy's business cycle and with the low level of interest rates. This situation has also been conducive to a decline in the relative level of bad and doubtful debtors to lows not witnessed in recent decades. Combined with the introduction of the new provision, which adjusts for the effects of the business cycle, this has pushed the coverage indices for these assets far above the related asset amounts.

The strong growth of credit has been largely directed at financing construction and house purchases, against a background of strongly rising prices. The strategy of many institutions has been geared to gaining market share in mortgage financing, through policies involving flexible loans, lengthier maturities and a preference for floating-rate credit, in view of the strategic importance of this business area where customers enter into a long-term relationship with the institution.

The composition of the securities portfolio, with growth similar to that of credit, also shows changes. Government bonds have been replaced by corporate bonds and equities, although the latter contracted in the final part of the period running from 1998 to 2001 further to the successive dents to the stock markets since the technology-stock bubble burst in mid-2000.

The financing of this expansion in activity has been underpinned by resident private-sector deposits, which have also benefited in recent years from the diminished attractiveness of investment in collective investment institutions.

In this expansionary setting, the results of deposit institutions (DIs) (encompassing banks, savings banks and credit co-operatives) have also increased significantly during the 1998-2001

period. However, with much lower growth, the year 2001 was clearly different from the two previous years for the following reasons: *a)* a notable increase in net interest income, due largely to dividends received from investee companies; *b)* weak growth in revenue from services, linked to the unfavourable performance of securities markets; *c)* a substantial reduction in resources in respect of the provisioning of permanent holdings affected by the Argentine crisis; and *d)* the first set-aside to the statistical provision for a complete financial year.

The activity of the consolidated groups of credit institutions (1), measured by the balance sheet total, has increased notably. This increase was all the more marked in 2000 owing to the acquisition of large banks, in particular in Latin America, where two-thirds of bank assets abroad are located. That year, the foreign business of groups (essentially banking intermediation and fund management) rose to account for more than one-quarter of the total, with a contribution to profits after tax of 20 %. Conversely, in 2001, the Argentine crisis led to a slide in such foreign activity and its contribution to group profits, affected by the growth of provisioning (2).

Changes in the solvency ratio largely reflect changes in the composition of the consolidated groups of credit institutions. The ratio had shown a slow but sustained decline as from 1996. In 2000, the decline in the ratio steepened owing to a notable increase in requirements and to the fact that the goodwill generated on the acquisition of foreign institutions subtracted much of the growth in tier 1 capital. As a result, the ratio for that year stood at a low of 10.5 %, which was still indicative of a considerable surplus of resources in the system. In 2001, the ratio picked up to 11.1 % (13 % if the Basel Capital Accord were directly applied), with robust growth in resources and in the buffers over the minimum regulatory capital requirements.

I.1. STRUCTURE AND COMPOSITION OF THE SYSTEM

I.1.1. Number of credit institutions

The number of credit institutions (CIs) has held on the declining trend marking the last decade, although this has slowed somewhat in the past year. The number of institutions in the corresponding register (see Table I.1 and Chart I.1) was, as at December 2001, 369, compared with 404 in 1998, virtually half the number in 1988 (754). In this latter year, Law 26/1988, of 29 July 1988, on the Discipline and Intervention of Credit Institutions, attributed the supervision of specialist CIs to the Banco de España, and the first merger between two major banks took place.

There have been many reasons for the reduction in numbers of CIs: the fact the different types of institutions move within the same operational and requirements-related sphere (entailing the redundancy of activities within the group); the tightening of requirements to operate; the search for a more appropriate size to compete within the European Union (EU); and the rationalisation of activity. The effects of the first two factors appear to have concluded, while the latter two continue to bear on the number of institutions (3).

(1) Consolidated groups of credit institutions (CGs) encompass all financial institutions, except insurers (domestic and foreign), over which a Spanish credit institution exerts control (see Annex 1). Nonetheless, for analytical purposes, and unless indicated otherwise, the concept of consolidated groups used adds to these those Spanish credit institutions not belonging to any group, in order to obtain an overall view.

(2) Nonetheless, the contribution of foreign business to results is biased upwards, since the amortisation of goodwill is attributed in the main to activity in Spain, which has a significant adverse impact on the results of local activity and, therefore, of its contribution.

(3) A small number of non-operational institutions are pending de-registration, for various reasons, as at December each year. In this chapter the data refer to operational institutions, and do not include the ICO (Official Credit Institute). Moreover, the data relate to the close of the period, except in the case of results, which are average data, or when otherwise indicated.

TABLE I.1

Number of credit institutions registered at year-end

	1998	1999	2000	2001
Total	**404**	**391**	**371**	**369**
Banks	153	147	143	146
Domestic	76	71	66	63
Foreign	77	76	77	83
Subsidiaries	24	23	25	27
Branches	53	53	52	56
EU	*35*	*41*	*41*	*48*
Other countries	*18*	*12*	*11*	*8*
Savings banks	51	50	48	47
Credit co-operatives	97	97	94	92
SCIs	103	97	86	84
Consolidated groups (a)	31	29	30	32
Institutions belonging to groups	129	123	116	121
Stand-alone institutions	275	268	255	248
MEMORANDUM ITEMS:				
Operational Institutions	396	383	364	364
EU insitutions operating in Spain without an establishment	162	190	246	274

(a) With at least two Spanish credit institutions consolidated. This is more restrictive than the definition in Annex 3.

Over the last four years the reduction has especially affected specialised credit institutions (SCIs) (4) and domestic banks. SCIs were established as specialist CIs and were those most affected by activity redundancy within groups. The reduction in the number of domestic banks is the outcome of mergers in the quest for a suitable size with which to compete, with those of major banks between 1998 and 2000 proving of note (5). Mergers between savings banks and credit co-operatives involve the restructuring of those operating in the same region. It is considered that this latter process, which was resumed in 1999, is not yet over.

(4) At present, the only differences remaining among credit institutions are the inability of the SCIs to raise deposits and constraints on the regional presence of credit co-operatives, depending on their statutes.

(5) The banking mergers involved Banco Santander and Banco Central-Hispano, on one hand, and BBV and Argentaria, Caja Postal and Banco Hipotecario, on the other.

CHART I.1

Number of registered credit institutions

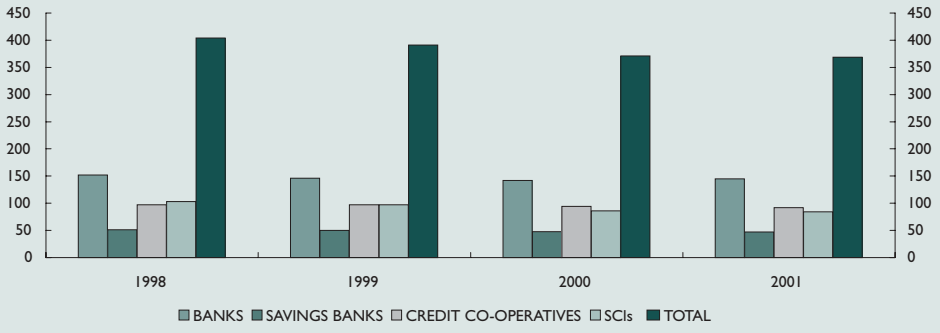
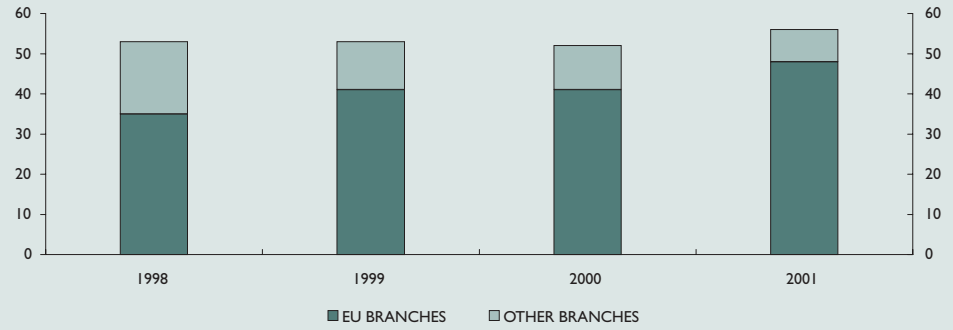


CHART I.2

Number of branches of foreign credit institutions



Among foreign banks (see Chart I.2) there has been a clear reduction in the number of branches of non-Community institutions. This has been due to mergers, in the home country, of institutions with a presence in Spain, although some abandoned the Spanish market due to earnings expectations not being met. There has further been an increase in Community banks established in Spain under the Single Licence envisaged in the Second Banking Co-ordination Directive, which came into force in 1993. The year 2001 also saw an increase in the number of subsidiaries, due to the acquisition of small Spanish banks by banks headquartered in the EU.

Chart I.3 shows that the number of consolidation groups (considering as such those including at least two CIs) and the institutions included therein have held stable despite merger processes. Consequently, the reduction has mainly affected stand-alone institutions.

Also of note is the increase in the number of institutions which, by virtue of the Community passport, plan to engage in some type of activity in Spain without a permanent presence. Four Community countries (France, United Kingdom, Luxembourg and Germany) accounted for 85 % of such institutions as at end-2001, 61 of which intend to engage in all the financial services envisaged in the Directive.

I.1.2. Personnel, branch offices and automated teller machines of credit institutions

As can be seen in detail in Table I.A.1 (see appendix at the end of this chapter), the personnel employed by CIs have grown slightly, predominantly in the last two years of the period.

CHART I.3

Consolidated groups of credit institutions and stand-alone institutions

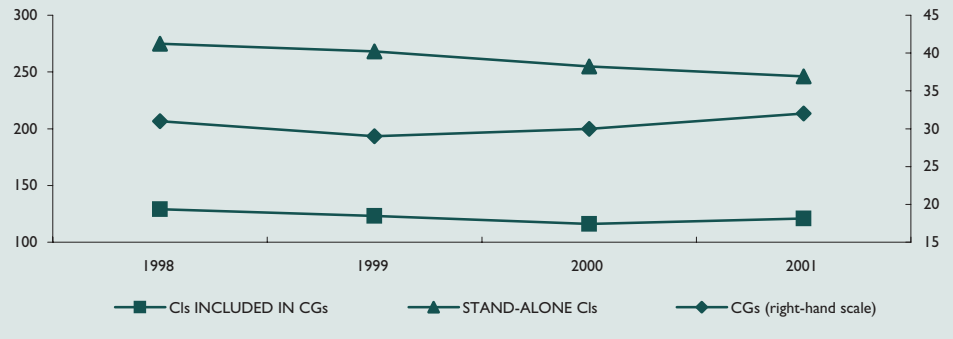
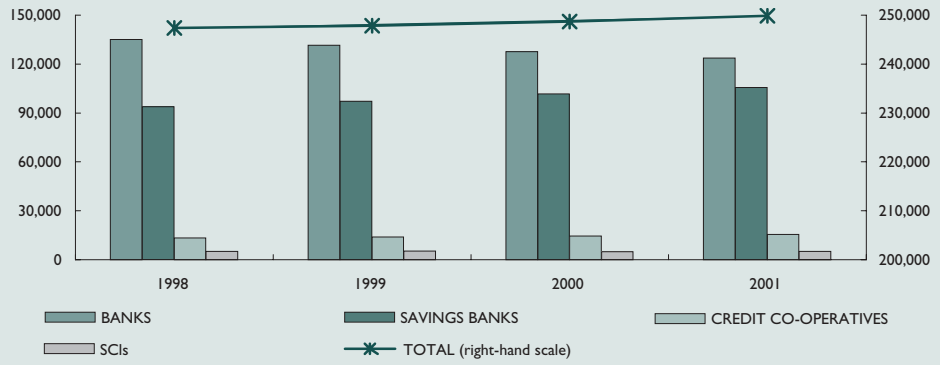


CHART 1.4

Number of employees of credit institutions



The aggregate result stems from a reduction in the personnel employed by banks, relative stability in numbers of SCI staff and an increase at savings banks and credit co-operatives (see Chart 1.4). The decline in employees at banks is the outcome of the reduction in the number of institutions and technological progress, while the increase at savings banks reflects their forceful regional expansion, particularly outside their home regions.

The branch network (see Table 1.A.1 and Chart 1.5) has remained practically unchanged since 1998. Once again, this is the result of a fall in the number of bank branches, primarily due to the superimposition of networks arising from mergers, and of an increase in those of savings banks and credit co-operatives. Significantly, there are 33 % more savings-bank branch offices than bank branch offices, even though banks outnumber savings banks by three to one.

Meanwhile, the process of elimination of jobs and streamlining of the branch network seems to have operated in reverse among foreign banks, where both variables increased in 2001.

Customer attention has been strengthened by a notable increase in the ATM network. The number of ATMs has exceeded the number of bank branch offices since 1999 (see Table I.A.1). In this case, the growth was across all the different types of institution, although in 2001 the number of ATMs of domestic banks decreased, as a consequence of the merger of major banks the previous year.

The number of employees per institution in Spain is practically double the European average. By contrast, the greater density of the Spanish network means that the number of employees per branch office is practically half the European average. In terms of population, the

CHART 1.5

Number of branch offices of credit institutions

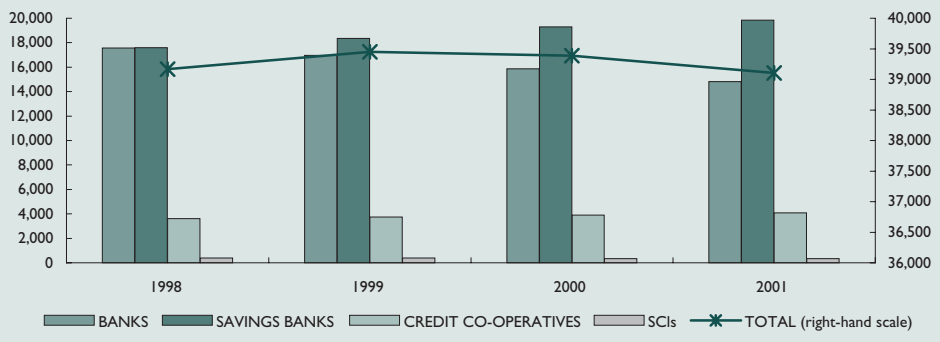
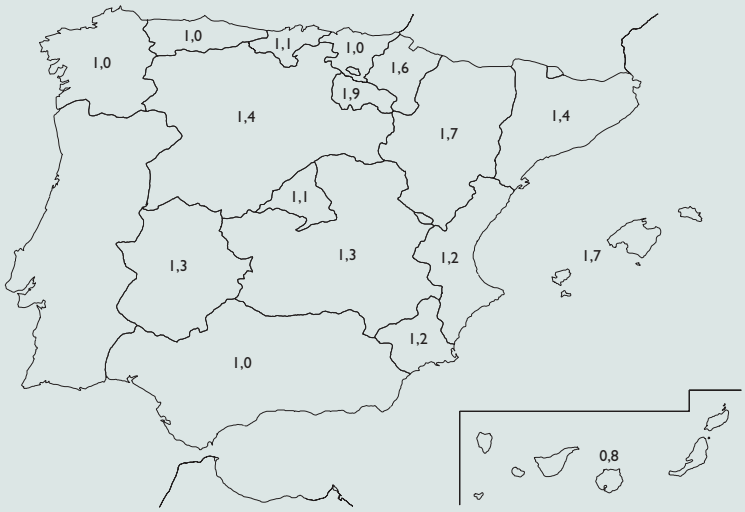


CHART I.6

Branch offices per 1,000 inhabitants over the age of 16
Deposit institutions. December 2001



number of branch offices per thousand inhabitants is very close to one in Spain, as against an average of 0.55 in the European Union in December 1999 (see Chart I.6).

I.1.3. Concentration of domestic activity (6)

At the end of 2001, the five major Spanish banking groups accounted for 53.2 % of the assets of the system (see Chart I.7) and a somewhat lower percentage of lending (48.9 %). The percentage falls to 43.7 % (see Table I.A.2) when resident private sector creditors are considered, which shows the greater importance for these groups of other alternative sources of finance.

The concentration in the five largest institutions increased significantly between 1998 and 2000 (7), with the mergers of Banco Santander and Banco Central Hispano and of BBV and Argentaria, which made room for two new institutions, albeit smaller in size than the ones they replaced. In 2001 there was a fall in concentration at this level, with losses of share in the different segments of between one percentage point (pp), in the case of total assets, and 1.5 pp, in that of lending to residents (see Table I.A.2). This was attributable in part to the sale of a medium-sized bank (hitherto the subsidiary of one of these groups), which was then included among the 10 largest banks, so that the loss of concentration was significantly smaller at the latter level.

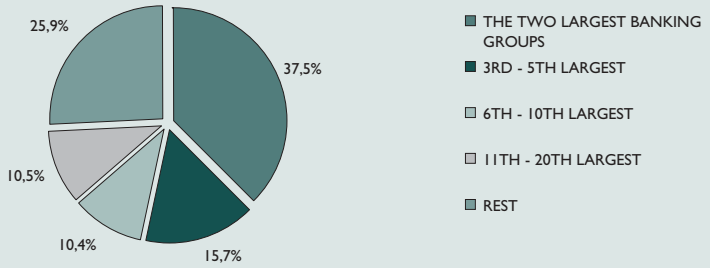
The following five groups by size add somewhat more than 10 pp to concentration in terms of assets, and the following ten a very similar percentage, so that the twenty largest institutions or groups account for almost three-quarters of the assets of the system. At the levels of the ten largest and twenty largest institutions, there is less disparity between concentration in terms of assets and that in terms of creditors or lending. At the same time, although concen-

(6) This section refers to the concentration of activity in the domestic market, so that the external activity carried out directly by the domestic institutions or by their foreign subsidiaries is not considered.

(7) The merger, in 1998, between Argentaria, Caja Postal and Banco Hipotecario did not affect concentration, as it was between institutions belonging to the same group..

CHART I.7

Concentration of assets among consolidated groups of credit institutions in 2001



tration at these levels is more stable, 1999 and 2000 saw the entry of larger institutions, as a result of mergers (see Chart I.8).

I.2. ACTIVITY OF CREDIT INSTITUTIONS

I.2.1. Activity of consolidated groups

The aggregate balance sheet total of the consolidated groups of credit institutions (CGs) and stand-alone institutions not included in CGs amounted, as at end 2001, to € 1,459 billion. During the four years preceding that date, this figure grew at an annual rate of 12.9 %, which exceeds the 10 % figure for the Spanish CIs on their own. However, 2001 saw a turning point and these two rates are similar again.

While the growth of the CGs was very concentrated in 2000 (23 %) (see Chart I.9), that of the Spanish CIs was more stable. The growth of the CGs in 2000 was linked to the acquisition abroad of several large subsidiaries that year, to the extent that the weight of foreign activity within their overall activity rose from 20 % to 27.4 %.

The year 2001 was characterised by stability in the number of institutions of the CGs, by a sharp decline in foreign activity, due to the Argentine crisis, and by some buoyancy in the domestic activity of the CGs, which grew at a higher rate (13.5 %) than that of the CIs (9.6 %).

The reduction in foreign business particularly affected loans (–7 %) and the bond portfolio, both as regards government bonds (–18 %), which were affected by the Argentine renegotiations, and corporate bonds (–21 %). At the level of the CGs as a whole, the reduction was negligible, owing to the parallel increase in these items in activity in Spain.

The separation into domestic and foreign business means that the assets and liabilities of the respective areas do not coincide. In 2001, the assets of business in Spain exceeded the liabilities by € 52.5 billion, which means that domestic business is being financed to that extent by international activity. This financing is obtained, in particular, from the issuance of debt securities and subordinated debt, which during the years considered increased at average annual rates of around 35 %, as well as from the issuance of preference shares, which are shown in the consolidated statements with other minority interests (holdings of third parties outside the group).

Apart from financial intermediation, CGs also have significant fund management business (in relation to mutual funds and pension funds). The assets of the funds under management totalled € 280 billion in 2001 (equivalent to 19 % of the balance sheet total of the CGs), with annual growth of 9.8 %.

CHART 1.8.1

The five largest consolidated groups of credit institutions

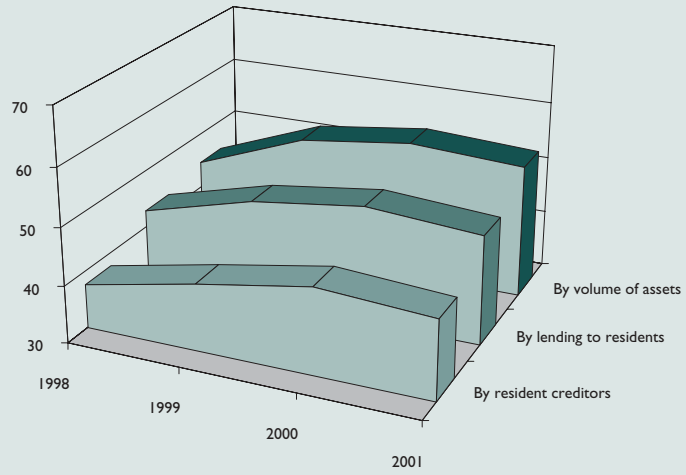


CHART 1.8.2

The ten largest consolidated groups of credit institutions

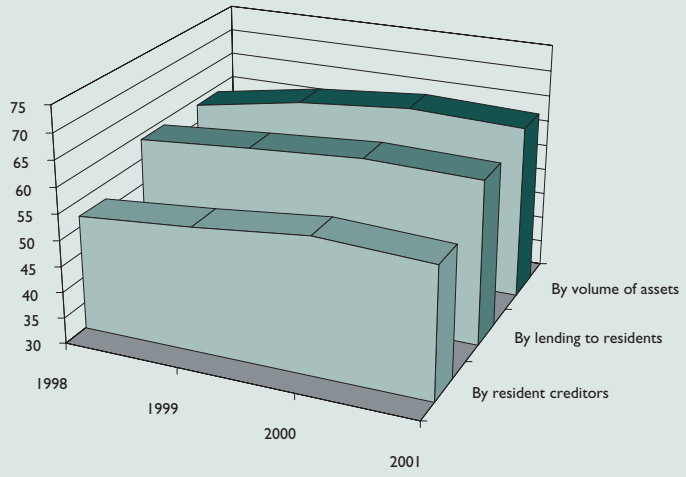


CHART 1.8.3

The twenty largest consolidated groups of credit institutions

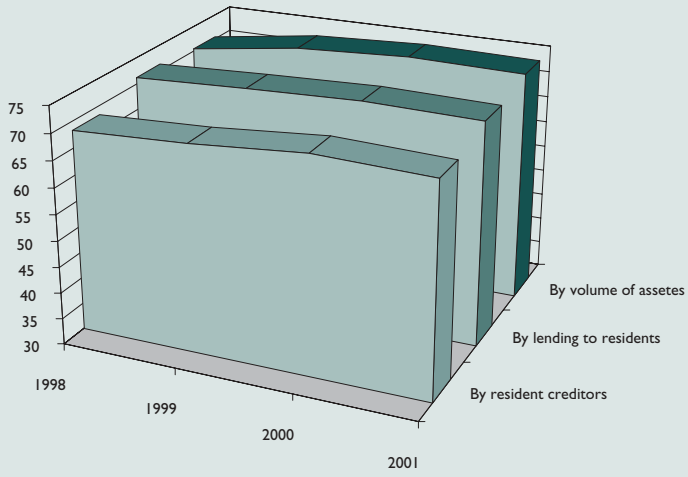
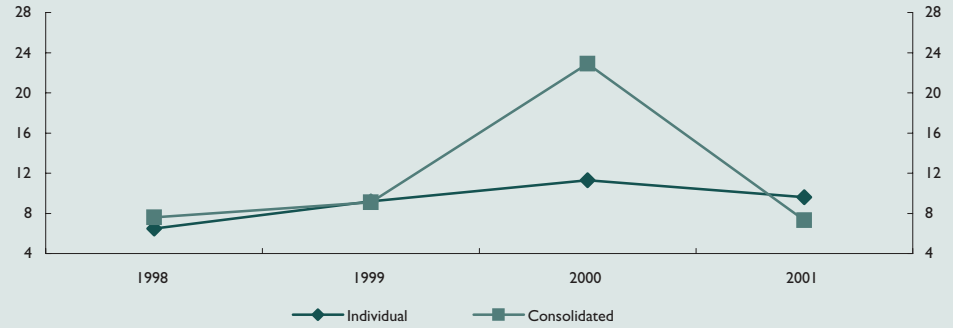


CHART I.9

Growth of the balance sheet total for credit institutions and for consolidated groups of credit institutions (%)



Leaving aside cross-border activity and considering solely the local activity performed by subsidiaries and branches with a physical presence abroad (see Table I.A.3), the geographical concentration of CGs is clear. Two thirds of financial assets and liabilities (8) and almost 85 % of the funds under management correspond to Latin America. Among the other areas, the EU is the most important destination for investment and has been growing progressively in the last three years. The rest of the areas (which include other OECD countries, such as the US, Japan and Switzerland, as well as off-shore centres) have greater importance as a source of finance.

The spectacular growth of activity in Latin America, which doubled in 2000, and its stagnation in 2001, can also be seen in Table I.A.3.

I.2.2. Activity of credit institutions

The balance sheet of the CIs has grown over the last four years at an annual rate of 10 % to stand at € 1,264 billion. The slowdown in the Spanish economy in 2001 (GDP grew at 2.8 %, as against 4 % on average in the three previous years) reduced growth that year to 9.6 % (see Table I.3).

The most dynamic items in the period were lending and the securities portfolio, which grew at annual rates of 13.5 % and 13.7 % respectively, the rates being 11.7 % and 12.2 % in 2001. Notable within lending was the growth of collateralised loans, while within the securities portfolio corporate bonds and equities increased at similar rates (around 30 % annually). In 2001, however, equities grew at a lower rate than the balance sheet, on account of the greater instability on stock markets, while corporate bonds increased at a rate of 27 %.

At the opposite extreme, the decline in assets and liabilities vis-à-vis financial intermediaries and the stagnation in exposure to the public sector (credit and securities) over the last four years were notable. In the case of the public sector, the favourable trend in the deficit explains the lower borrowing requirement.

Quantitatively, most of the growth was financed by an increase in the accounts of resident creditors. However, the other liability headings were more dynamic. Debt securities, in

(8) The figure for the consolidated balance sheet abroad is obtained by applying to the balance sheet total of Table I.2 the percentage of foreign business corresponding to each year.

The financial assets consist of: cash and deposits at central banks, credit institutions, lending to all sectors, securities portfolio and doubtful assets. The financial liabilities include: central banks, credit institutions, creditors of all sectors, debt securities and subordinated debt.

TABLE I.2

Consolidated activity of credit institutions (end-period data) (€ m and %)

	1998	1999	2000	2001	Business in Spain		Business abroad	
					2000	2001	2000	2001
ASSETS:								
Cash and central banks	16,096	26,090	25,140	34,801	54,2	59,7	45,8	40,3
Financial intermediaries	212,567	175,215	181,874	179,623	78,5	78,8	21,5	21,2
Loans and credits	518,215	591,482	730,997	805,627	79,1	82,3	20,9	17,7
Securities portfolio	194,746	224,520	287,428	301,180	59,5	68,5	40,5	31,5
Government bonds	*136,520*	*143,737*	*187,228*	*185,260*	*52,9*	*62,2*	*47,1*	*37,8*
Corporate bonds	*25,276*	*38,604*	*47,113*	*60,109*	*61,0*	*75,9*	*39,0*	*24,1*
Equities	*32,949*	*42,178*	*53,087*	*55,811*	*81,7*	*81,7*	*18,3*	*18,3*
Fixed assets	30,961	32,679	36,553	37,624	59,2	62,3	40,8	37,7
Other assets	42,188	56,739	97,638	100,395	61,6	64,8	38,4	35,2
Of which: consolidated goodwill	*4,082*	*6,148*	*19,825*	*19,375*		*37,2*		*62,8*
BALANCE SHEET TOTAL	**1,014,772**	**1,106,725**	**1,359,631**	**1,459,250**	**72,6**	**76,8**	**27,4**	**23,2**
LIABILITIES:								
Financial Intermediaries	268,614	261,411	290,399	269,339	74,0	82,3	26,0	17,7
Depósits	557,377	588,261	714,593	810,860	74,3	75,5	25,7	24,5
Debt securities	43,379	77,369	105,245	107,184	29,8	36,9	70,2	63,1
Subordinated debt	12,765	16,478	22,758	30,526	34,1	40,5	65,9	59,5
Provisions	27,523	29,868	54,743	56,828	53,7	66,1	46,3	33,9
Capital and reserves	60,078	70,755	95,881	102,963	77,5	78,4	22,5	21,6
Of which: minority interests	*9,959*	*15,852*	*21,805*	*22,131*	*24,5*	*26,7*	*75,5*	*73,3*
Other liabilities	44,801	62,584	76,011	81,549	78,6	77,8	21,4	22,2
Of which: negative first consolidation difference	*224*	*149*	*309*	*139*	*48,5*	*88,5*	*51,5*	*11,5*
Mismatch between areas of business (€ m)					38,570.0	52,539.0	–38,570.0	–52,539.0
MEMORANDUM ITEM:								
Net worth of managed funds	211,181	229,969	249,985	279,752				

TABLE I.3

Activity of credit institutions. Total business (€ m)

	1998	1999	2000	2001
ASSETS:				
Cash and central banks	12,076	19,718	14,249	21,015
Financial intermediaries	228,821	212,011	203,981	203,580
Loans and credit	472,202	534,942	622,626	694,700
General government	30,394	29,589	29,788	32,497
Resident private sector	409,246	472,091	554,035	618,882
Of which: Secured	*180,069*	*215,855*	*259,357*	*305,638*
Non-residents	32,562	33,262	38,803	43,321
Securities portfolio	176,740	204,333	230,038	258,041
Government bonds	105,619	102,908	96,958	104,236
Corporate bonds	32,251	51,145	57,496	72,963
Equities	38,870	50,280	75,584	80,842
Of which: Own group	*19,975*	*24,033*	*51,960*	*55,296*
Fixed assets	19,861	19,528	19,102	18,887
Other assets	39,636	46,148	63,757	67,814
BALANCE SHEET TOTAL	**949,336**	**1,036,680**	**1,153,753**	**1,264,037**
LIABILITIES:				
Financial intermediaries	298,833	296,098	294,996	291,431
Creditors	497,120	546,457	624,822	704,539
Of which:				
Resident private sector	432,983	454,140	507,441	563,657
Current accounts	*102,988*	*114,452*	*124,490*	*144,890*
Savings accounts	*92,259*	*104,953*	*107,473*	*120,149*
Time deposits	*150,971*	*158,709*	*190,642*	*208,438*
Repos	*86,295*	*76,009*	*84,549*	*89,762*
Other	*470*	*17*	*11*	*418*
Non-residents	46,885	74,456	97,283	107,580
Debt securities	15,935	38,100	33,928	40,649
Subordinated debt	15,582	21,790	33,885	44,678
Provisions	24,440	26,387	35,780	42,058
Capital and reserves	47,513	50,480	66,071	71,267
Other liabilities	49,913	57,368	64,271	69,415

particular subordinated debt, which grew at an annual rate of 42 %, and non-resident creditors (32 %) were notable. Own funds (capital and reserves) and provisions grew faster than the balance sheet, at rates of 14.5 % and 19.8 %, respectively. The growth of provisions in 2000, linked to the introduction of the statistical provision, was notable (35.6 %).

Interest rates on new business

The interest rates applied (9) by banks and savings banks in their transactions with resident customers fell notably in 1999, followed by an even sharper rise in 2000, before holding steady in 2001. However, in the second half of 2001 they began to turn downwards, in response to the progressive lowering of the Eurosystem policy interest rate, as can be seen in the data for the last quarter (see Table I.4).

Despite the upturn in 2000 and the relative stability over the last four years, nominal rates and, especially, real rates have, over the long term, followed a clear downward trend, as a consequence of the more stable economic environment associated with Spain's participation in Stage Three of EMU. For example, the average rate of all the institutions on loans for house

(9) These rates are equivalent annual rates, which take into account the periodicity of accrual and the commissions payable to the entity.

TABLE 1.4

Interest rates on new business with the resident private sector (in pesetas or euro) [Business in Spain (%)]

	Banks Memorandum item: last quarter							Saving banks Memorandum item: last quarter						
	1998	1999	2000	2001	2001 Oct	2001 Nov	2001 Dec	1998	1999	2000	2001	2001 Oct	2001 Nov	2001 Dec
LENDING:														
Credit accounts														
Threes months to one year	*4.93*	*3.94*	*5.31*	*5.35*	*4.59*	*4.73*	*4.51*	*5.87*	*5.56*	*6.68*	*6.57*	*6.00*	*6.22*	*5.96*
One year to three years	*5.54*	*4.24*	*5.23*	*5.41*	*4.80*	*5.05*	*4.29*	*6.29*	*5.35*	*6.26*	*6.11*	*5.82*	*5.98*	*5.05*
Personal loans														
Three years or more	*6.73*	*5.86*	*6.98*	*7.11*	*6.97*	*6.53*	*5.74*	*7.86*	*7.20*	*8.00*	*8.01*	*7.77*	*7.40*	*6.78*
Mortgage loans for the purchase of unsubsidised housing														
Three years or more (fixed and variable rate)	*5.34*	*4.54*	*5.62*	*5.48*	*5.22*	*4.91*	*4.64*	*5.58*	*4.91*	*5.89*	*5.94*	*5.68*	*5.46*	*5.12*
Variable rate credit (non-housing)														
Revisable monthly	*4.51*	*3.20*	*4.45*	*4.69*	*4.30*	*3.97*	*3.85*	*4.30*	*3.00*	*4.47*	*4.75*	*4.20*	*3.80*	*3.70*
Revisable every three or more months	*4.89*	*3.96*	*5.34*	*5.21*	*4.70*	*4.68*	*4.31*	*5.28*	*4.63*	*5.60*	*5.63*	*5.36*	*5.12*	*4.75*
BORROWING:														
Current accounts	2.21	1.41	1.79	1.79	1.57	1.57	1.57	1.91	1.50	1.95	2.11	1.93	1.80	1.66
Saving accounts	0.73	0.38	0.54	1.62	1.65	1.66	1.37	0.97	0.66	0.62	0.54	0.49	0.49	0.48
Time deposits														
Up to three months	*3.30*	*2.23*	*3.90*	*3.96*	*3.37*	*2.98*	*2.81*	*3.31*	*2.28*	*3.25*	*3.56*	*3.10*	*2.90*	*2.90*
One year and up to two year	*3.09*	*2.23*	*3.44*	*3.30*	*2.38*	*2.44*	*2.74*	*3.23*	*2.32*	*3.47*	*3.52*	*3.08*	*2.85*	*2.70*
Repos														
Up to three months	*3.81*	*2.64*	*4.04*	*4.24*	*3.78*	*3.75*	*3.26*	*3.88*	*2.64*	*4.01*	*4.28*	*3.85*	*3.39*	*3.26*
MEMORANDUM ITEMS:														
Variable rate credit (outstanding amount as at December)	77,469	96,395	140,350	160,295				106,574	129,229	159,248	189,951			
Total credit to "other resident sectors"	210,007	237,210	272,912	295,309				161,924	189,003	227,818	260,520			
Variable rate credit/total credit	36.90	40.60	51.40	54.30				65.80	68.40	69.90	72.90			

purchases was 16.7 % at end 1990 (10.2 % in real terms), 11 % (6.3 %) in 1995 and 4.85 % (1.25 %) in 2001. This fall in rates explains, in part, the growth of lending, since it has been easier to sustain the higher private debt ratios.

A high percentage of loans (54.3 % in the case of banks and 72.9 % in that of savings banks) are extended at variable rates. A very significant part of this type of lending corresponds to mortgage loans, which explains why this percentage is higher in the case of savings banks, given that a higher percentage of their lending to residents is in the form of mortgage loans (10).

Lending to the resident private sector

Lending to the resident private sector (business in Spain) represents 89 % of all lending. In the period 1998-2001 it grew at an annual rate of 14.8 %, which was higher than the rate for total lending (13.7 %), although it slowed to 11.7 % in 2001.

The higher growth rates in the period were linked to the construction and purchase of housing, as is apparent from the growth in mortgage lending (see following section) and lend-

(10) On sector estimates, 80 % of mortgage lending is at variable rates.

CHART 1.10

Lending by type (€ m)

ing to construction (11), which grew at an annual rate of 18.5 %, with a very sharp increase (51 %) in 2000. The slowdown in 2001 also affected the construction sector (9.4 %), while it only entailed a slight slowdown in lending to households for house purchases (Table I.A.4 gives a breakdown of lending to the resident private sector).

All the same, it was the services sector that continued to sustain above-average growth rates. In terms of the structure of lending to businesses, this has meant a gain in the share of services from 55 % in 1998 to 57 % today. The other sectors grew at lower than average rates and slowed in 2001, when they grew at all.

Lending to households (see Chart I.10), basically consisting of loans for house purchases and, to a lesser extent, consumer credit, grew at an annual rate of 15.6 %, somewhat faster than lending to businesses, owing to the expansion of housing loans. Consumer credit decelerated in 2000 and held unchanged in absolute terms in 2001.

Mortgage lending

Over the last four years managed mortgage loans (12) have grown at an annual rate of 20.4 % (see Chart I.11).

The high growth of mortgage lending to 2000 was a consequence of the cyclical upswing, and is explained, among other factors, by the fall in interest rates mentioned above and the parallel increase in the price of housing. This growth was expected to decelerate in 2001, at least in line with the slowdown in total lending to the private sector (of more than 5 pp). However, the failure of such expectations to be fulfilled may be partly explained, during the second half of the year, by fresh falls in interest rates and by processes associated with the introduction of the euro and falling stock markets, which may have stimulated a strong increase in the demand for housing and in house prices.

The annual growth of on-balance sheet mortgage lending (19.3 %) was somewhat lower than that of managed loans, since securitisation in the period led to the removal of significant

(11) Note that in Table I.A.4, the sum of lending to businesses and households exceeds the figure for lending to the resident private sector in Table I.3, although the latter includes total business and the former only business in Spain. This is because Table I.A.4 uses two different sources of data, which results in the double counting of lending to sole proprietorships, which in one case are treated as businesses and in the other as households.

(12) Managed lending comprises balance sheet balances and other loans granted by institutions, which are transferred, along with all their risks, to vehicle companies that issue securities, but which the institution continues to manage (securitisation). As compared with the balance sheet balance, managed lending gives a more accurate idea of mortgage activity.

CHART I.11

Lending growth rates (%)

balances from the balance sheet (see Chart I.A.5). In some years, the very institutions that originated the mortgage loans acquired some of the mortgage-backed bonds, so as to have high quality securities available for use as collateral in money market financing transactions.

Lending to households for house purchases (mostly mortgage loans) grew at an annual rate of 18.7 % (16.5 % in 2001), without counting securitisation. This shows that mortgage lending for purposes other than house purchases, although of relatively less importance, has been more buoyant.

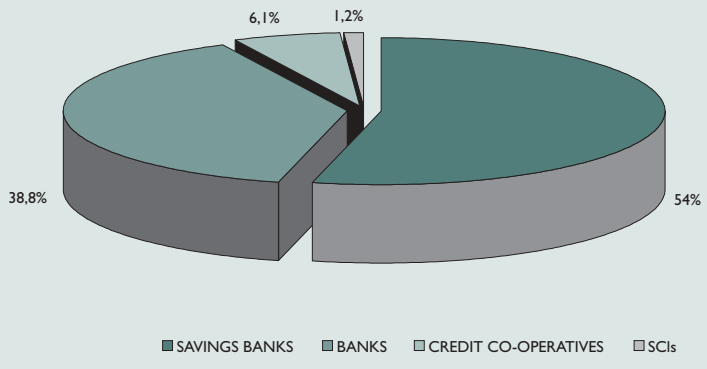
Savings banks account for 53.9 % of on-balance sheet mortgage lending and banks for 38.8 % (see Chart I.12). Since 1998, the former have increased their share by 1.1 pp at the expense of the banks. SCIs have only a small share of the market (1.2 %), although some of them are quite active in the securitisation business.

Securities activity

The securities portfolio has seen two major changes. Its composition has changed, as private-sector securities have increased while public debt has remained stagnant, and the distribution by portfolio has changed, with the permanent portfolio gaining weight at the expense of the others. The first change reflects the behaviour of the public-sector deficit mentioned above, and can be seen throughout the period, while the second one is linked to the significant acquisition of holdings in group companies and was especially prominent in 2000.

CHART I.12

Mortgage lending. Market share of each type of credit institution in 2001



The growth of corporate bonds is related to the change in the conduct of monetary policy in Stage Three of EMU. As a result of this change, the CIs required substitutes for government bonds to use as collateral when obtaining financing from the European Central Bank.

The securities portfolio of the DIs (13) can be considered conservative, both as regards its composition (see Chart I.13), with bonds making up more than 67 % of the total, and its distribution by portfolio, with the trading book representing less than 9 % of the total (see breakdown in Table I. A. 6).

Last year saw weak growth in the permanent portfolio, while the trading book grew by 15 % and the available for sale portfolio by 19 %, with the bond component proving especially dynamic. Also significant last year was the 11.7 % increase in the equities held in the trading book, despite the market instability from September.

Doubtful loans and their coverage

Doubtful exposures (in respect of loans, bonds and guarantees) vis-à-vis the resident private sector stood at 1 % of total at end-2001. Such a low level has not been seen in previous decades. Over the last four years total exposures have grown at an annual rate of 15.7 %, while doubtful exposures have declined by 2 % per annum, reducing the default rate from 1.57 % to 0.96 % (see Table I.5).

The improvement in the default rate is also confirmed when the net change in written-off assets (i.e. the difference between new write-offs owing to the expiry of the period in which recovery is considered probable and actual recoveries) is added to doubtful exposures.

The fall in total doubtful exposures has been accompanied by an increase in transfers to provisions. The specific provision for doubtful exposures declined during the period up to 2000, while the quality of debtors improved during the cyclical upturn, and held steady in 2001. The general provision, for other exposures, moves in accordance with the growth of activity and with the nature of the exposures (14). This latter provision increased by 12.2 % in 2001, as compared with an average annual rate of 17.2 % over the period.

In addition to these two traditional provisions, CBE 9/1999 established a new (statistical) provision to cover the potential losses on exposures estimated in accordance with historical experience. The strong growth in this provision in 2001 is explained by the fact that the circular only came into force in mid-2000, so that the transfers that year relate solely to the second half. In total, the amount of provisions is practically double (191.3 %) the amount of doubtful exposures (see Chart I.14).

Financing of activity

The interbank market provides, in net terms, somewhat less than 9 % of the financing of the activity of CIs. Its importance fell during the period by 1.6 pp, the whole of this fall oc-

(13) The figures in this paragraph, like those in Table I.A.6, take no account of data for SCIs. However, the weight of the latter in the total is very low.

(14) Mortgage lending for house purchases requires, when certain conditions are fulfilled, a smaller percentage of general provisions. By contrast, the shift from public to private-sector debt has resulted in higher requirements, given that no provision is required for public debt.

CHART 1.13

Credit institutions' securities portfolio

curring in 2001 (see Table 1.6), to approximately the level prior to the introduction of the new monetary policy arrangements, which notably increased the dependence of Spanish banks on interbank financing (15).

Among the other items there was a reduction of 3 pp in the financing of creditors, significant increases in the issuance of debt securities (16), subordinated debt and provisions, as well as relative stability in capital and reserves.

(15) The extent of prorating under the ECB's fixed rate tenders meant that the institutions had to have large volumes of bonds available to serve as collateral for the amounts requested. The Spanish banks, which lacked sufficient bonds, were forced to obtain financing from other financial intermediaries. In mid-1999 the ECB switched to using variable rate tenders with a reference floor, which significantly reduced the rationing of the amounts allotted.

(16) Its growth in 1999 must be related to the improvement entailed by the reform of the Securities Market Law. There was a notable increase in the issuance of commercial paper which, in terms of its withholding tax treatment, was put on an equal footing with public debt.

TABLE 1.5

Credit institutions. Doubtful exposures and their coverage
Total business (€ m and %)

	1998	1999	2000	2001
Doubtful assets and guarantees	7,521	6,655	6,417	7,076
Of which:				
Past due	*3,895*	*3,573*	*2,849*	*3,184*
Mortgage	*872*	*725*	*481*	*481*
Non-mortgage	*3,023*	*2,848*	*2,368*	*2,703*
Provisions	9,209	9,318	10,822	13,534
Specific	*5,257*	*4,734*	*3,913*	*3,933*
General	*3,952*	*4,584*	*5,678*	*6,369*
Statistical	*n.a*	*n.a*	*1,231*	*3,232*
Total exposures	478,128	557,733	655,894	741,169
Write-offs	19,039	21,902	22,144	22,262
Of which: write-offs during the year (a)	*3,691*	*2,368*	*2,082*	*1,601*
RATIOS (%):				
Doubtful/total exposures	1.57	1.19	0.98	0.96
Doubtful exposures/lending to other resident sectors	1.72	1.26	1.05	1.02
Doubtful exposures+write-offs during year/total exposures (a)	1.8	1.67	0.95	0.89
Provisions/doubtful exposures	122.4	140	168.6	191.3

(a) Not including SCIs.

TABLE 1.6

Financing of the activity of credit institutions (%)

	1998	1999	2000	2001
Assets	**100**	**100**	**100**	**100**
Loans and credits	70.41	69.72	70.31	70.1
Securities portfolio	26.36	26.63	25.98	26.04
Other (net) (a)	3.23	3.65	3.71	3.86
Liabilities	**100**	**100**	**100**	**100**
Financial intermediaries (net)	10.44	10.96	10.28	8.86
Creditors	74.13	71.22	70.56	71.09
Of which:				
Resident private sector	64.57	59.19	57.3	56.88
Current accounts	*15.36*	*14.92*	*14.06*	*14.62*
Savings accounts	*13.76*	*13.68*	*12.14*	*12.12*
Time deposits	*22.51*	*20.68*	*21.56*	*21.03*
Repos	*12.87*	*9.91*	*9.55*	*9.06*
Other	*0.07*	*0*	*0*	*0.04*
Non-residents	6.99	9.7	10.99	10.86
Debt securities	2.38	4.97	3.83	4.1
Subordinated debt	2.32	2.84	3.83	4.51
Provisions	3.64	3.44	4.04	4.24
Capital and reserves	7.09	6.58	7.46	7.19

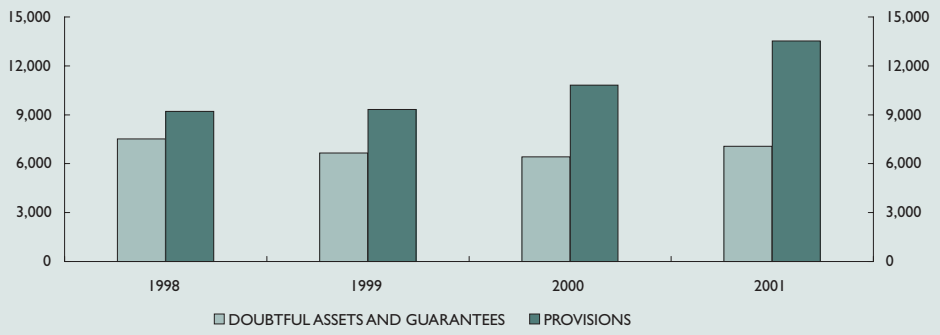
(a) Including cash and central bank. fixed assets and the net balance of other balance sheet accounts.

The loss of importance of creditors came to a halt in 2001, exclusively on account of the behaviour of public-sector creditors, owing to the transfer to the CIs of the balance of the Treasury's account with the Banco de España. There was also a slowdown last year in the loss of weight of resident private-sector creditors, influenced by the unfavourable developments on the stock market and in relation to mutual funds, the main alternatives to bank securities in the public's portfolio of financial assets.

Despite its loss of significance the resident private sector still provides 57 % of the CIs' financing. As regards its composition, this financing has remained relatively stable, with the exception of repurchase agreements, which fell by 3.8 pp over the period, as a result of the decline in public debt, the main instrument underlying such agreements. The improvement in the tax treatment of bank interest, from 1999, which was brought into line with that of mutual funds led to an increase in bank liabilities the following year, basically in the form of time deposits, which rose by almost 1 pp in that period.

CHART 1.14

Doubtful exposures and their coverage



The financing of non-residents amounts to almost 11 % with an increase of 4 pp over the period. In part, these deposits come from subsidiaries located offshore that raise funds by issuing securities on international markets.

I.2.3. Activity of individual institutions broken down by groups of institution

In terms of groups of institution, domestic banks account for 48.5 % of the balance sheet total for the CIs, and the savings banks for 36.5 %, while foreign banks represent 8.5 %. Credit co-operatives, with a share of 3.6 %, and SCIs, with somewhat less than 3 % complete the institutional spectrum (see Chart I.15). The period considered was characterised by a rise in the share of savings banks (32 % at end-1997) and by a loss in those of domestic banks (51.3 %) and foreign banks (11.2 %), while credit co-operatives and SCIs recorded small increases in their shares of the balance sheet total. In 2001, the decline in the share of the domestic banks steepened (–1.4 pp), while that of the foreign banks picked up (+ 0.4 pp), in particular that of the branches of EU banks, in line with the increase in their numbers.

Table I.A.7 shows how the various segments of activity are distributed across the institutional groupings. The differences are in some cases attributable to vocational factors and in others to historical differences in their regulation; the only remaining operational difference is the inability of the SCIs to raise deposits from the public.

As regards their assets, domestic and foreign banks have larger interbank positions and positions with non-residents, as well as larger portfolios of private-sector securities. Meanwhile, the savings banks, credit co-operatives and SCI's account for higher proportions of lending to the resident private sector.

As for their liabilities, savings banks account for 51 % of the funds of the resident sector and credit co-operatives for 6.4 %, which is almost double the share of the latter in the balance sheet total. By contrast, banks, in particular foreign banks, and SCIs (owing to restrictions on their operations) depend more on interbank financing. The domestic banks account for the bulk of subordinated debt, although the share of savings banks is increasing very rapidly.

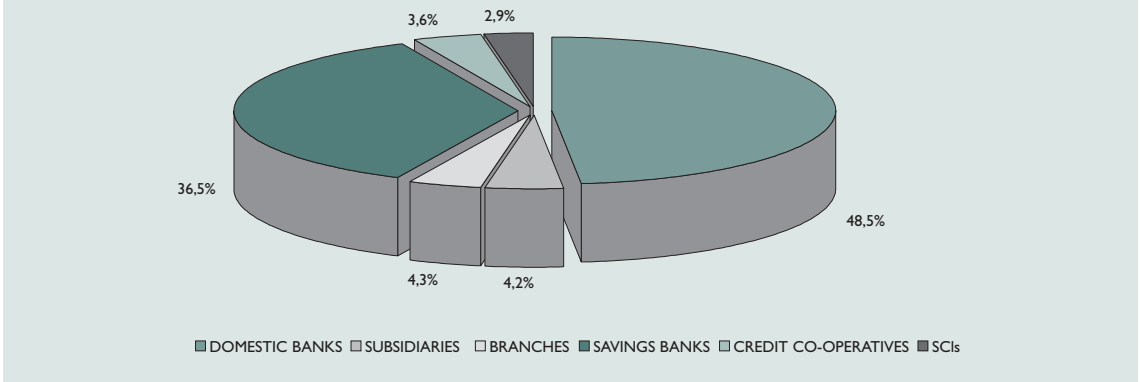
I.3. THE RESULTS OF DEPOSIT INSTITUTIONS

I.3.1. Results of consolidated groups

The significant growth of CGs during the period also left its mark on results. The margins of CGs in balance-sheet terms are clearly higher than those of the individual institutions. This is

CHART I.15

Share in balance sheet total of each type of credit institution



Box 1.1

The accounting framework for credit institutions

The Ministry of Economy and, by delegation, the Banco de España, have the power to establish and alter the *accounting standards and the financial statement formats* for individual and consolidated groups of credit institutions. The provisions issued by the Banco de España in this area, contained in CBE 4/1991 of 14 June 1991, apply and adapt the accounting standards stipulated by Spanish law to the sector of CIs and CGs.

The aim of this circular is to ensure that the balance sheet, profit and loss account, notes to the accounts and other supplementary statements give a true and fair view of the institution as regards its financial position, net profit and exposures. To this end, inter alia, the following principles are taken into account: historic cost, accruals, consistency, recording, no on- or off- balance sheet netting and, in particular, that of prudence of valuation. The latter has priority over the others in the event of any conflict between them.

To take account of the particular nature of the operations of credit institutions, CBE 4/91 sets out in great detail the criteria applicable to the valuation of rights and obligations and the recognition of profit and, owing to its importance, special attention is given to lending. Notable, for their economic significance, are the standards relating to provisioning for credit risk and country risk; those for the valuation of different portfolios of securities, according to their objectives, such as the trading book where the objective is short-term profit; those that attempt to discern the real effects of asset mobilisation operations or which seek to reflect relatively precisely the consequences of derivatives activities.

As the CIs are required by the Commercial Code to consolidate their financial statements with those of the financial institutions (other than insurance corporations) that make up their economic group, and for the purposes of assessing solvency, the accounting standards also include the different methods applicable to CGs. Global integration is the consolidation method normally used. The proportional integration method is only used when entities outside the CG share in the responsibility for managing the financial institutions. The equity method, which is more a valuation than a consolidation method, is applied to non-financial and insurance corporations that form part of the company's economic group, and to the companies in which the group has a stake or exerts a significant influence.

Finally, to enable the BE to carry out its control and inspection functions and the compilation of statistics of a monetary, financial and economic nature, CBE 4/91 provides for the periodical sending of numerous statements of a confidential nature. These shall reflect, with a high degree of detail, the different aspects of the net-worth and economic and financial situation of the institution according to the public information supplied by the institutions to the market.

because foreign subsidiaries normally start with wider net interest margins, the difference being even more pronounced in the case of the gross margin. However, the differences between CGs and DIs considered individually are smaller in terms of the net operating margin (owing to higher on-going expenses) and profit before tax (owing to higher provisioning, including amortisation of goodwill), up to the point that in 1998 and 1999 the differences in the latter variable were reversed in favour of the individual institutions.

Two sub-periods can be distinguished in the consolidated results of the period: 1998-2000 and the year 2001 (see Table I.7). The former is characterised by the stability of the net interest margin and by an increase in non-interest income, which generated an increase in the gross margin. This, together with the reduction in operating expenses, led to an increase in the net operating margin which, despite the higher provisioning needs, translated into an increase in profit before tax, which rose from 1.14 % to 1.29 % of average total assets (ATA) between 1998 and 2000.

The year 2001 was characterised by strong growth in net interest income, as a consequence of higher activity and of the consolidation during the year of some of the important subsidiaries acquired in the middle of the previous year. By contrast, non-interest income declined, owing to the unfavourable performance of securities markets and the decline in the net asset value of mutual funds, while the downward trend in operating expenses was sustained.

Provisioning (below net operating income) increased sharply and was only partly offset by the favourable trend in other income, in which profits on the disposal of investee companies were notable. Thus, in terms of ATA, the final items at the bottom of the profit and loss account subtracted 34 basis points (bp) from profit, as against 11 bp the previous year. This heavy amortisation of goodwill and provisioning stemmed largely from the Argentine crisis and from adverse developments on stock markets, and was a response to Banco de España requirements. As a consequence of all this, profit before tax fell to 1.16 % of ATA, although this was still more favourable than the 0.86 % of ATA recorded by the DIs (see Chart I.16).

The ROA of the CGs (profit after tax as a percentage of ATA) stood at 0.93 % in 2001, while their ROE (return on equity) (17) was 17.2 %. In 2000 these variables were 1.02 % and 18.5 % respectively, while in the European Economic Area (EEA) (18), in weighted average terms, they were 0.64 % and 15.9 % respectively.

I.3.2. Results of individual institutions

The first two years of the period analysed were characterised by a contraction, of around 10 bp per annum, in the *net interest margin,* which is basically explained by the fact that the reduction in interest rates had a greater impact (19) on financial income than on expenses (see Chart I.17).

As Table I.A.8 shows, in 2000 the contraction of the margin was curbed significantly (–2 bp), owing to activity growth, accompanied by structural improvements and an easing of the fall in rates. In 2001, this margin grew notably, to 2.44 % of ATA (2.18 % in 2000), with an increase of 24.9 % in absolute terms, which was double that in ATA (11.7 %). This growth stemmed from a widening of the spread on customer operations and, primarily, from certain significant dividend revenues obtained from holdings in CGs.

(17) Understood to be net worth, a subset of eligible own funds as defined for the purpose of solvency requirements.

(18) The European Economic Area includes, along with the EU countries, Norway, Liechtenstein and Iceland. However, the impact of these countries on the weighted averages is very small.

(19) Reference has been made above to the fall in rates, and in particular in mortgage rates, which the institutions used as the basis of their competitive strategies, and which had risen most.

TABLE I.7

Profit and loss account of consolidated groups of deposit institutions (€ m and %)

	1998			1999			2000			2001		
	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ
Net interest income	**25,236**	**2.61**	**9.5**	**26,594**	**2.58**	**5.4**	**30,689**	**2.59**	**15.4**	**36,907**	**2.70**	**20.3**
Non-interest income	10,704	1.11	19.6	11,667	1.13	9.0	14,573	1.23	24.9	15,945	1.17	9.4
Gross income	**35,935**	**3.72**	**12.3**	**38,261**	**3.72**	**6.5**	**45,263**	**3.82**	**18.3**	**52,852**	**3.87**	**16.8**
Operating expenses	–23,890	–2.47	13.4	–25,223	–2.45	5.6	–28,879	–2.44	14.5	–32,406	–2.37	12.2
Net operating income	**12,044**	**1.25**	**10.2**	**13,038**	**1.27**	**8.3**	**16,384**	**1.38**	**25.7**	**20,446**	**1.50**	**24.8**
Amortisation of goodwill	–1,370	–0.14	–36.0	–1,644	–0.16	20.0	–1,764	–0.15	7.3	–3,004	–0.22	70.3
Loan and country-risk provisions	–2,500	–0.26	–21.9	–2,569	–0.25	2.8	–3,672	–0.31	42.9	–5,869	–0.43	59.8
Securities and other write-downs	–1,112	–0.12	–	–563	–0.05	–49.4	–1,289	–0.11	129.0	–3,795	–0.28	194.4
Other net income	3,937	0.41	–51.0	4,357	0.42	10.7	5,640	0.48	29.4	8,042	0.59	42.6
Profit before tax	**10,999**	**1.14**	**15.4**	**12,619**	**1.23**	**14.7**	**15,299**	**1.29**	**21.2**	**15,820**	**1.16**	**3.4**
Profit after tax	**8,276**	**0.86**	**16.1**	**9,498**	**0.92**	**14.8**	**11,924**	**1.01**	**25.5**	**12,687**	**0.93**	**6.4**
Or which: of the group	*7,302*	*0.76*	*18.0*	*8,260*	*0.80*	*13.1*	*10,051*	*0.85*	*21.7*	*10,724*	*0.78*	*6.7*
MEMORANDUM ITEMS:												
Average total assets (ATA)	966,361		9.0	1,029,331		6.5	1,185,683		15.2	1,367,093		15.3
Return on equity		16.27			16.67			18.48			17.18	
Of de group		*17.55*			*19.32*			*22.16*			*21.17*	
COMPOSITION OF CONSOLIDATED GROUPS												
	No.	% annual Δ		No.	% annual Δ		No.	% annual Δ		No.	% annual Δ	
Globally consolidated institutions	1,220	5.4		1,234	1.1		1,381	11.9		1,342	–2.8	
Proportionately consolidated institutions	81	6.6		67	–17.3		76	13.4		96	26.3	
Institutions consolidated by equity method	1,290	14.5		1,401	8.6		1,598	14.1		1,653	3.4	
MEMORANDUM ITEM:												
Deposit institutions not belonging to any group (a)	169			161			158			156		

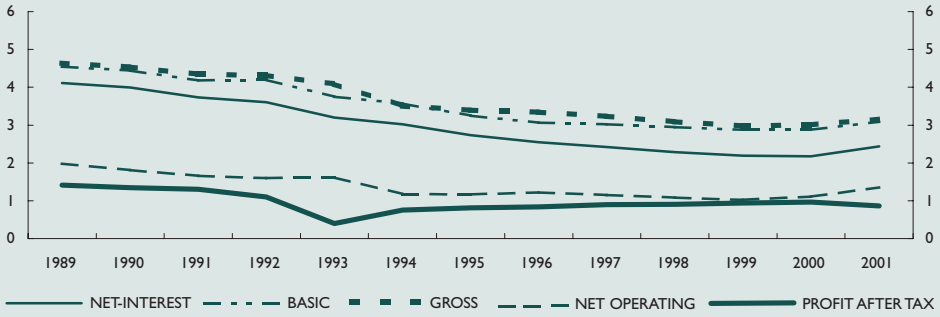
(a) Not including SCIs independent of Spanish deposit institutions.

The narrowing of the net interest margin was accompanied by a significant rise in fees and commissions receivable. The growth of this item was a consequence of the spread of charging for services provided and the increase in the activity generating this income: activity on securities markets, the privatisation of public-sector companies, IPOs and the marketing of non-bank financial products, in particular mutual funds. However, in 2000 the growth of this item stabilised, largely on account of lower mutual funds activity. In 2001 it grew by only 3.5 % (as against 11.7 % growth in ATA), owing to the unfavourable trend in securities trading, mutual funds and a certain slowdown in receipt and payment services. Table I.A.9 shows fees and commissions receivable along with the basic and gross margins.

Meanwhile, *profit on other financial transactions* has been in a sharp decline, which was only interrupted in 2000, owing to the favourable impact of currency valuation gains that year.

CHART 1.16

Main profit margins of consolidated groups of deposit institutions
Percentage of average total assets



Despite the unfavourable behaviour of non-interest income, there was a significant acceleration in the growth of gross *income,* prompted by net interest income. This was a change from the deceleration it had been displaying and from its stagnation in 2000, and enabled it to reach 3.16 % of ATA, which was higher than in 1998.

Following several years of weak growth, operating expenses accelerated in 2000, both in respect of personnel costs and other operating expenses. The former surged again in 2001, while the growth in other operating expenses was contained. However, despite these increases, the downward trend (see Chart I.18) since 1992 in operating expenses relative to ATA has been sustained (details of these costs are given in Table I.A.10, which also shows net operating income). The efficiency ratio, meanwhile, has improved over the last two years (operating expenses expressed as a percentage of gross income), to stand at 57 %, as against 65.5 % in 1999.

All this has favoured significant growth in net operating income, both in absolute terms and relative to ATA (to 1.35 %), after successive falls in previous years had taken it to a low in 1999 (1.03 %).

The trend in the *final block of items below net operating income* which, in total, deducted only 9 bp from the net operating margin in 1999, increased this deduction to 15 bp in 2000. The trend was exceptionally adverse in 2001, when these items absorbed 49 bp of the net operating margin, to leave the accounting profit before tax at 0.86 % of ATA (see Table I.A.11).

CHART 1.17

Return, average cost and differential. Total activity (%)

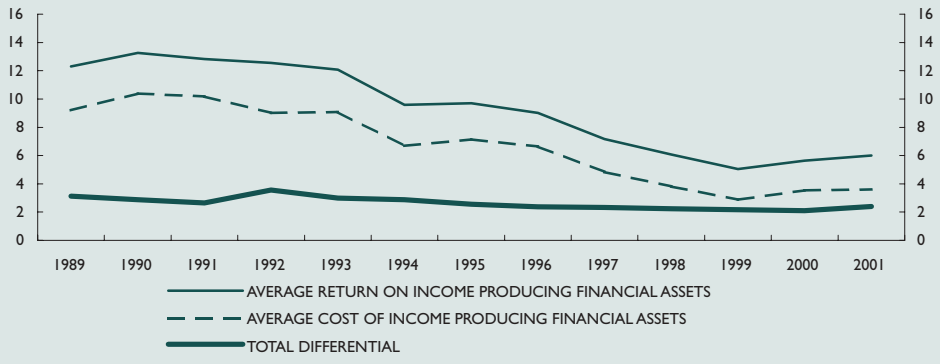
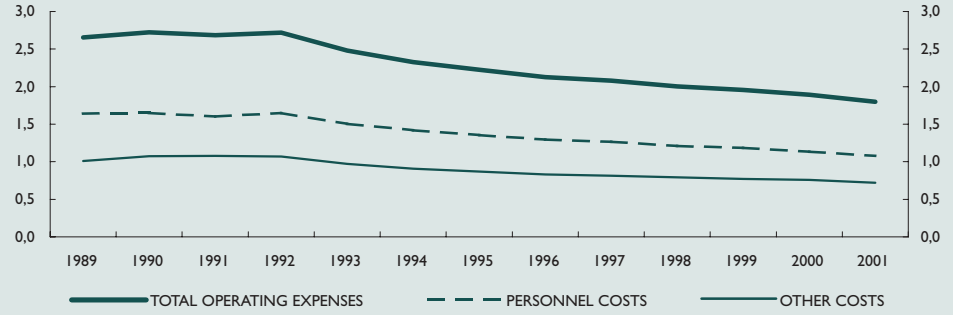


CHART I.18

Operating expenses
(percentage of average total assets)



The performance in 2000 is explained by the introduction of the new system of provisions for bad debts and by the higher securities provisioning requirements amid adverse stock market developments. That of 2001 is attributable to the lower profit on securities and real property sales and, especially, to the heavy provisioning.

As a result, the negative impact of the final block of the profit and loss account outweighed the improvement in the net operating margin in 2001. This opened up a significant gap, in terms of ATA, between the net operating margin and profit before tax, which reached levels not seen since the early 1990s. Even so, the ROA was 0.75 % in 2001, somewhat down on 2000 (0.81 %), but very much in line with its level during the period 1998-99 (see Chart I.19).

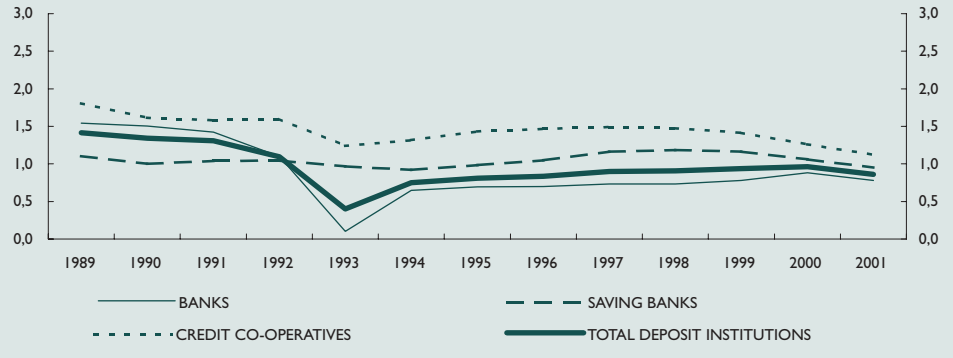
I.3.3. Provisioning by individual institutions

The provisioning referred to above, which includes that corresponding to doubtful and past-due assets, country risk, securities and other specific provisions, was increased in 2001 by 95 %, its weight in ATA rising by 26 bp, to 0.61 %.

The most notable example of this negative behaviour of provisioning in 2001 was the six-fold increase in securities write-downs, which absorbed 29 bp of ATA, from a level of 5 bp of ATA in 2000. The main reason for this response by the institutions was the greater need, on

CHART I.19

Profit before tax of deposit institutions
(percentage of average total assets)



account of the Argentine crisis, for write-downs of permanent holdings. As regards loan provisioning, this rose by 50.6 %, and by 7 bp of ATA, to 29 bp of ATA.

These developments were not the result of a deterioration in the quality of the loan portfolio, but a consequence of prudential regulation, since 2001 was the first full year of effectiveness of the new law on the statistical provision, which had only affected the second half of 2000. Indeed, the negative contribution of other provisions to the accounting profit fell in 2001, mainly because of the lower extraordinary transfers to pension funds, since the higher requirements introduced by a new law that came into force in 2000 had had to be covered that year. It is worth highlighting, although not because of its amount, that the positive impact of provisioning for country risk (negative amounts in Table I.8) is partly associated with the recovery of provisions available in the parent undertakings of CGs following the relocation of operations to other group entities (mainly foreign subsidiaries), although there was also some reduction in operations subject to cover. All this is reflected by more moderate figures in the consolidated statements.

The 86 % increase in the statistical provision is exclusively due to 2001 being the first full year of its application. In fact, the impact of the statistical provision has displayed a downward trend since its introduction in September 2000, in parallel with the increase in "net transfers to provisions for bad debts", which the statistical provision supplements. Even so, this impact has always been higher than that of other provisions for bad debts, which has led to the statistical provision representing 24 % of the provisions in the balance sheet, with an increase of 13 pp in 2001. As at December 2001, the cumulative balance of the statistical provision was € 3,117 million, 0.42 % of the overall credit risk, whereas a year earlier it had been only 0.18 %. This amount is still only 35 % of the upper limit to the provision. However, if the general provision for bad debts is considered along with the statistical provision, the percentage of credit risk covered rises to 1.26 % in 2001, slightly above the limit to the statistical cover.

The above-mentioned trends in the statistical provision are the result of divergent behaviour across the different groups of institution. The banks were responsible for the progressive moderation in the impact of this provision owing to the increase in the specific provisions of these institutions. By contrast, savings banks sustained a slight upward trend, while co-operatives showed a substantial increase linked to the strong expansion in their activities and recoveries of specific provisions and written-off assets.

I.3.4. Results by group of institution

In 2001, accounting profit before tax as a percentage of ATA was 0.78 % for banks, 0.95 % for savings banks and 1.12 % for co-operatives. At the same time, the profits of banks showed greater stability over time (if 2000 is excluded), while those of savings banks and co-operatives have been falling progressively. As a result the profit rates of these three groups have been converging (see Chart I.19).

The greater expansion of the business of savings banks and co-operatives (20) in recent years has been largely based on containment of the return on assets. In 1998 the average profitability of savings banks and co-operatives stood, respectively, at 38 bp and 62 bp above that of banks, while the equivalent rates in 2001 were 52 bp and 21 bp below that of banks. This has been possible owing to the low average cost of the liabilities of savings banks and co-operatives,

(20) The ATA of savings banks and co-operatives have grown over the last four years at a cumulative annual rate of 12.5 % and 12.7 %, respectively, as against 6.8 % in the case of banks.

TABLE I.8

Provisioning by deposit institutions (€ m and %)

	1998			1999			2000			2001		
	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ
Loan provisions	1,209	0.14	–16.7	1,250	0.13	3.4	2,264	0.22	81.1	3,409	0.29	50.6
Specific and general	*1,209*	*0.14*	*–16.7*	*1,250*	*0.13*	*3.4*	*1,228*	*0.12*	*–1.8*	*1,477*	*0.13*	*20.3*
Statistical	—	—	—	—	—	—	*1,036*	*0.10*	—	*1,932*	*0.17*	*86.6*
Country-risk	208	0.02	–13.8	8	0.00	–96.0	–121	–0.01	—	–146	–0.01	20.8
Securities write-downs	1,322	0.15	211.2	808	0.09	–38.9	554	0.05	–31.4	3,397	0.29	513.1
Other	847	0.09	–36.9	218	0.02	–74.3	949	0.09	335.4	447	0.04	–52.9
Total provisions	**3,586**	**0.40**	**3.7**	**2,284**	**0.24**	**–36.3**	**3,646**	**0.35**	**59.6**	**7,107**	**0.61**	**95.0**
Banks	2,110	0.37	14.8	1,220	0.21	–42.2	1,762	0.28	44.5	5,109	0.75	189.9
Savings banks	1,386	0.46	–7.6	983	0.29	–29.1	1,714	0.45	74.4	1,761	0.41	2.8
Credit co-operatives	90	0.31	–25.5	81	0.25	–9.8	171	0.46	109.5	237	0.56	39.0

which are 95 bp and 138 bp, respectively, below that of banks. However, this expansion of the activity of savings banks and co-operatives, with significant increases in employment and branch offices, has led to higher growth in their operating expenses.

I.4. THE SOLVENCY OF CREDIT INSTITUTIONS

I.4.1. The solvency ratio of consolidated groups

The solvency ratio, or the ratio between own funds and risk-weighted assets, of the CGs (calculated in accordance with Spanish law) as at end-2001 was 11.1 %, i.e. 3.1 percentage points higher than the required minimum of 8 %. If only tier 1 funds are considered, the tier 1 ratio was 8.7 %, so that tier 1 funds alone exceeded the solvency requirements (see Table I.9 and Chart I.20).

If instead of Spanish law the definition accepted by the Basel Capital Accord is applied, the ratio rises to 13 %, and the tier 1 ratio to 9.1 %. Alternatively, if a simulation were carried out based on the minimum required by the Community Solvency Directive (21), the ratio would be 12.2 % in 2001 and 11.7 % in 2000, which compares favourably with the EEA weighted average of 11.4 %.

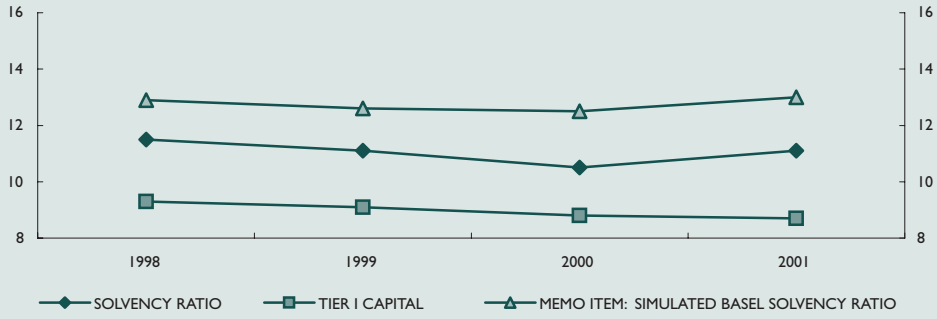
Over the period analysed, the ratio declined from 11.5 % in 1998 to the current level of 11.1 %, having reached a low of 10.5 % in December 2000. Since 1993, when the Community law on solvency was adopted, the ratio has fluctuated between a high of 12.4 % in 1996 and the above-mentioned low in 2000. By contrast, the tier 1 ratio displays a slow but sustained decline, from a high of 10.4 % in 1994, which seems to have bottomed out in the last two years.

In the distribution of values of the solvency ratio by intervals, CGs accounting for 63.5 % of assets come within the 10-11 % interval. During the period there was an increase in the concentration within this interval, although it should be noted that the distribution of assets

(21) Community legislation imposes minimum requirements which can be tightened by each Member State. In the Spanish case, the simulation exercise has been carried out considering, basically, the own funds that Spanish law does not recognise, but which the Directive would allow to be recognised. The differences in relation to requirements arise, primarily, from specific interpretations, so that they are more difficult to assess.

CHART 1.20

Solvency ratio of consolidated groups of credit institutions (%)



will be significantly affected from one year to the next by larger institutions moving from one interval to another. Cases of non-compliance (ratio of less than 8 %) are exceptional, temporary and relate to small institutions (see Table I.A.12).

Own funds

Own funds have the following structure: 79 % are tier 1 funds and 26.8 % tier 2, while deductions account for 5.9 %.

Own funds increased over the period at a cumulative annual rate of 15.5 %, which was higher than the growth of the consolidated balance sheet (12.9 %). By component, tier 1 funds grew at a rate of 14.3 %, while tier 2 funds were more dynamic (25.5 %), and the deductions from total funds grew at a cumulative annual rate of 55.6 %, after having doubled in 2000.

Tier 1 funds are 85 % capital and reserves, while the rest is mainly accounted for by (net) valuation differences of the consolidated companies. The reserves, in turn, include minority interests (of third parties outside the group), part of which corresponds to preference shares (22). Tier 1 funds are calculated net, having deducted those held by the group, losses and intangible assets (including goodwill).

In the period 1998-2001, the growth of tier 1 funds was driven by capital and reserves. In 2000 there was a significant increase in share premium reserve, which enabled new institutions to be acquired. Part of the increase in reserves corresponded to minority interests, located in the acquired institutions, and to the issuance of preference shares by foreign subsidiaries, which in December 2001 represented 21.7 % of tier 1 funds. In 2000 there was also a significant increase in goodwill, which reduced tier 1 funds. In 2001, the decline in profit moderated the growth of reserves. In spite of this, the growth rate of tier 1 funds was 9 %.

Subordinated debt (23) accounts for 92.6 % of the *tier 2 funds*. Their rapid growth is partly explained by their low starting level. However, it should be noted that, despite their development, these funds account for 33.9 % of tier 1 funds, well below their upper limit (50 %). *Deductions from total funds* arise from holdings in non-consolidated undertakings that exceed certain thresholds. These excess holdings are mainly found in financial institutions, although they also occur in non-financial firms.

(22) Securities of indefinite duration, normally without voting rights, which receive a fixed interest rate when there are profits and absorb any losses that may arise.

(23) Long-term debt securities on which interest is deferred in the event of losses. The claims of their holders come behind those of ordinary creditors.

Box 1.2

The statistical provision in the accounting rules for Spanish banks

Spanish bank accounts include a detailed classification of risk assets and of the provisions to cover them, distinguishing between general and specific provisions. A third category of provisions has recently been introduced called the statistical or dynamic provision. While the general provision is calculated for all loans, the specific one covers the losses on impaired loans and contingent liabilities and the statistical one seeks to cover potential losses in advance of impairment.

The statistical provision was introduced by CBE 9/1999 of 17 December 1999, which entered into force on 1 July 2000. Two methods may be used to calculate the statistical provision which differ in the way in which the embedded or expected losses are estimated: an internal method developed by the institution or a standard method. Both methods can be used at the same time, provided that they are applied to different portfolios.

The institutions' internal methods are based on their own experience of default and on expected losses on homogenous credit-risk categories, taking into account the quality of the different types of counterparty, the guarantees given and their recoverable value, the life of the operations, when relevant, and the future levels of risk arising from foreseeable changes in the economic situation in the medium and long term. Internal methods shall form part of a suitable system to measure and manage credit risk, shall use an historical database spanning a complete cycle and shall be checked by the Banco de España's Supervision Inspectorates. This approach is a stimulus for the banks to measure and manage credit risk in accordance with the new guidelines of the revised Basel Capital Accord.

The standard method described in Circular 9/1999 involves classifying the credit risk into six categories based on coefficients established by the regulator. The categories and coefficients established are:

1) No appreciable risk (0 %). Exposures vis-à-vis the public sector.

2) Low risk (0.1 %). Exposures vis-à-vis firms whose long-term debt is at least A rated by a reputable credit rating agency; and mortgage loans with an outstanding risk of less than 80 % of the value of the property.

3) Medium-low risk (0.4 %). Financial leases and other secured risks (other than those included in (2) above).

4) Medium risk (0.6 %). Exposures not mentioned in other categories.

5) Medium-high risk (1 %). Loans and credit to individuals for the purchase of consumer durables.

6) High risk (1.5 %). Credit card balances, current account overdrafts and credit account overdrafts, whoever the holder may be.

These categories roughly correspond to the different levels of portfolio credit risk. The coefficients reflect the average net specific provision over the business cycle. They are based on information for the period 1986-1998 and also take into account the improvements made to the measurement and management of risk by the CIs during that period. The objective of the statistical provision is, therefore, to anticipate the next business cycle and not merely reflect the past.

Transfers are made quarterly, on a cumulative basis over the year, to the statistical loan loss provision. The difference between the estimate (internal, standard, or a combination of both) of the total bad debts embedded in the different portfolios of homogeneous risks and the entity's net transfers for bad debts are charged to the profit and loss account. If this difference is negative, the amount shall be paid to the profit and loss account and charged to the fund set aside for this purpose, provided that there is a balance available.

The provision for the statistical coverage of bad debts shall be no more than three times the sum of the amounts of the different categories of credit risk multiplied by their related coefficients. This limit takes into account the maximum non-specific deduction (4 %) included in Directive 86/635/EEC. Finally, it should be noted that the statistical provision is not a tax-deductible expense.

CHART 1.21

Own funds of consolidated groups of credit institutions. Composition (%)

Risk coverage requirements

Risk coverage requirements rose during the period at a cumulative annual rate of 16.9 %, which was higher than the rate of 15.5 % at which own funds grew. This greater dynamism is explained by the rapid growth of activity and by the changes in its structure, involving a shift from the public sector (0 % weighting) to the private sector (100 % weighting). These weightings are applied prior to the general application of the 8 % capital requirement.

Credit risk accounts for 94 % of the requirements, while the risk associated with the trading book accounts for only 2.9 % (see Chart 1.22). Lower percentages are accounted for by foreign-exchange risk (2 %) and additional requirements (1.1 %) (24). During the period a very slight loss of weight is appreciated in credit risk and additional requirements in favour of foreign-exchange risk.

In turn, 87 % of *credit risk* relates to balance-sheet activity, a percentage that seems to have levelled out over the last two years, after declining in previous years. The capital requirements for balance-sheet activity grew at a cumulative annual rate of 16.4 %, as a consequence of an increase in activity (12.9 %) and of an increase in the average weighting, which rose from 52.4 % in 1998 to 58.3 % in 2001. This increase in weighting would have been greater had it not been for the growth in mortgage credit, whose basic component of lending for house purchase receives a weighting of 50 % (as against the normal 100 % for the private sector), provided that it satisfies certain characteristics (25). The rest of the credit risk relates to guarantees and contingent liabilities (12 %) and to counterparty risk on derivative instruments (1 %).

Market risk arises from the trading book (26). The requirements cover both the general risk (price risk), which relates to changes in market prices in response to changes in interest rates and other factors, and the specific risk, which relates to changes in the solvency of the issuer. Market risk represents 92 % of the total requirements for the trading book. The other requirements for the trading book relate to other risks, of which the most important is the

(24) The requirements of a consolidated group of credit institutions are the greater of: the result of applying to the whole group the requirements contained in CBE 5/1993, or the sum of applying to each category of institution included in the consolidation, its own specific requirements. If the latter are greater than those of the group, additional requirements are generated equal to the difference.

(25) The most important are that the loan granted is no more than 80 % of the appraisal value of the mortgaged dwelling and that the borrower occupies or rents it out.

(26) For the purposes of the risk of the trading book the following are also included: derivative instruments traded on organised markets as well as those that are not traded but serve to hedge the book; liabilities in respect of repos and securities loans and the underwriting of issues of securities that may be included in this book.

TABLE 1.9

Solvency ratio of consolidated groups of credit institutions (€ m and %)

	1998	1999	2000	2001
Own funds	**65,643**	**74,682**	**88,274**	**101,148**
Tier 1 capital	53,532	61,212	73,432	80,051
Tier 2 capital	13,705	16,655	20,724	27,104
Deductions	1,594	3,185	5,882	6,007
Requirements	**45,818**	**53,831**	**67,015**	**73,222**
Credit risk	43,193	50,443	63,079	68,835
Market risk	1,338	1,628	1,680	2,151
Foreign-exchange risk	684	1,053	1,357	1,444
Additional	603	706	900	792
***Solvency ratio* (%)**	**11.5**	**11.1**	**10.5**	**11.1**
Of which: tier 1 (%)	9.3	9.1	8.8	8.7
MEMORANDUM ITEM: *Solvency ratio.*				
Basel Capital Accord simulation (%)	12.9	12.6	12.5	13.0
Of which: tier 1 (%)	*9.8*	*9.5*	*9.2*	*9.1*
Simulation of EU regulation (%)	12.5	12.1	11.7	12.3

counterparty risk in relation to the derivatives included in the book. Of the total market risk, 84 % related to fixed income in 2001.

The increase in *foreign-exchange risk,* despite the launch of Stage Three of EMU, with the establishment of irreversible exchange rates between the currencies of the participating countries, is explained by the growing international presence of Spanish credit institutions.

In order to ensure that own funds are adequately distributed within the group, irrespective of compliance with requirements at the consolidated level, Spanish subsidiary credit institutions are also required to comply with an individual solvency ratio. In Spanish law, the individual requirements are the result of applying to the gross requirements of each subsidiary, a percentage (varying between 50 % and 90 %) that decreases as the holding of the CG in the institution increases. The funds shall be those recorded in the individual balance sheet of the institution.

This ratio is satisfied by a wide margin, since the funds represent almost 200 % of adjusted requirements (see Chart 1.23). The coverage improved significantly in 1998, to 235 %, declining over the next three years to 192 % in 2001.

CHART 1.22

Capital requirements of consolidated groups of credit institutions by type of risk

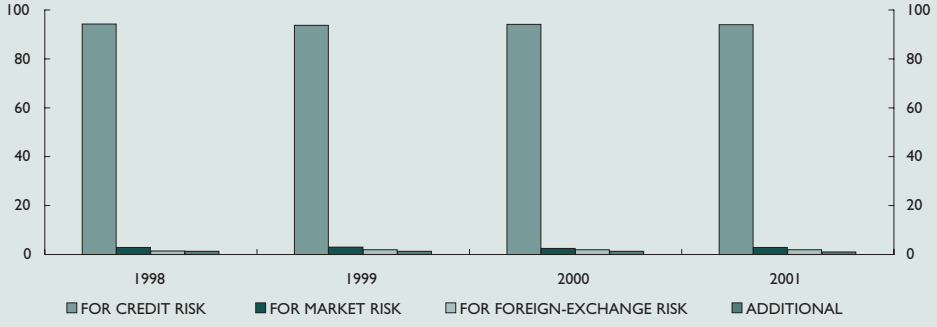
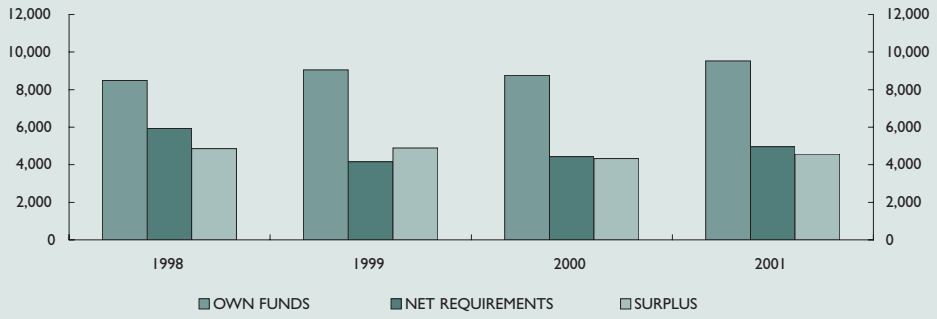


CHART 1.23

Solvency ratio of individual credit institutions belonging to consolidated groups (€ m)



I.4.2. The solvency ratio of mixed groups

Non-consolidated mixed groups of financial institutions subject to supervision by the Banco de España ("mixed groups") incorporate, along with CGs, their subsidiary insurance companies. Since 1997, mixed groups must comply with specific capital requirements. Their eligible capital is, basically, the sum of that of the CGs and the uncommitted assets of the insurance companies, having deducted any cross-holdings between these two components. The requirements shall, in turn, be the sum of the requirements for the CG and the solvency margin of the insurance companies, without taking into account the requirements corresponding to cross-risks, again to avoid double counting.

Within mixed groups, credit institutions are much larger than insurance companies, both in terms of own funds and capital requirements. As at December 2001, these groups had excess capital of 34 %. If 2000 is excluded, when this excess fell to 27 %, the percentage of excess cover remained the same in the other years (see Table I.10).

TABLE I.10

Solvency margin of non-consolidated mixed groups of financial institutions subject to supervision by the BE (€ m)

	1998	1999	2000	2001
Effective own funds	**54,608**	**63,205**	**68,653**	**76,115**
Credit institutions or groups	53,728	62,129	67,578	74,739
Insurance undertakings or groups	2,475	3,246	3,733	3,744
Deductions	1,594	2,169	2,657	2,367
Capital requirements	**39,506**	**47,153**	**54,028**	**56,909**
Credit institutions or groups	38,356	45,769	52,683	55,359
Insurance undertakings or groups	1,304	1,609	1,633	1,845
Deductions	155	224	288	294
Surplus or deficit of mixed groups	**15,102**	**16,052**	**14,624**	**19,206**
Surplus or deficit of CGs	**15,371**	**16,360**	**14,895**	**19,380**
MEMORANDUM ITEM:				
Number of mixed groups	36	37	35	34

TABLE I.11

Concentration of risks of consolidated groups of credit institutions (%)

	1998	1999	2000	2001
Concentration with single customer:				
Most important large exposure/own funds	18.2	20.9	20.9	19.3
Three most important large exposures/own funds	39.8	52.5	51.2	48.5
Aggregate large exposures/own funds	**48.7**	**82.6**	**86.8**	**79.3**

I.4.3. Concentration of exposures

Exposures are subject to the two limits envisaged in Community law. First, the total exposure vis-à-vis a single client or a group of interrelated clients shall not exceed 25 % (27) of the own funds of the CG (20 % in the case of non-consolidated companies belonging to the same economic group). Second, aggregate large exposures (those that individually account for 10 % or more of own funds) shall not exceed eight times the own funds of the CG. Both limits are strict, although the CG may opt to deduct the excess from its total own funds.

For the CGs as a whole, the most important large exposure (calculated as the weighted average of the largest exposure of each consolidated group or individual institution) accounts for 19.3 % of own funds in 2001, which was slightly lower than in previous years. If the three most important large exposures are considered, their average falls to 16.2 % in 2001 (see Table I.11).

Aggregate large exposures amount to 79.3 % of the own funds of the CGs, having increased very significantly in 1999 owing to a change in their definition (28). Aggregate large exposures were well within the limit of 800 % of the own funds of CGs.

(27) Until 31 December 1998 the limit was 40 %, and 30 % in the case of a company of the same group.

(28) Until 31 December 1998, the threshold for large exposures was set at 15 %.

APPENDIX

TABLE I.A.1

Number of employees, branch offices and ATMs of credit institutions

	1998	1999	2000	2001
	PERSONAL			
Total	**247,381**	**247,820**	**248,684**	**249,848**
Banks	135,164	131,460	127,582	123,613
Domestic	118,919	116,325	112,236	107,749
Foreign	16,245	15,135	15,346	15,864
Subsidiaries	12,878	11,733	11,902	12,169
Branches	3,367	3,402	3,444	3,695
EU	*2,659*	*2,764*	*2,874*	*3,168*
Other countries	*708*	*638*	*570*	*527*
Savings banks	93,812	97,276	101,718	105,593
Credit co-operatives	13,292	13,855	14,495	15,580
SCIs	5,113	5,229	4,889	5,062
MEMORANDUM ITEM:				
Employees/branch office	6,32	6,28	6,31	6,39
	BRANCH OFFICES			
Total	**39,167**	**39,449**	**39,389**	**39,104**
Banks	17,569	16,963	15,873	14,817
Domestic	16,063	15,609	14,541	13,452
Foreign	1,506	1,354	1,332	1,365
Subsidiaries	1,379	1,229	1,208	1,227
Branches	127	125	124	138
EU	*101*	*105*	*108*	*117*
Other countries	*26*	*20*	*16*	*21*
Savings banks	17,592	18,355	19,285	19,848
Credit co-operatives	3,607	3,740	3,888	4,092
SCIs	399	391	343	347
MEMORANDUM ITEM:				
Branch offices/1,000 inhabitants	0,99	1,00	0,99	0,97
	ATMs			
Total	**37,599**	**41,129**	**45,772**	**46,623**
Banks	15,042	16,193	18,470	17,590
Domestic	14,047	15,200	17,437	16,461
Foreign	995	993	1,033	1,129
Subsidiaries	981	977	1,017	1,114
Branches	14	16	16	15
EU	*14*	*16*	*16*	*15*
Other countries	*0*	*0*	*0*	*0*
Savings banks	20,198	22,300	24,331	25,625
Credit co-operatives	2,359	2,636	2,971	3,408

TABLE I.A.2

Concentration of the banking system (%)

	1998	1999	2000	2001
	VOLUME OF ASSETS			
The 5 largest banking groups	44.6	51.9	54.3	53.2
The 10 largest banking groups	58.7	62.4	64.3	63.6
The 20 largest banking groups	70.5	73.4	74.5	74.1
	LENDING TO RESIDENTS			
The 5 largest banking groups	42.9	47.9	50.4	48.9
The 10 largest banking groups	58.9	60.6	62.1	61.6
The 20 largest banking groups	71.3	72.2	72.9	72.5
	RESIDENT CREDITORS			
The 5 largest banking groups	37.7	41.6	45.0	43.7
The 10 largest banking groups	52.0	53.9	56.2	55.2
The 20 largest banking groups	68.3	69.3	71.0	70.2

TABLE I.A.3

Foreign business of consolidated groups and stand-alone credit institutions (€ m)

	1999	2000	2001
Consolidated foreign balance sheet (assets)	**211,500**	**372,428**	**338,932**
Financial assets	138,371	243,421	250,813
European Union	*31,232*	*47,563*	*54,154*
Latin America	*81,510*	*169,737*	*170,312*
Rest	*25,629*	*26,121*	*26,347*
Financial liabilities	125,656	246,553	245,899
European Union	*20,478*	*40,421*	*34,743*
Latin America	*73,448*	*147,866*	*155,829*
Rest	*31,730*	*58,266*	*55,327*
MEMORANDUM ITEM 1:			
Funds managed by groups (net asset value)	**24,668**	**50,972**	**74,490**
European Union	2,999	4,626	5,968
Latin America	21,209	44,673	63,285
Rest	460	1,673	5,237
MEMORANDUM ITEM 2: No. of banks abroad (a)			
Total	**181**	**185**	**185**
Subsidiaries	78	95	95
Branches	103	90	90
European Union	**83**	**79**	**82**
Subsidiaries	11	15	15
Branches	72	64	67
Latin America	**32**	**35**	**35**
Subsidiaries	28	31	32
Branches	4	4	3
Rest	**66**	**71**	**68**
Subsidiaries	39	49	48
Branches	27	22	20

(a) Subsidiaries or branches of deposit institutions.

TABLE I.A.4

Credit institutions. Lending to resident private sector (Business in Spain) (€ m and %)

	1998	1999	2000	2001	Structure 2001	Change 2001/2000
Lending to businesses	**214,783**	**243,712**	**293,985**	**321,468**	**100.0**	**9.3**
Agriculture and fishing	8,095	11,694	12,945	13,065	4.1	0.9
Mining and quarrying	2,808	3,271	3,281	3,202	1.0	-2.4
Manufacturing	46,433	54,426	59,735	62,336	19.4	4,4
Energy and electricity	11,423	10,715	12,211	13,231	4.1	8.4
Construction	27,318	27,534	41,480	45,380	14.1	9.4
Services	118,706	136,072	164,334	184,254	57.3	12.1
Lending to households	**199,764**	**235,262**	**276,242**	**308,680**		**11.7**
(as at December)						
Of which: consumer credit	36,652	43,326	48,570	48,876		0.6
MEMORANDUM ITEM:						
Number of credit cards (total)	42,137,080	46,015,992	49,696,626	62,611,232		26.0

TABLE I.A.5

Credit institutions. Mortgage lending to resident private sector (€ m)

	1998	1999	2000	2001
Managed mortgage loans	179,983	220,687	263,396	313,927
Of which: on balance sheet	*176,066*	*211,456*	*252,372*	*298,787*
Lending to households for house purchase (including non-mortgage lending)	123,243	145,171	176,639	205,774
MEMORANDUM ITEM:				
Credit linked to public housing programmes (not including SCIs)	22,021	21,965	21,428	20,503

TABLE I.A.6

Credit institutions. Securities: breakdown by portfolio (a) (€ m and %)

	1998	1999	2000	2001	Change	
					During year	2001/2000
TOTAL	**176,169**	**204,269**	**230,008**	**257,992**	**13.60**	**12.17**
Trading book	**20,371**	**16,711**	**19,872**	**22,889**	**3.96**	**15.18**
Bonds	18,413	13,565	16,536	19,164	1.30	15.89
Equities	1,958	3,146	3,336	3,725	23.90	11.66
Available for sale portfolio	**99,319**	**125,139**	**118,296**	**140,251**	**12.20**	**18.56**
Bonds	92,900	113,611	108,266	130,006	11.90	20.08
Equities	6,419	11,528	10,030	10,245	16.90	2.14
Permanent portfolio	**56,479**	**62,419**	**91,840**	**94,852**	**18.80**	**3.28**
Bonds	26,118	26,853	29,649	28,029	2.40	–5.46
Shares and other equity	30,361	35,556	62,191	66,823	30.10	7.45

(a) The figures are for banks, savings banks and credit co-operatives only.

TABLE I.A.7

Activity of credit institutions in 2001
Breakdown by type of institution (€ m and %)

2001	Banks							Savings banks	Credit Co-operatives	SCIs
	Total	Domestic	Foreign							
			Total	Subsidiaries	Branches					
					Total	EU	Other EU			
ASSETS:										
Cash and central banks	21,015	46.95	42.76	4.18	3.33	0.86	0.72	0.13	45.81	7.05	0.19
Financial intermediaries	203,580	68.59	53.11	15.48	8.24	7.24	6.83	0.41	27.42	3.35	0.64
Loans and credit	694,698	50.29	42.95	7.34	4.22	3.12	2.88	0.24	40.29	4.46	4.96
Government bonds	*32,496*	*56.47*	*49.49*	*6.97*	*4.55*	*2.42*	*2.26*	*0.17*	*38.28*	*1.47*	*3.78*
Resident private sector	*618,882*	*47.72*	*40.47*	*7.24*	*4.29*	*2.95*	*2.75*	*0.20*	*42.10*	*4.92*	*5.27*
Non-residents	*43,320*	*82.41*	*73.45*	*8.96*	*2.96*	*6.00*	*5.22*	*0.78*	*15.98*	*0.14*	*1.47*
Securities portfolio	258,043	63.50	56.89	6.61	1.51	5.11	4.98	0.13	34.66	1.81	0.02
Government bonds	*104,237*	*55.63*	*50.03*	*5.60*	*2.65*	*2.95*	*2.93*	*0.02*	*41.75*	*2.61*	*0.00*
Corporate bonds	*72,964*	*67.33*	*55.31*	*12.02*	*0.76*	*11.26*	*10.99*	*0.27*	*31.07*	*1.59*	*0.00*
Equities	*80,842*	*70.20*	*67.16*	*3.04*	*0.71*	*2.33*	*2.20*	*0.13*	*28.76*	*0.97*	*0.06*
Fixed assets	18,888	46.06	40.68	5.37	3.64	1.73	1.61	0.12	47.13	5.33	1.49
Other assets	67,813	71.25	62.65	8.61	3.17	5.44	5.22	0.22	26.13	1.60	1.01
BALANCE SHEET TOTAL	**1,264,037**	**56.94**	**48.45**	**8.49**	**4.23**	**4.25**	**4.02**	**0.24**	**36.50**	**3.64**	**2.91**
LIABILITIES:											
Financial intermediaries	291,431	71.34	50.80	20.54	7.14	13.40	12.86	0.54	18.72	0.74	9.20
Creditors	704,540	49.11	44.29	4.83	3.55	1.27	1.21	0.06	45.09	5.29	0.51
Of which:											
Resident private sector	*563,657*	*42.75*	*37.80*	*4.95*	*3.54*	*1.41*	*1.36*	*0.04*	*50.80*	*6.38*	*0.07*
Non-residents	*107,580*	*76.94*	*71.52*	*5.42*	*4.46*	*0.95*	*0.76*	*0.19*	*19.55*	*0.56*	*2.96*
Debt securities	40,648	54.16	52.91	1.25	1.25	0.00	0.00	0.00	43.94	0.37	1.53
Subordinated debt	44,678	67.79	66.60	1.18	1.16	0.02	0.00	0.02	31.08	0.33	0.80
Provisions	42,058	68.54	63.99	4.56	3.20	1.35	1.18	0.17	26.58	2.79	2.09
Capital and reserves	71,268	58.17	52.04	6.13	4.49	1.65	0.72	0.93	33.89	5.02	2.92
Other liabilities	69,414	62.27	53.50	8.77	3.00	5.78	5.44	0.34	31.85	2.29	3.58

TABLE I.A.8

Deposit institutions. Net interest margin (€ m and %)

	1998			1999			2000			2001		
	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% anual Δ
Financial income	50,522	5.65	–8.0	44,713	4.72	–11.5	54,442	5.25	21.8	64,575	5.58	18.6
Financial costs	–29,973	–3.35	–13.9	–23,873	–2.52	–20.4	–31,833	–3.07	33.3	–36,333	–3.14	14.1
Net interest margin	**20,549**	**2.30**	**2.3**	**20,841**	**2.20**	**1.4**	**22,609**	**2.18**	**8.5**	**28,242**	**2.44**	**24.9**
Banks	10,577	1.88	3.7	10,432	1.80	–1.4	11,326	1.82	8.6	15,488	2.26	36.7
Savings Banks	8,886	2.94	0.5	9,270	2.76	4.3	10,031	2.66	8.2	11,317	2.63	12.8
Credit co-operatives	1,087	3.70	2.8	1,139	3.51	4.8	1,252	3.41	9.9	1,437	3.42	14.8
MEMORANDUM ITEM:												
Average total assets	894,165	—	8.7	947,115	—	5.9	1,036,780	—	9.5	1,157.678	—	11.7

TABLE I.A.9

Deposit institutions. Basic margin and gross margin (€ m and %)

	1998			1999			2000			2001		
	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ
Fees and commissions	5,904	0.66	19.6	6,507	0.69	10.2	7,217	0.70	10.9	7,467	0.64	3.5
Basic margin	**26,453**	**2.96**	**5.7**	**27,348**	**2.89**	**3.4**	**29,826**	**2.88**	**9.1**	**35,709**	**3.08**	**19.7**
Non-interest income	1,290	0.14	-25.8	980	0.10	-24.0	1,339	0.13	36.6	830	0.07	-38.0
Gross margin	**27,744**	**3.10**	**3.6**	**28,333**	**2.99**	**2.1**	**31,164**	**3.01**	**10.0**	**36,540**	**3.16**	**17.2**
Banks	15,157	2.69	3.0	15,202	2.62	0.3	17,058	2.74	12.2	20,687	3.02	21.3
Savings banks	11,290	3.74	4.3	11,751	3.50	4.1	12,621	3.34	7.4	14,161	3.29	12.2
Credit co-operatives	1,297	4.42	4.8	1,375	4.24	6.0	1,484	4.04	7.9	1,691	4.02	14.0

TABLE I.A.10

Deposit institutions. Net operating margin (€ m and %)

	1998			1999			2000			2001		
	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ
Personnel costs	–10,878	–1.22	3.8	–11,235	–1.19	3.3	–11,756	–1.13	4.6	–12,472	–1.08	6.1
Other operating expenses	–7,106	–0.80	5.4	–7,328	–0.77	3.1	–7,854	–0.76	7.2	–8,397	–0.72	6.9
Net operating margin	**9,761**	**1.09**	**2.1**	**9,766**	**1.03**	**0.1**	**11,553**	**1.11**	**18.3**	**15,671**	**1.35**	**35.6**
Banks	5,223	0.93	2.6	5,077	0.88	–2.8	6,447	1.04	27.0	9,615	1.40	49.2
Savings banks	4,030	1.33	1.7	4,146	1.24	2.9	4,516	1.20	8.9	5,370	1.25	18.9
Credit co-operatives	507	1.73	0.8	543	1.67	7.0	591	1.61	8.8	686	1.63	16.1

TABLE I.A.11

Deposit institutions. Profit before tax (€ m and %)

	1998			1999			2000			2001		
	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ	Amount	% ATA	% annual Δ
Sales of securities and property	2,193	0.25	56.8	1,720	0.18	–21.6	3,550	0.34	106.4	1,611	0.14	–54.6
Loan provisions	–1,417	–0.16	–16.3	–1,258	–0.13	–11.2	–2,143	–0.21	70.3	–3,260	–0.28	52.2
Securities and other write-downs	–2,169	–0.24	22.8	–1,025	–0.11	–52.7	–1,503	–0.14	46.6	–3,835	–0.33	155.2
Results from previous years	329	0.04	–19.2	331	0.03	0.5	97	0.01	–70.9	264	0.02	173.3
Other income	–538	–0.06	24.8	–638	–0.07	18.6	–1,572	–0.15	146.2	–538	–0.05	–65.8
Profit before tax	**8,159**	**0.91**	**9.2**	**8,895**	**0.94**	**9.0**	**9,982**	**0.96**	**12.2**	**9,912**	**0.86**	**–0.7**
Banks	4,184	0.74	5.6	4,599	0.79	9.9	5,515	0.88	19.9	5,359	0.78	–2.8
Savings banks	3,542	1.17	13.7	3,836	1.14	8.3	4,005	1.06	4.4	4,084	0.95	2.0
Credit co-operatives	433	1.48	9.1	460	1.42	6.1	462	1.26	0.6	469	1.12	1.5

TABLE I.A.12

Distribution of consolidated groups of credit institutions by level of solvency ratio and their importance in terms of assets of the system (a)

	1998		1999		2000		2001	
	No. of CGs	% assets	No. of CGs	% assets	No. of CGs	% assets	No. of CGs	% assets
< 8 %	5	0.4	0	0	2	0.2	3	0.1
> = 8 and < 9 %	16	2.7	19	4.9	21	3.1	23	3.3
> = 9 % and < 10 %	31	17.2	24	17.9	36	58.5	24	7.6
> = 10 % and <11 %	22	21.9	32	39.7	23	10.1	38	63.5
> = 11 % and < 12 %	19	37.8	23	15.5	27	8.4	21	5.6
> 12 %	159	16.0	142	18.6	122	16.7	115	16.4
MEMORANDUM ITEM:								
No. of declarations (b)	252		240		231		224	

(a) The remaining assets, up to 100 %, correspond to institutions not subject to minimum capital requirements in Spain (mainly branches of EU institutions).

(b) The number of declarations of CGs (according to Table I.1 for 2001) = consolidated groups (32) + individual institutions (248) – inactive (5) – EU branches (48) – other branches subject to equivalent requirements (3).

II

BANKING SUPERVISION IN SPAIN

II.1. RATIONALE FOR THE EXISTENCE OF A PUBLIC BANKING SUPERVISION SYSTEM

International and Spanish experience has highlighted the need for special arrangements for the public supervision of financial institutions (especially credit institutions), on account of the important role of this sector in the economy, and in payment systems and financial intermediation in particular. Banking activity is commonly subject to specific regulations and a public supervision system owing to a number of important and generally accepted reasons.

These reasons revolve around the social importance of supervisory activity and the specific nature of banking. The business of a bank is highly leveraged, so that impairment of a small percentage of its assets may have a very significant impact on its own funds and, in consequence, on its solvency.

Supervision is an activity of great social significance because of the public interest it seeks to protect, namely, the smooth operation, efficiency and stability of the financial system.

Effective regulation and supervision contributes to the *smooth functioning* of the system as a whole by promoting the fluidity of financial intermediation mechanisms and generating confidence, on the part of savers, in the institutions. Banking is a business based on the confidence of depositors. It needs a suitable institutional environment, including a well-organised system of supervision, to make up partially for the inability of depositors to measure precisely the risk they are incurring.

Supervision is also conducive to *efficiency*. It requires and provides incentives for credit institutions (CIs) to adopt comprehensive and prudent risk-management systems, it promotes competition and it stimulates the adoption of practices that increase transparency for the customer and markets in general.

Finally, the basic objective of *stability* involves minimising the importance and cost of banking crises, on one hand, and avoiding outbreaks of "systemic risk" effects.

In short, banking supervision benefits the CIs themselves by providing a sound and prudent regulated channel for the pursuit of their business and a system of supervision to supplement that of the directors, shareholders and internal and external auditors. It also benefits depositors and investors, who can take their decisions in an environment marked by greater confidence, and society in general, which will have a healthy and efficient financial system.

Furthermore, the very nature of banking must be cited as a justification for the general existence of public models of supervision. Without a system of supervision of a business such

as banking, the achievement of the objectives of efficiency, stability and smooth functioning described above would be hindered.

The classic definition of a bank is *a business that receives funds from the public to invest on its own account in loan and credit transactions and, in addition to this channelling function, assumes the risks of liquidity, which arises when maturities are transformed, and of borrower insolvency.* This definition has the merit of capturing in a few lines two of the elements that best serve to characterise banking business, namely financial intermediation and risk management. However, since the activity of CIs has developed in line with financial and technological innovation, the definition is nowadays insufficient, both on account of the types of transactions referred to (deposit and lending) and the types of risk mentioned (credit and liquidity). The proliferation of new and increasingly complex instruments (e.g. financial futures, options, securitisation, credit derivatives) and the existence of numerous factors that daily management must bear in mind (counterparty solvency, interest rates, exchange rates, the maturity of transactions, procedures, applicable legislation, strategies and policies, etc.) have given rise to a wide range of risks that need to be subject to a process of regulation and prudential supervision if confidence in the system is to be maintained.

The reasons set out above also justify, in part, the existence of two other functions that supplement public banking supervision systems by seeking to contribute to the orderly management of situations of difficulty or crisis that may affect CIs. These are, first, the "lender of last resort" function whereby the monetary authorities address temporary liquidity problems and, second, that of the Deposit Guarantee Funds (DGFs), which are referred to in section II.3.

The public supervision systems and protection mechanisms mentioned above should be designed so as to enable market discipline to function properly.

II.2. THE SUPERVISORY POWERS OF THE BANCO DE ESPAÑA

Since 1962 various legal provisions have conferred on the Banco de España (BE) the power to supervise credit institutions and their consolidated groups (CGs).

Currently, the basic definition of the powers of the BE in relation to banking supervision is to be found in Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions (LDI), and in Law 13/1994 of 1 June 1994 on the Autonomy of the Banco de España (LABE). Other provisions supplement the regulatory framework in this area (see Box II.1).

The confidence of depositors in the sound operation of the banking system is fostered by modern public supervisory arrangements, which basically consist of two inter-related sets of rules. The first set consists of legal provisions that aim to guide and, where applicable, limit the operations that expose CIs to the various types of banking risk. This end is pursued through, inter alia, various controls on taking up the business and, among those rules relating to the pursuit of the business, through the so-called solvency coefficient. The second set of rules gives the supervisory authorities complete information on the actual economic, financial, net-worth and risk management situation of the CIs operating on the markets. Backing up both sets of rules are the coercive powers, on which the efficacy of the public supervision system ultimately hinges.

In particular, article 43 bis of the LDI reiterated that it is the BE's responsibility to oversee and inspect the CIs and their CGs. For its part, the LABE confirmed the supervisory function of this institution, establishing in article 7 (6) that the scope of such function includes both the solvency and the activities of the institutions and markets it has been made respon-

BOX II.1

Legal basis for the supervisory functions of the Banco de España

	LAW	ART.	SCOPE	CONTENT
1.	LAW OF AUTONOMY OF THE BANCO DE ESPAÑA (Law 13/1994 of 1 June 1994)	7.4	CREDIT INSTITUTIONS, OTHER ENTITIES AND MARKETS	The BE is made responsible for supervising CIs, and the possibility is envisaged that other laws will give it further powers.
2.	LAW ON THE DISCIPLINE AND INTERVENTION OF CREDIT INSTITUTIONS (Law 26/1988 of 29 July 1998)	43 bis	CREDIT INSTITUTIONS	The BE is made responsible for overseeing and inspecting CIs and their consolidated groups. This power extends to any branch office in or outside Spain and, insofar as necessary, to group companies. The powers of the BE over the branches of Community institutions operating in Spain is limited to reviewing their liquidity and checking their compliance with rules adopted in the interest of the general good.
			MORTGAGE MARKET	The BE is made responsible for overseeing and inspecting the mortgage market.
3.	LAW ON OWN FUNDS (Law 13/1985 of 25 May 1985)	9.2	CREDIT INSTITUTIONS	The BE is given powers to analyse non-financial entities controlled by banking groups, in order to determine their impact on the economic and financial position of the group. It can also analyse companies, to determine whether they should be consolidated with the economic group of the credit institution.
		12.2	CREDIT INSTITUTIONS	The BE is made responsible for supervising the prudential rules relating to certain non-consolidated mixed groups (normally those whose parent company is a credit institution).
4.	SECURITIES MARKET LAW (Law 24/1988 of 28 July 1988)	88	PUBLIC DEBT MARKET. BANKS' SECURITIES MARKET ACTIVITIES	The BE is empowered to supervise and inspect all the account holders and management entities of the public debt market, as well as the activities of CIs connected with the securities market. In all cases in which the powers of the BE and of the CNMV overlap, these two supervisory institutions shall coordinate their activities on the basis that effective supervision of the solvency of the institutions concerned falls to the institution that keeps the register while the functioning of the securities market is the CNMV's responsibility.
5.	LAW OF ADAPTATION OF 2ND BANKING DIRECTIVE (Law 3/1994 of 14 April 1994)	D.A. 10.[a]	APPRAISAL COMPANIES	The BE is given the task of inspecting and sanctioning ACs.
6.	LAW ON MUTUAL GUARANTEE COMPANIES Law 1/1994 of 11 March 1994	66	MUTUAL GUARANTEE COMPANIES REGUARANTEE COMPANIES	The BE is made responsible for overseeing and inspecting MGCs and reguarantee companies.
7.	LAW ACCOMPANYING THE 1997 BUDGET (Law 13/1996 of 30 December 1996)	48	CURRENCY-EXCHANGE BUREAUX	The BE is made responsible for supervising and overseeing currency-exchange bureaux.

sible for supervising and their compliance with the law, without prejudice to the powers of the regional (autonomous) governments (RGs). The legislation cited includes that which aims to promote the transparency of CIs both for their customers and the market. Accordingly, the BE's powers to supervise the CIs are exercised in accordance with the law currently in force and, in particular, in accordance with the oversight and inspection powers conferred on it by the LDI, i.e. access to the CIs and to information that may be relevant for supervisory purposes.

The BE's supervisory powers over Spanish CIs extend also to their branches abroad. In addition, the BE supervises the activities of branches of foreign CIs located in Spain, although in the case of branches of EU countries, in accordance with the directives in force, its powers are limited to checking the liquidity of the branch and compliance with rules adopted in the interest of the general good.

As a consequence of such inspection activities, and its supervision work in general, the BE can make any recommendations and requirements that may be necessary and also take the precautionary measures provided for in the legal system, including exceptional measures involving administration or the replacement of directors. At the same time, it should be noted that various laws give the BE powers to authorise certain operations and to open sanctioning proceedings and impose sanctions, with the exception of very serious ones, which the Ministry of the Economy has the power to impose, on a proposal from the BE, unless they involve the revocation of an authorisation, in which case only the government has the power to impose them. As for its legislative powers in the supervision field, the BE can only issue the necessary circulars to implement those provisions it has been expressly authorised to implement.

In all, as at 31 December 2001, the BE supervised 512 institutions, of which 369 were CIs (89 banks, 47 savings banks, 92 credit co-operatives, 56 branches of foreign CIs and another 85 institutions, basically specialised credit institutions).

Apart from CIs, the BE's supervisory powers, in accordance with specific provisions, also extend to 23 mutual guarantee companies (MGCs), which basically assume credit risk by granting guarantees to their members; to 49 currency-exchange bureaux, which buy and sell foreign currency and arrange money transfers, and to 74 appraisal companies (ACs), which carry out valuations of assets that may have effects in various financial spheres, such as the mortgage market, the valuation of property for insurance companies and the valuation of real-estate mutual funds.

Furthermore, as the BE has been made legally responsible for supervising Spanish consolidated banking groups, its oversight functions extend, in those respects necessary to exercise such functions, to 138 bank subsidiaries and specialised credit institutions abroad and to a wide range of non-bank financial subsidiaries.

Finally, the BE is responsible for promoting the smooth operation of payment systems, and has also been charged with particular supervision functions in relation to the public debt market and the mortgage market.

II.3. BASIC OBJECTIVES OF THE SPANISH BANKING SUPERVISION SYSTEM

As mentioned above, the basic aim of banking supervision is to safeguard the stability of the system, attempting to prevent the performance of the banking sector's important functions in the economy being significantly disrupted or even brought to a standstill. To carry out

BOX II.2

Cross-border activity

With other EU Member States

According to the provisions of Community law, on the basis of which harmonised conditions have been established for the taking-up and pursuit of the business of banking, the authorities of one EU Member State cannot prevent CIs authorised in other Member States from operating within their territory. The business of each institution throughout the Community is basically subject to the control of the supervisory authorities of the home country.

Consequently, Community CIs may operate in Spain, either by opening a branch or under the freedom to provide services, from the moment the BE receives notification from the supervisory authority of their home country containing the minimum information laid down for the purpose. The same rule applies, the other way round, to Spanish CIs that wish to operate in another Member State, although in this case the BE may oppose the opening of the proposed branch for reasons based on the financial or organisational situation of the Spanish institution in question.

The setting up of subsidiaries or the acquisition of holdings in an existing institution shall be subject in each host EU country to the domestic rules in force. These reflect the harmonised criteria on prior authorisation and minimum requirements laid down in Community legislation although, before pronouncing on the application, the competent authority shall obtain the opinion of the supervisory authority of the parent credit institution.

With non-European Union countries

The opening of a branch in Spain, the setting up of a Spanish subsidiary or the acquisition of a controlling interest in an existing Spanish CI by CIs from countries not belonging to the EU shall be subject to prior authorisation. The procedure involved is similar to the one for setting up new banks, which considers the suitability of the shareholders. However, authorisation may be refused or limited on account of, as well as failure to meet the requirements laid down for the purpose, application of the general principle of reciprocity. Activity in Spain under the freedom to provide services must be notified to the BE, which may make it conditional upon the fulfilment of certain requirements in order to guarantee compliance with rules adopted in the interest of the general good.

The opening of branches, the setting up of subsidiaries and the acquisition of holdings in an existing institution in countries not belonging to the EU by a Spanish credit institution is subject to, as well as the requirements to be fulfilled in the country in question, the prior consent of the BE. The latter may withhold its consent for a number of specified reasons, basically relating to the existence of obstacles to the performance of prudential supervision. The provision of services without an establishment shall be notified to the BE.

its legal mandate, the BE, like the other supervisory authorities of developed systems, directs its attention, in the first place, to the solvency and activities of the institutions, as stipulated by the LABE. The reasonable scope of banking supervision thus revolves around the basic tasks of safeguarding the stability of the financial system and monitoring its solvency and activities and has two facets:

- First, it is sought to *minimise the effects of individual crises*, although it is not possible to avoid the existence of badly managed or inefficient institutions and, therefore, no attempt is made to impede the market's disciplinary function. It is the managers of banks who are directly and solely responsible for their actions. Accordingly, the supervisory function involves designing and applying systems to analyse institutions, which help to forestall potential crises and to reduce their number, importance and cost.

- Second, the stability objective requires more than just reducing individual crises. It requires preventing one or more individual crises from generating a chain of default affecting the system as a whole. To this end, it is essential to ensure the smooth operation of payment systems and to establish proper protection against risks of contagion. The minimisation of "systemic risk" is certainly a concern (and supervisory task) of the utmost importance, to which the greatest effort is devoted.

In any event, efficiency is strengthened through the response of institutions to competitive forces. This is why banking supervision cannot be interventionist, but must be respectful of market mechanisms and the autonomy of directors and managers in business matters.

In view of its legal mandate, the BE's supervision is designed to verify compliance with the specific banking provisions for which it is responsible, among which should be highlighted, along with those relating to the financial situation and solvency of the institutions, those relating to customer protection and transparency vis-à-vis the market. This entails the adoption of appropriate measures, including, where applicable, the opening of sanctioning proceedings.

In this context of verification of compliance with specific financial provisions it is important to point out that there are other provisions that do not affect CI's alone, and which other authorities are responsible for supervising, in particular:

- The tax authorities, with powers in relation to tax provisions.

- The National Securities Market Commission (CNMV), with powers in relation to the operating rules of such markets.

- The Directorate General of Insurance (DGS), responsible for provisions relating to insurance contracts and pension funds.

- The Commission for the Prevention of Monetary Laundering and Money Offences, with powers in these fields.

Nevertheless, although the Inspection Department of the BE does not have powers over the above matters, and its activities are not planned with a view to verifying them, when in the course of its work information is obtained that may interest other authorities, they are notified of it, where appropriate, in accordance with the provisions of the law. Moreover, the BE takes

an active approach in this respect, requiring CIs to comply with all the provisions that regulate both their activity in Spain, and the activity of their branches and subsidiaries abroad, especially those intended to avoid the financial system being used for illicit purposes.

The supervisory functions of the BE are specified and framed in the light of the objectives mentioned above, which enables them to be distinguished from others with which they sometimes have common features. Among the latter the following should be noted:

Management and administration of institutions. The directors and managers are responsible for their activities, successes and failures. The supervisor, for its part, carries out the necessary analysis and verification to obtain a reasonable awareness of their solvency and situation, using for the purpose the most appropriate procedures in the light of the situation of each institution, taking into account its size, complexity, risk profile and the possibility that potential difficulties in the institution or default thereby may spread to the financial system. Such activities do not involve, nor could they involve, exhaustive review of the operations carried out by the institution. That task is only entrusted, exceptionally, to legally appointed administrators, in accordance with the provisions of the LDI, in particularly serious cases.

External auditing of accounts. The external auditor is required to check and report whether the annual accounts give a true and fair view of the net worth, financial position and net profit of the company audited. It states its opinion in a report filed at the Mercantile Registry, to ensure that it has adequate publicity and to secure the relevant effects vis-à-vis third parties. The BE also carries out data verification tasks during its on-site inspections as part of the continuous supervision of CIs and CGs, but its work is focused on the achievement of the objectives described above, not on supplying information to third parties on the conclusions reached. In fact, with the exceptions expressly provided for, all the data and information in its possession is secret and may not be divulged to third parties (see article 6 of Royal Legislative Degree 1298/1986 of 28 June 1986).

At the same time, external auditors, in accordance with the technical rules that regulate their activity, assess the viability of CIs over a one-year time horizon, while the supervisor makes its assessment without any limit. However, the annual report of the external auditors furnishes confidence to the system insofar as it is periodic, independent and public, and provides information that is useful to the supervisory authorities themselves.

Internal auditing and risk control. Internal auditors review the different areas of the institution, ensuring that the internal controls established by the directors and managers, including the internal rules and procedures in force, are correctly applied. In a broad sense, internal auditing is one more element of CIs' system of management, although its function is not legally recognised. The supervisor, for its part, relies on the work of internal auditors, among others, and like them performs checks, but it never takes part in the management of CIs.

Investor compensation and deposit guarantee schemes. As mentioned above, financial supervision seeks to give the system the necessary stability, which involves a reduction in the probability of bank crises. In this respect, supervision is, indirectly, a means of protecting depositors and creditors in general. However, the supervisory authorities cannot guarantee, in the strict sense, the transactions of bank customers.

To carry out that function, guarantee schemes have been organised in developed countries which, in the event of crisis, provide for the repayment of deposits or for compensation for the loss of securities entrusted to CIs, on certain conditions. The Spanish scheme, basically regulated by Royal Decree 2606/1996 of 20 December 1996, on Credit Institutions' Deposit Guarantee

Funds, is financed by the CIs themselves (although it is envisaged that the BE could be authorised by law to make contributions for exceptional reasons). This Decree sets a limit of € 20,000 on the compensation paid to depositors and another limit, of the same amount, on that paid in respect of securities or financial instruments deposited with CIs for the purpose of provision of an investment service.

Independent external analysis of CIs. External analysts and rating agencies make an independent assessment of the situation of each institution, normally for the purpose of guiding the decisions of potential investors. The supervisory process also involves analytical work, but its purposes are limited to the securing by the supervisory authority of the information necessary to take its decisions.

When exercising its supervisory powers the BE is mindful of the objectives and limits of its function. Accordingly, to assign its resources efficiently, when drawing up its supervision plans it takes into account the importance and the risk profile of each institution and the priority that it should afford to the monitoring of its solvency.

In addition, the supervisory activities of the BE are based on prudence, since they are directed at a very sensitive sector which is founded on confidence. Its activities thus have a constructive orientation, since their objective is to solve the problems that are identified to the benefit of the solvency and viability of the CIs and of the stability of the system. Accordingly, the supervisor must accumulate sufficient evidence before taking appropriate action. This involves carrying out numerous activities with discretion possibly over a long period. In addition, the supervisor, must have the agility to take urgent measures in the event of a situation of crisis.

II.4. BANKING SUPERVISION AND ITS RELATIONSHIP WITH OTHER FINANCIAL SUPERVISION AGENCIES

Supervision of the financial system is organised on an institutional basis. Thus, each institution is registered at a single supervisory centre, even if its activity is diversified. This individual allocation is based on the legal status of each institution. In practice it depends on which of the three main financial activities (banking, securities and insurance) makes up the core of its business.

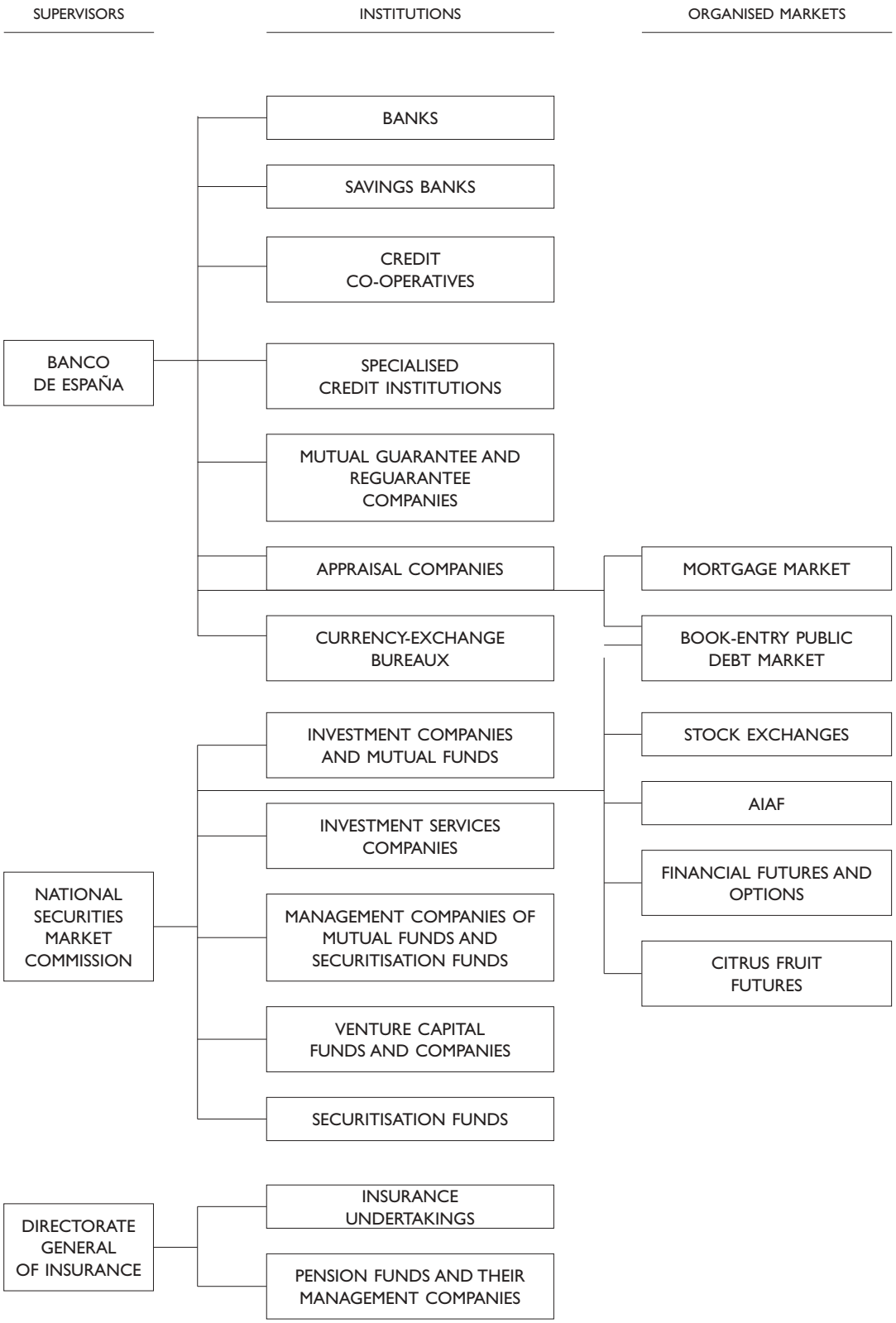
Considering that the different elements of these three types of activity give rise to different risks, have different objectives and require different supervisory procedures, there are three specialised supervisory centres in the Spanish financial system: the BE which, besides being a central bank belonging to the European System of Central Banks, is also responsible for the supervision of CIs; the CNMV, dedicated to the sphere of marketable securities; and the DGS of the Ministry of Economy, which has in its charge those entities whose business is basically focused on insurance contracts (see Box II.3).

In the case of CGs of financial institutions encompassing different kinds of entities, the determination of which agency is responsible for their supervision depends on the nature of the controlling entity and, in the absence thereof, on the type of their main activity. Rules establish the necessary collaboration between supervisory agencies to ensure that mixed groups are duly monitored and also to improve the performance of their respective supervisory functions. The state organisation of supervision also includes the Ministry of Economy, which has, inter alia, the power to authorise institutions and to impose very serious sanctions, notwithstanding the autonomy with which the above-mentioned agencies carry out their supervisory functions.

Completing this range of supervisory institutions are the regional (autonomous) governments, which have assumed supervisory powers over regional securities markets and over cer-

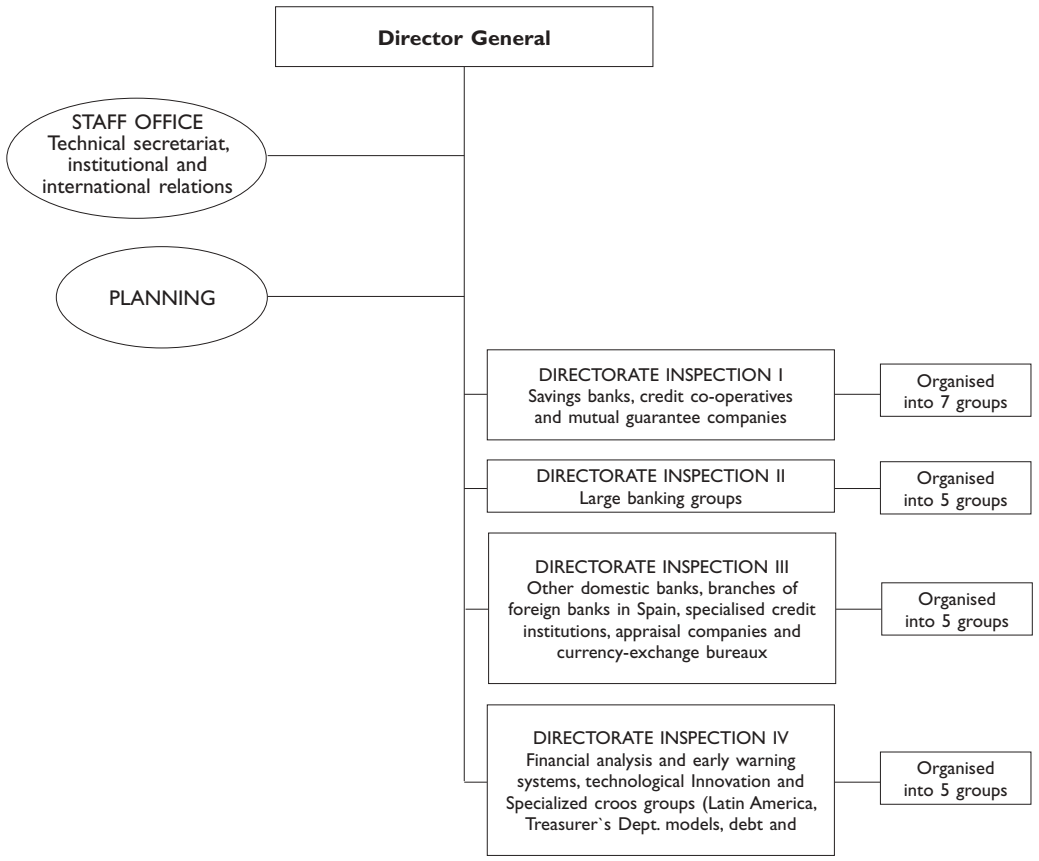
BOX II.3

Financial supervision agencies in Spain



BOX II.4

Directorate General Banking Supervision: Organisation Chart



tain aspects of savings banks and credit co-operatives (the latter point is discussed in greater detail in Annex I of this report).

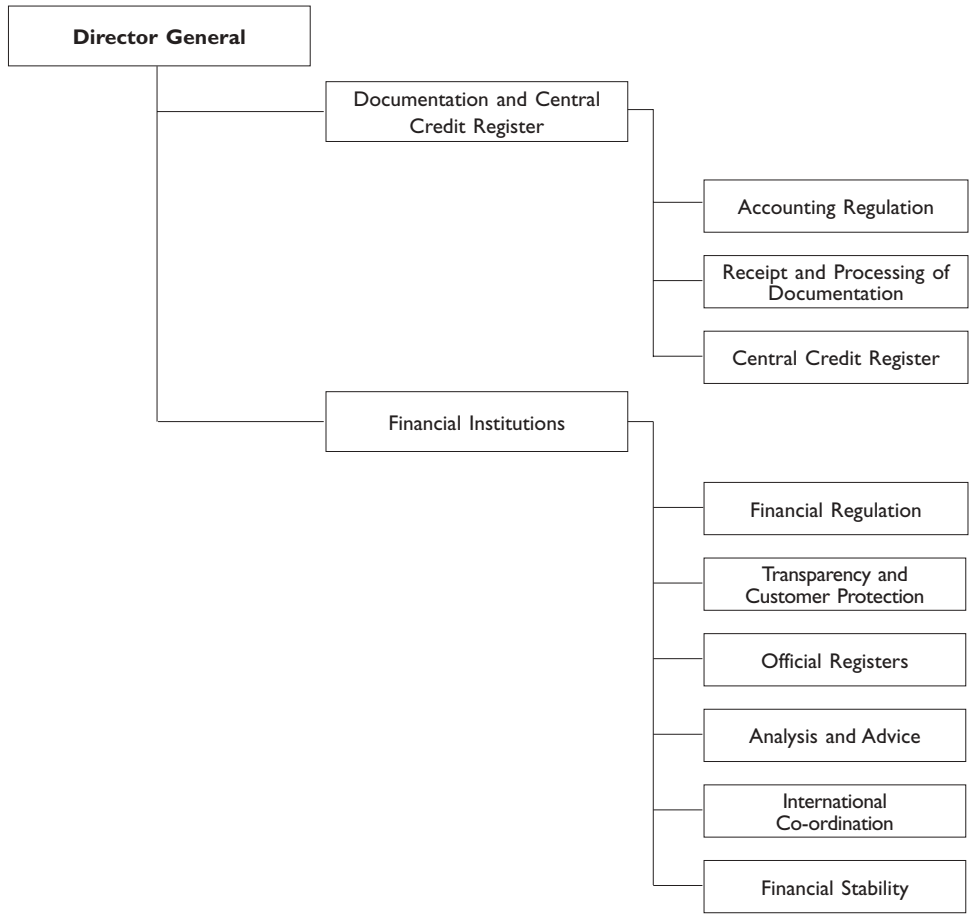
Within the BE, the power to take decisions is vested, in accordance with its internal rules, in the Executive Commission, subject to the guidelines of the Governing Council, while the function of banking supervision and regulation is organised into two general directorates: the Directorate General Banking Supervision and the Directorate General Regulation (see Boxes II.4 and II.5).

The Directorate General Banking Supervision basically has the powers to supervise the credit system, analysing the situation of the CIs and their financial groups, to verify legal compliance, to formulate proposals for the adoption of disciplinary or preventive measures, to conduct the administrative procedures for which it is responsible and to collaborate with national and foreign agencies on supervision matters.

The Directorate General Regulation is basically in charge of the preparation of reports and proposals relating to financial regulation, advice on technical and economic aspects of banking policy, designing the information CIs must submit to the BE and processing it, conducting the administrative procedures for which it is responsible and collaborating with other domestic and foreign agencies on the above matters. It also has in its charge the official register of CIs and other entities.

BOX II.5

Directorate General Regulation: Organisation Chart



Both directorates general participate and collaborate closely in the definition of the banking supervision and regulation policy applied by the BE. To improve banking supervision, this collaboration is supplemented by contributions from other parts of the BE, such as the Directorate General Operations, Markets and Payment Systems and the Legal Services.

II.5. THE BASIC COMPONENTS OF THE SPANISH MODEL OF BANKING SUPERVISION

The location of the banking supervision function within the BE is helpful for the performance of the function of monitoring the stability of the system for which every central bank is responsible and enables the information synergies that arise from having the powers typical of a central bank as well as those of banking supervision within a single institution to be exploited. Thus, the orientation of the supervisory work benefits from the overall analyses of the Spanish financial and credit system carried out by the BE and, in general, from the knowledge afforded to it by its attention to the general economic situation and, in particular, to the money and financial markets, as well as the operation of the payment systems.

To achieve its objectives, the BE must always maintain a well-founded and up-to-date view on all factors (both quantitative and qualitative) that shed light on the risk profile of the CIs and CGs, their solvency and degree of compliance with applicable rules, in order to assess

their stability and future viability and to be able, where applicable, to take the prudential or legal measures necessary.

For this purpose, and in line with the international standards for effective bank supervision, the Spanish model incorporates the elements included in Box II.6, which are discussed below.

II.5.1. Effective and prudent regulation

Three major groups of rules can be distinguished: *a)* rules on taking up the business, which include prior authorisations subject to certain conditions for setting up CIs, the acquisition of qualifying shareholdings, registration in the register of directors and senior executives, etc.; *b)* rules on conduct of the business, such as the minimum capital requirements, according to the level of risk, limits on risk concentration, limits on the acquisition of shareholdings, authorisation of branches and subsidiaries outside the EU, requirements for adequate internal control systems, rules on transparency and customer protection, accounting regulations, etc., and *c)* banking discipline.

As Box II.8 shows, the participation of the BE in the process of drafting prudential regulations is limited to those aspects for which it is expressly authorised by higher-ranking provisions. In fact, the government and the Ministry of Economy play a prominent role in this process, unlike in some other countries.

The formulation of accounting regulations as a supervisory tool requires particular comment. This power is conferred by the current LDI on the Ministry of Economy, which is authorised to delegate it to the BE, as it has indeed done since the 1960s. This power has enabled the BE to adapt the general accounting regulations to the specific characteristics and ongoing operational innovation of the sector, as well as the challenges that general economic developments have posed. Notable, in particular, are the rules on minimum provisions for bad debts and, in general, all the rules on prudent valuation of assets, liabilities and commitments recorded off-balance sheet.

Prudent accounting standards, which in banking must be especially so, due to the characteristics of the business and its risks, are essential to ensure that the balance sheet figures reflect all the losses that can be reasonably expected and, therefore, that the solvency data derived from it are reliable. The figures for own funds and the solvency ratios are only useful if there is first sufficient certainty regarding the prudent valuation of the balance sheet figures, i.e., if the provisions to cover any capital losses are adequate.

II.5.2. Broad information system

The BE collects from the CIs, on a compulsory basis, for prudential supervision and also statistical reasons, a wide range of information. This includes economic and financial information (balance sheets, profit and loss accounts, external auditors' reports, solvency reports and supplementary details); the information of the Banco de España's Central Credit Register, which includes comprehensive information on the credit risks of each customer; information on shareholders; information on directors and senior executives, etc.

In addition to this information, which the CIs send periodically, the BE increasingly makes use of the CIs' own internal management information and documentation relating to strategies, risk assumption policies, organisation, internal control systems, etc. It also analyses the information on CIs generated by the market.

II.5.3. Adequate resources

Banking supervision is one of the functions performed by the BE, which allocates the necessary human and material resources. The former are in a process of growth and their quality is the main basis for effective supervision (see Table II.1). Along with the human resources, the IT tools and other material resources require significant investment as databases, programs for processing and analysing information and computer systems to support the verification work are continuously being prepared, updated and improved.

The costs of supervision are paid for out of the BE's budgets. The supervised CIs do not participate in the financing of such costs, unlike in some other countries and sectors (1).

II.5.4. Continuous analysis and monitoring

Each institution is overseen and analysed by a team of persons who are given the task of keeping up-to-date with its situation by monitoring all the information mentioned above. This information is qualitatively enriched, like the supervisory function as a whole, by constant direct contact with management.

From the organisational viewpoint, the task of analysing and monitoring CIs and their CGs falls to Inspection Groups. The assignment of this task to these groups brings together the remote analysis and monitoring work and that of on-site inspection, thereby enhancing the model of continuous supervision, which consists of maintaining systematic and up-to-date information on each institution and banking group.

The financial statements received periodically (along with other kinds of documentation) are analysed by the Inspection Group concerned. When they deem necessary, those responsible for carrying out the monitoring may, using the BE's legal powers, request further information. Consultations on specific aspects of the applicable regulations are also frequent. They are resolved within the framework of the normal activity of the different areas.

As part of the monitoring activities carried out by the BE, regular reports are prepared and various kinds of administrative procedure conducted. In 2001, monitoring reports were prepared on the situation of the supervised institutions, technical background notes of various

(1) External verification of compliance by the BE with its budget is carried out by the *Tribunal de Cuentas* (audit office). In addition, the annual accounts of every central bank belonging to the European System of Central Banks are audited by an external firm.

The BE also has an Accounts Review Committee, made up of three members of the Governing Council, whose functions include supervising relations with the external auditor and its work, and reporting on the annual accounts of the BE. This committee supervises the operation of the internal audit department.

TABLE II.1

Banco de España staff directly assigned to banking supervision tasks. 31.12.2001

	Directorate General	
	Supervision	Regulation
Total	**336**	**137**
Senior management	31	24
Inspectors and other specialist staff	184	11
IT auditors	33	
Analysts	37	39
Administrative staff	51	63

TABLE II.2

Supervisory activity of the Banco de España in 2001

Recommendation and requirement letters	**112**
Banks	28
Savings banks	16
Credit co-operatives	42
Specialised credit institutions	13
Mutual guarantee companies	7
Appraisal companies	4
Unregistered entities conducting restricted operations	2
Administrative procedures resolved by the Executive Commission	**198**

kinds were drafted to support decisions and the BE conducted the administrative procedures it is responsible for in relation to the supervised institutions. Of such procedures, 198 relating to matters of importance were resolved by the Executive Commission (see Table II.2). These included, inter alia: the setting up of supervised institutions, the acquisition of qualifying holdings, the setting up of subsidiaries and the purchase of holdings in CIs in countries not belonging to the European Union, the opening of branches abroad, the eligibility of capital instruments, the maintenance of internal pension funds, mergers and the use of internal methods to calculate the statistical provision.

In conclusion, receipt and constant analysis of the information available plays a central role in the preparation of the individual supervision plans. These, in short, synthesise the knowledge possessed at the time and enable the general supervision needs of each institution or group to be properly identified.

II.5.5. On-site inspections

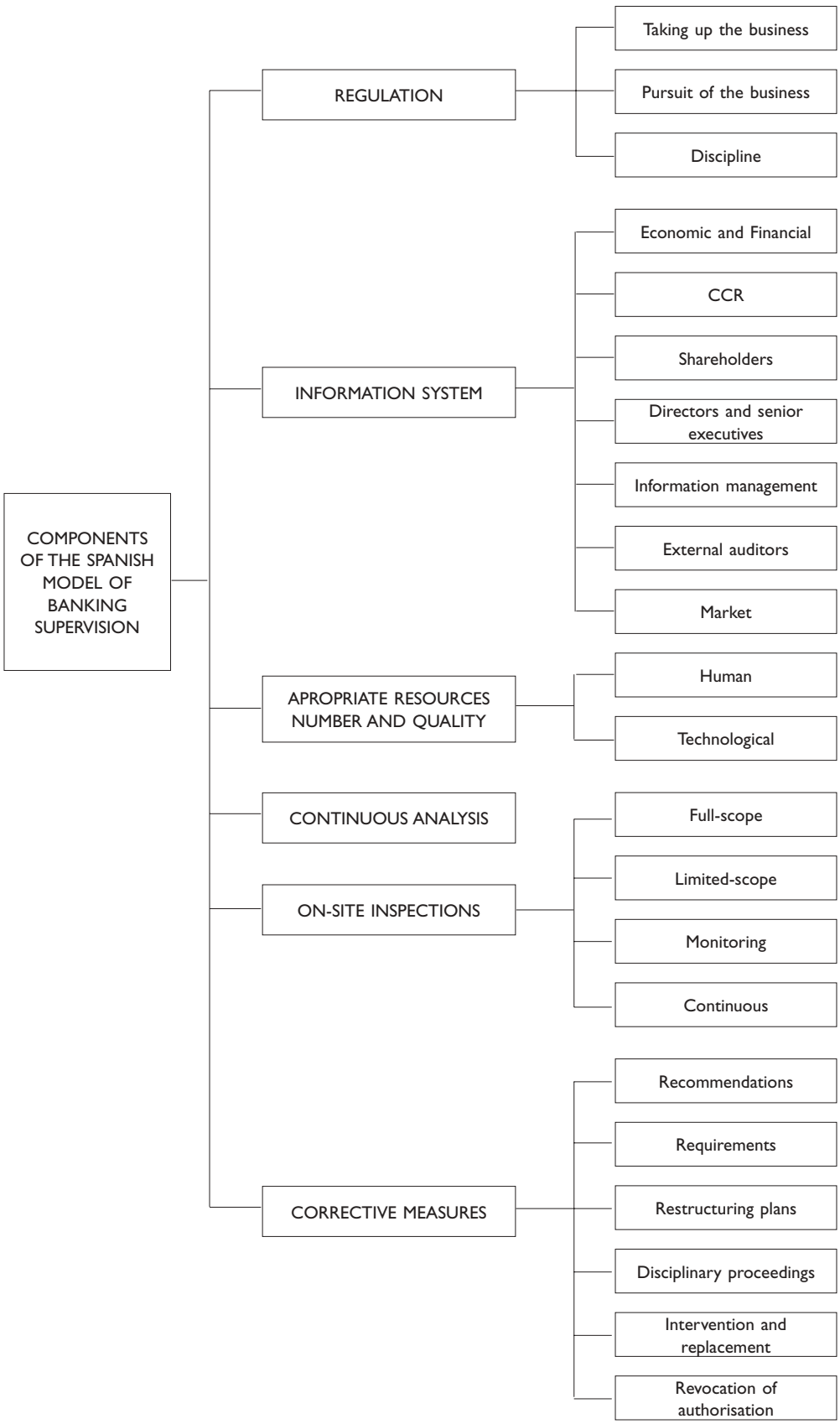
The system of continuous supervision is backed up by a programme of on-site inspections. These enable the BE to verify directly the accounting data and other information supplied, to identify possible weaknesses or poor practices in the valuation of assets and risks, to analyse the degree of legal compliance and, in general, to be familiar with all the quantitative and qualitative aspects (policies, organisation, controls) of the situation of the CI concerned.

Not all countries use on-site inspection as a supervisory tool to the same degree. However, direct inspection of CIs, pursuant to the LDI, is a fundamental component of the Spanish system of banking supervision. Indeed, the conduct of frequent on-site inspections is one of the distinctive features of the Spanish model of supervision, particularly when comparing with countries where the work of external auditors is used to check the information received by the supervisory agency. The important role played by on-site inspection requires considerable human resources, so that inspections can be carried out with sufficient frequency to enable the opinions supplied by continuous monitoring to be confirmed and updated. However, supervisory efficiency must also be considered when determining this frequency, so that a reasonable balance is always maintained between the sufficiency and reliability of the information sources and the need to verify them.

Inspections fall into two categories: full-scope and limited-scope. Full-scope *inspections* are those which seek to obtain up-to-date and reasonably complete information on all the aspects of an institution or group that are relevant from a supervisory point of view. Limited-scope inspections *seek* to obtain sufficient knowledge of one or more areas of the institution or group. The aim of a limited-scope inspection may be to review specific areas (e.g. the loan portfolio, the treasury

BOX II.6

Components of the Spanish model of banking supervision



department or custody activity) or to monitor specific aspects (e.g. the degree of compliance with requirements previously made by the BE, the relevant circumstances for the close of the financial year, etc.).

Finally, in the case of large banking groups, on-site inspections are carried out continuously. Inspectors are present at the institution on a permanent basis, in order to review the different areas and risks constantly and successively.

II.5.6. Corrective measures and exercise of sanctioning powers

As mentioned above, article 43 bis of the LDI provides that the BE is responsible for overseeing and inspecting the CIs and their consolidated groups. The BE is entitled to request any documentation necessary to perform such function and to make inspection visits to their head offices, central offices and branches.

As a consequence of the information obtained on the situation of CIs, whether in the course of its inspection visits or of its continuous analysis, the BE may adopt various corrective measures. In particular:

- *Formulation of recommendations and requirements*. In 2001 the Executive Commission of the BE sent 112 recommendation and requirement letters, as a consequence of the BE's supervisory activities (see Table II.2). The main recommendations related to various aspects of the management of CIs that could be improved, while the requirements highlighted the existence of deficiencies or irregularities that, without amounting to breaches of regulations or disciplinary rules, still required the immediate adoption of remedial measures by the governing and management bodies of the CIs concerned.

- *Approval of restructuring plans*. These plans specify the measures CIs have undertaken to adopt in order to restore compliance with solvency requirements, especially in cases of breach of the obligation to meet minimum capital requirements or of the obligation to observe the limits for exposures with one single entity or group. In 2001 it was not necessary to approve any plan of this kind, although the one that was in force during the year was subject to a number of changes and special monitoring.

- *Opening of disciplinary proceedings and imposition of sanctions*. The administrative bodies given powers by the State to sanction CIs are specified in article 18 of the LDI, which "without prejudice to the provisions of article 42" (relating to the powers of RGs in this area), provides that the BE shall be responsible for conducting proceedings, as well as for imposing sanctions for serious and minor offences. Sanctions for very serious offences shall be imposed by the Ministry of the Economy, on a proposal from the BE, except in the case of revocation of the authorisation to operate as a credit institution, which the government has the power to impose.

  In 2001, 11 sanctioning proceedings were opened, of which 6 were still unresolved at the beginning of 2002. Box II.7 gives details of the disciplinary proceedings resolved in 2001, that had been opened that year or previously, breaking down the offences into very serious, serious and minor. The most frequent grounds for the application of sanctions related to breaches of transparency rules and customer information obligations, of the rules relating to directors and senior executives, significant shortfalls in bad-debt and other provisions, insufficient eligible own funds and, in the case of an appraisal company, failure to satisfy the requirements for authorisation to remain in effect.

BOX II.7

Proceedings resolved in 2001

Nature of the offence	Sanctions applied
Infringement of regulatory and disciplinary rules with the status of law	FIVE offences of this nature were sanctioned. In TWO cases directors or senior executives were found to have defaulted on payments under transactions in contravention of article 9 (8) (d) of Law 13/1989 of 26 May on Credit Co-operatives. In one of these cases the offence was classified as VERY SERIOUS, while in the other it was classified as SERIOUS because the default had been occasional or isolated. The THREE other offences were considered SERIOUS, all involving breach of article 19 (4) of Consumer Credit Law No. 7/1995 of 23 March 1995; the institutions had charged an interest rate of more than 2.5 times the legal interest rate on the current account overdrafts of their consumer customers.
Infringement of rules on the transparency of transactions and customer protection.	FIVE institutions were sanctioned. The cases related to breach of customer information requirements, transparency of the financial conditions of mortgage loans or other rules on commissions and interest rates. Of the five cases, FOUR were SERIOUS and ONE VERY SERIOUS. The latter was because the institution had already been sanctioned for the same type of offence within the previous five years.
Complete or partial failure to send compulsory data and information to the BE	FOUR institutions were sanctioned for errors and omissions in the data they are required to supply to the CCR, the Register of Directors and Senior Executives and the BE's Directorate General Supervision. The offences were found to be SERIOUS AND MINOR.
Fraudulent acts or the use of individuals or legal entities to achieve aims contrary to the regulatory and disciplinary rules	There were TWO SERIOUS OFFENCES of this nature. In one case, a director of an institution was sanctioned for using intermediaries in a transaction so that the institution could not be identified as a party thereto. In the second case transactions were carried out to avoid the application of the Ministerial Order of 5 May 1994 on mortgage loans. Both the institution and its directors and management were sanctioned.
Offences directly concerning institutions' solvency (insufficient own funds, insufficient provisions and failure to reflect the true balance sheet situation)	FIVE sanctions were imposed: ONE VERY SERIOUS one, TWO SERIOUS ones and ONE MINOR one. The very serious offence involved failing to satisfy the minimum capital requirements for more than six months. The serious offences involved an excessive concentration of risk, insufficient loan provisions and an insufficient balance in the early-retirement fund. Finally, the minor offence was a minor breach of the rules contained in CBE 4/91 on the accounting framework for CIs.
Sanctions imposed on supervised institutions other than CIs	FOUR offences of this nature were sanctioned. ONE was considered VERY SERIOUS, involving infringement of the requirements to obtain and retain approval to carry out appraisals in relation to the mortgage market. TWO were considered SERIOUS, the first one involving the issuance of appraisal reports that departed –without expressly stating the fact- from the principles and procedures laid down in the legislation applicable. The second serious offence involved infringement of the rules on conflict of interest in the pursuit of appraisal activity. The only MINOR infringement arose from the lack of an internal register of appraisers, as required by article 12 (1) (l) of Royal Decree 775/1997 on the approval of appraisal services and companies.
Sanctions for infringement of name and activity restrictions	TWO companies were sanctioned for unlawfully using the terms "Investment Bank" and "Bank", pursuant to article 28 of the LDI, which bans individuals and legal entities without the relevant authorisation from carrying out operations restricted to CIs and from using names specific to the latter or others that may lead to confusion with them.

Annex II gives more information on the exercise of disciplinary powers, with a brief description of the legal proceeding in force and statistical details of the proceedings conducted between 1997 and 2001.

- *Administration and replacement of directors*. Administration of an institution and the provisional replacement of its board of directors or management are measures that can only be taken when a credit institution is in a situation of exceptional gravity that jeopardises the effectiveness of its own funds or its stability, liquidity or solvency. No such measures have been taken since 1994.

Finally, it should be pointed out that the Banco de España is not the only institution involved in the various processes that we have referred to as the "basic components of the Spanish model of banking supervision" (see Box II.8).

II.6. BASIC OUTLINE OF THE REGULATION

As mentioned above, the main objective of the wide range of administrative provisions that make up the legal regime governing the activity of CIs is to protect, under the general principle enshrined in Spanish law of free enterprise, the stability of the credit and financial system, which is of such great public interest.

Accordingly, the basic aim of prudential regulation and supervision is to promote an appropriate level of solvency in the CIs and CGs subject thereto, commensurate with the risks assumed in the course of their business, and to verify the existence of such a level. Also, the strength of the CIs is a prerequisite for the public to have the necessary confidence to deposit their funds with them, trusting that they will be repaid on the conditions agreed.

Spanish banking regulations apply international principles and, in particular, those of Community law with a number of slight differences that make them more demanding in certain areas (see Box II.9). The regulatory framework is rather dispersed and complex, so that a complete description far exceeds the limits of this section, the content of which is supplemented in Annex I.

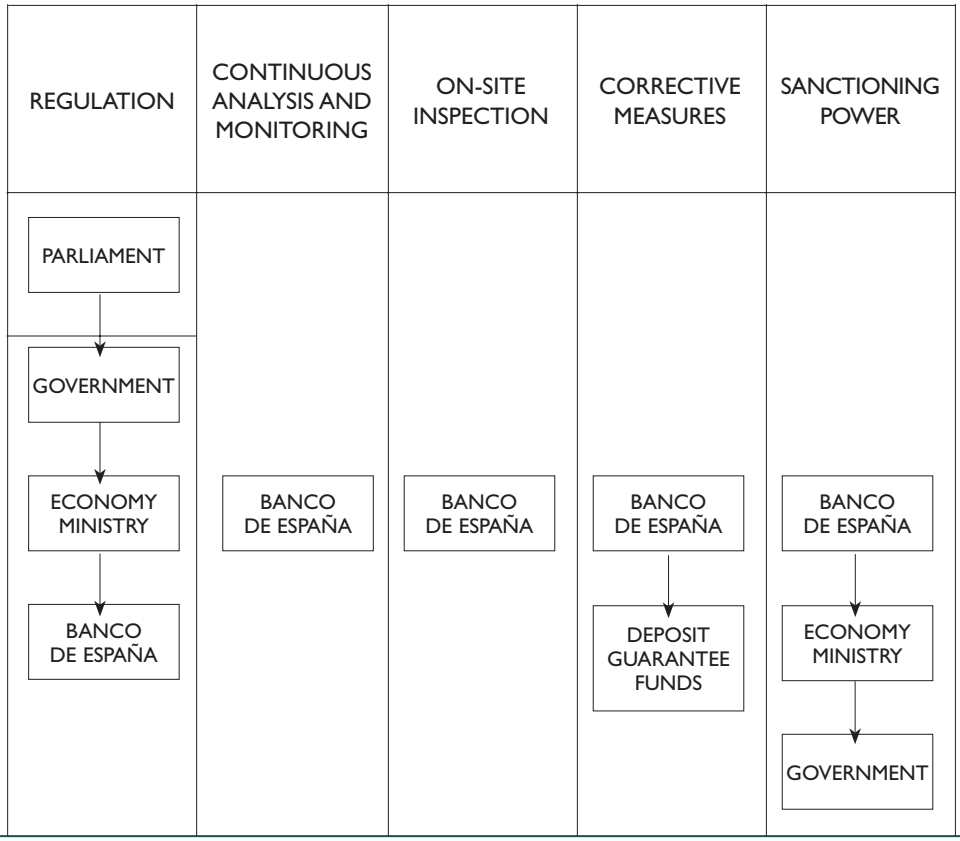
The specific banking provisions applicable to CIs can be divided into three areas:

The first one consists of the set of rules that regulate *access to the business of banking*. This includes both the conditions for setting up new CIs and for mergers as well as the controls established for the acquisition of stakes in CIs that already exist. These rules, which are based on a common harmonised threshold at the European level, provide for the existence of a prior authorisation to operate as a credit institution. This can only be granted if certain minimum conditions are met, including a minimum share capital, an adequate organisation, suitable shareholders with qualifying holdings and a reputable and professional top management.

The provisions regulating the cross-border activity of CIs, including that of both Spanish CIs abroad and foreign CIs in Spain, should also be highlighted. The particular provisions applicable to those based in the Community are notable, their most striking aspect being the general principle of single licences, also known as Community passports, under which no Member State can stop a CI authorised in another Member State from operating freely within its territory. CIs can operate in Member States other than their home one either by opening a permanent establishment (branch) there, or else under the freedom to provide services, with their business generally being subject to the rules and supervision of the home country authorities.

BOX II.8

Participation of the Banco de España and other institutions in the components of the Spanish system of banking supervision



NOTE: The participation of the regional (autonomous) governments in the supervisory process depends on their legal powers.

The second area is made up of the provisions that establish the *specific conditions for carrying on banking activity*. As mentioned above, the most significant ones relate to solvency and their general outline usually reflects the provisions of Community law, although in many cases stricter provisions have been enacted. These provisions establish a solvency coefficient, the purpose of which is to ensure that CIs always have own funds commensurate with the different types of risk assumed in the course of their activity.

This regulation has a number of different aspects. First, it defines eligible own funds, which are classified into tiers, depending on the degree to which they perform the typical functions of capital (its capacity to absorb losses and its indefinite availability to the institution). Second, it defines and quantifies the risks to be covered and establishes the amount of the related minimum level of own funds. Finally, certain limits are put on risks and the consequences of failure to comply with the solvency coefficient are specified. These basically consist of the applicable sanctioning regime, certain restrictions on the distribution of profits and the drafting of plans to restore compliance with the coefficient.

Another set of rules governing banking activity relates to accounting. These rules establish the criteria that must be applied in CIs' financial statements to value the different accounting items and for income recognition so that such statements reflect the true situation. This relatively harmonised field is based on generally accepted accounting principles, although the principle of prudent valuation prevails over all others and is applied more strictly than in other sectors. These rules require much more detailed, extensive and frequent information to

BOX II.9

Spanish law and its relationship with European Union law

EU law on the prudential supervision of CIs generally lays down minimum requirements, so that each EU Member State can impose its own stricter conditions, provided that the principle of no discrimination on the basis of nationality is respected when such conditions are applied to institutions or persons having their home countries within the EU.

Based on a banking policy in which prudence must frequently prevail over simplistic fair competition conditions, Spanish law, like the law of other EU countries, imposes stricter requirements than Community law in the following areas:

As regards the setting up of CIs, Spanish law tightens the Community requirements in certain areas: a larger number of persons must effectively direct the business (board of directors with 3 or 5 members, compared with a minimum of 2 directors provided for in the Directive), the minimum capital is much higher (€ 18 m, as against € 5 m), the threshold for checks on shareholders, both when the institution is set up and when shareholdings are subsequently changed, is lower (5% compared to 10%), and certain tests are introduced to assess the suitability of shareholders that are not directly envisaged in the Directive (sufficient financial resources and implications of their non-financial activity).

Another special feature of Spanish law is the establishment of periods during which the activity of newly created CIs is subject to restrictions. The distribution of dividends is restricted during the first three years and, during the first five years, credit transactions with members, directors and senior executives (or their related companies) are prohibited and a non-financial company or group may not directly or indirectly hold more than 20% of the capital of the institution or exert control over the same.

As regards solvency regulations, and beginning with their scope of application, Spanish law imposes individual own funds requirements on Spanish bank subsidiaries included in consolidated groups or subgroups, although they may be lower than the general requirements, depending on the percentage of capital held by the parent company, and it contemplates certain cases of horizontal consolidation not provided for in Community law (groups with non-consolidated parent companies). It also makes certain requirements for minimum own funds (based on a system of net aggregation) in non-consolidated mixed groups, i.e. those that include insurance companies.

Eligible own funds are defined more strictly than under Community law (e.g. profits generated during the year are only eligible at the end of the year and the negative differences from first consolidation are not eligible), and there are a larger number of deductions (inter alia, financing to third parties that might be used for the acquisition of eligible elements). Also, a qualified holding in a non-financial institution is deemed to exist at a lower level than under Community law (10%, as against 15%).

In relation to the weightings applicable to the different types of risk, the Spanish rules are stricter than the European ones in certain cases, including the treatment of accruals and certain doubtful assets subject to country risk.

Spanish law also has two limits to risk that do not exist under Community law: the limit on tangible fixed assets, whereby the latter may not exceed 70% of own funds, and the individual limit on positions in each currency, which is set at 5%. Authorisation of the BE so required to exceed the latter limit.

A further special feature of Spanish law is that the exposures of banks and savings banks to directors and senior executives generally require prior authorisation of the BE.

In relation to accounting, valuation criteria and the provision of information to the supervisor, Spanish rules are more detailed than the Community ones. They establish a comprehensive treatment of credit risk and its coverage (by means of specific, general and statistical provisions) and require a wide range of confidential statements (not specifically included in the harmonised regulations) to be sent regularly to the supervisor.

As regards the rules on the transparency of transactions and customer protection, they are generally much more demanding and detailed than in Community law, as the level of regulatory harmonisation in this area is relatively low.

be provided to the supervisor than to the general public, to enable it to better exercise its powers over CIs.

This second area also contains another set of specific rules for which the BE is responsible. Noteworthy among them are rules of public law on the transparency of transactions and protection of customers. These seek to ensure that bank customers have sufficient and appropriate information on the transactions and services they demand so that they can form well founded opinions thereon.

Other specific rules which CIs must comply with include the regime for opening branches in Spain (generally there are no restrictions, except when the rules on solvency are infringed); the law on "incompatibilities" in relation to directors and senior executives, which limits the number of posts they can hold at the same time; and the rules regulating the Central Credit Register (CCR).

The third and final area contains *provisions seeking to correct the breach of specific banking rules and to address situations of particular gravity.* Notable here are, first, the sanctioning regime applicable to CIs. This regime, respecting the principle of the rule of law that underpins the Spanish legal system, provides for the sanctioning of conduct defined as infringements, which vary in their degree of seriousness. The institutions themselves, their directors and senior executives and even the holders of qualifying shareholdings are subject to this regime.

Second, for preventive, not sanctioning, purposes, there are provisions that envisage the possibility of certain measures (administration of the institution or replacement of its directors) being taken by the BE, whereby, in situations of exceptional gravity, an institution's management structure may be directly affected.

The regulation of deposit guarantee funds, to which all CIs must belong, is also worth highlighting. Besides insuring deposits and the securities and instruments intermediated by credit institutions, their functions include participating in the management of bank crises, both when insolvency proceedings take place and when banks are restructured without such proceedings.

Finally, this area includes the grounds and procedure for revoking the authorisation to operate as a credit institution, whether as a consequence of a sanctioning proceeding, breach of the requirements to obtain and maintain authorisation, insufficient own funds, or the existence of doubt as to whether the bank will fulfil its obligations to its creditors.

II.7. CONTINUOUS SUPERVISION OF CREDIT INSTITUTIONS AND THEIR GROUPS: CHARACTERISTICS OF THE SPANISH MODEL

II.7.1. The process of continuous supervision. Preventive supervision

As already indicated, the supervision model applied in Spain involves the continuous analysis of CIs and their groups, carried out through the monitoring of the economic and financial information received periodically or further to a specific request and through frequent contact with their representatives. The organisational structure of supervision has been designed to ensure that these tasks are performed effectively. This continuous process is reinforced and supplemented by an extensive programme of on-site inspections, which enables the information received to be directly verified and facilitates the formation of a well-founded opinion on all aspects relevant to the risk profile, solvency and prospects of the CIs and their CGs. The

intensity of the supervisory activities depends on the size, complexity and, in particular, the risk profile of the CIs and the GCs and their influence in the system.

Individualised oversight of CIs is based, therefore, on three fundamental elements: receipt of information, analysis and verification.

When the periodic information, and any extraordinary information requested from the CIs, has been received and treated, it is prepared for continuous analysis by the various Inspection Groups. The financial statements received cover all the relevant aspects of the institution and its group including, in particular, economic and financial information and data, on solvency, on the risks incurred with different customers and on shareholders. During the supervision work the periodic reports are supplemented with all the additional information and documentation requested from the CIs. Internal management information is increasingly of interest, owing to its usefulness.

From the constant analysis of such information and from the frequent contacts with CIs' representatives, extensive knowledge is obtained of their solvency, asset quality and profitability, which is checked during on-site inspections. This static approach to CIs' data is supplemented by a study of their capacity to manage banking risks appropriately. The BE is thus developing its own supervision methodology, focused on risk, which will enable it to incorporate the time factor dynamically and to strengthen preventive measures. This methodology, called SABER (the Spanish acronym for a risk-based approach to banking supervision), does not seek to replace the previous, basically static, approaches but to supplement them and incorporate them in a dynamic and preventive framework so as to obtain a deeper and more systematic understanding of the current and future performance of CIs and CGs.

From a practical point of view, this new methodology is applied in the following stages:

- *Quantification of the risks of the institution and its group*. Eight basic risks have been defined for this purpose: credit, market, interest rate, foreign-exchange, liquidity, business, operational and legal (see Box II.11). The supervisor is required to give an opinion on each, classifying it as *very high, high, medium, low or very low*.

- *Qualitative analysis of the control systems* of the institution and its group, to measure the capacity to control and mitigate the aforementioned risks. In particular, the following factors are assessed: the existence of management policies, the quality of the organisational structure, the existence of risk control systems, the sufficiency of IT systems, the integrity and quality of information systems and the adequacy of the internal audit.

- *Assessment of the residual risk*, understood as the possibility that the institution or its group incur losses after having taken into account both the quantitative and qualitative factors. The overall assessment of the level of residual risk of all the areas of business has been called the *institution's risk profile*.

- *Analysis of solvency in the broad sense*, i.e., not only of the sufficiency of own funds but also, among other aspects, their composition and quality, the existence of unrealised capital gains, as well as the capacity of the profit and loss account to generate recurrent profits with which to strengthen own funds through the accumulation of retained earnings.

BOX II.10

Regulatory changes in 2001

Among the new regulations enacted last year in the field of prudential supervision of CIs and other financial institutions for which the BE is responsible the following were notable:

— The final legislative steps have been taken to make *investor compensation schemes* fully effective in Spain. The purpose of these schemes is to provide a minimum guarantee for those persons who have entrusted securities or other financial instruments to an investment services firm or a credit institution for deposit or registration, or for the performance of some investment service. Royal Decree 948/2001 of 3 August 2001 (1) provides that, with effect from 1 June 1993, the temporary risk of unavailability of such securities or instruments, as a result of the insolvency or suspension of payments of the intermediary in question, or of failure to return the securities under certain conditions, shall be covered up to a maximum amount of € 20,000 per investor.

In the case of investment services firms "Investment Guarantee Funds" are to be set up to perform this task, while in the case of CIs it shall be performed by the existing Deposit Guarantee Funds ("DGFs"), along with their traditional task of insuring deposits made by the general public. Accordingly, the relevant changes have been made to the law governing DGFs.

This legal framework has been completed in relation to CIs by CBE 4/2001 of 24 September 2001 (2). This laid down the valuation criteria that should be applied to the various types of securities and instruments on the basis of which the annual contributions of CIs to the DGFs are calculated, as well as the information that the former shall send annually to the BE for the purposes of such calculation, highlighting the need for the CIs to exercise utmost care in the control of accounts representing custody activity.

— In relation to the *solvency of CIs*, Royal Decree 1419/2001 of 17 December 2001 (3) has made three changes: the scope of the rules applicable to government debt in relation to the capital ratio has been widened to cover debt securities issued by local authorities; the definition of the securities trading book has been widened to include positions in gold (which are given a similar treatment to positions in foreign currencies); and finally, and most importantly, CIs with BE authorisation are allowed to use internal risk management models to calculate their capital requirements to cover market and foreign-exchange risks.

— As regards the *transparency of transactions and the protection of bank customers*, CBE 8/1988 of 7 September 1988 has been updated by CBE 3/2001 of 24 September 2001 (4) to incorporate two changes.

First, CBE 3/2001 has incorporated in CBE 8/1988 the rules of Community law established by Law 9/1999 of 2 April 1999, which regulate the legal system for cross-border transfers between Member States, implementing that part which corresponds to the BE, as well as the Ministerial Order (MO) of 16 November implementing such law and other provisions relating to transfers in general. As regards the transfers included within the scope of application of this Law (generally euro transfers made between Member States that do not exceed € 50,000), the aforementioned rules, as a whole, lay down the following: the maximum terms for carrying out transactions and making the funds available to the beneficiary, together with the consequences of failure to comply with them; the obligation to carry out the transaction, in its whole amount, unless otherwise specified; the obligations for transparency vis-à-vis customers which refer to the requirements to publish the general conditions applicable to such trans-

(1) Official State Gazette (BOE) of 4 August 2001.
(2) BOE of 9 October 2001.
(3) BOE of 5 January 2002.
(4) BOE of 9 October 2001.

BOX II.10

Regulatory changes in 2001 (continued)

actions, to deliver to the customer a written offer binding on the institution and a receipt detailing the transaction performed. As regards other cross-border transfers, institutions shall also publish the general conditions applicable to them –albeit with a more restricted scope- and shall deliver a receipt detailing the transaction.

Second, various provisions have been introduced on the conduct of transactions through channels that do not require the customer's physical presence at the institution, in particular via Internet. Inter alia, they require institutions offering the use of Internet to include certain information in their own website, as well as to give customers the option of delivery of the contract in a durable electronic format. They also enable information to be sent by electronic means after execution of the contract, provided that the customer accepts or requests use of this new form of communication.

— In 2001 the *legal system for currency exchange bureaux* was completed with the publication of CBE 6/2001 of 29 October 2001 (5) pursuant to the authorisations contained in RD 2660/1998 of 14 December 1998 and in the subsequent MO of 16 November 2001. This circular specifies the procedure for obtaining authorisation, the information that shall be submitted to the BE and the rules on transparency of transactions and customer protection (in particular as regards the management of cross-border transfers), as well as developing the figure of agent, all this with the special features deriving from the scope of the activity that currency exchange bureaux can perform.

— Among the *provisions approved at the EU level* the following are notable:

Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the *reorganisation and winding up of CIs* (6), which must be transposed into Spanish law by 5 May 2004. According to this directive, these procedures shall be carried out, in relation to EU CIs, in accordance with the principles of unity and universality, which means that the authorities of the home Member State shall have sole power to adopt reorganisation measures and to commence winding-up proceedings with respect to a credit institution and all its branches in other Member States, where their decisions shall be recognised. In turn, such procedures shall, with certain exceptions, be conducted in accordance with the law of the home Member State.

Regulation (EC) 2560/2001 of the European Parliament and of the Council of 19 December 2001 (7) on *cross-border payments in euro*, which is directly applicable in Spain. This regulation provides that CIs' charges for electronic payments and transfers in euro whose amount does not exceed certain limits shall be equal, whether or not the cross-border transaction is between EU Member States or within one of them. These provisions shall come into force from 1 July 2002, with respect to electronic payments, and a year later in the case of transfers.

Finally, the European Commission, on 24 April 2001 (8), presented a proposal for a Directive of the European Parliament and of the Council on the supplementary supervision of CIs, insurance undertakings and investment firms in a financial conglomerate, the aim of which is to establish, for the first time, a harmonised prudential supervision framework for financial groups including insurance undertakings. During the Spanish presidency of the EU, the Council of Economics and Finance Ministers reached a political agreement on this Directive on 7 May 2002.

(5) BOE of 15 November 2001.
(6) O J L 125, of 5 May 2001.
(7) O J L 344, of 28 December 2001.
(8) O J L 213, of 31 July 2001.

BOX II.11

Definitions of risks included in the "SABER" methodology

TYPE OF RISK	CONCEPT
CREDIT RISK	Possibility of suffering losses arising from the failure of counterparties to perform their contractual obligations to the institution.
MARKET RISK	Possibility of suffering losses due to adverse movements in the market prices of negotiable financial instruments held by the institution.
INTEREST-RATE RISK	Possibility of suffering losses due to the negative impact of interest rate changes on the institution's financial margins.
FOREIGN-EXCHANGE RISK	Possibility of suffering losses due to adverse fluctuations in the exchange rates of currencies in which the assets, liabilities or off-balance-sheet transactions of the institution are denominated.
LIQUIDITY RISK	Possibility of suffering losses due to not having, or not having access to, sufficient liquid funds to meet its payment obligations.
BUSINESS RISK	Possibility of suffering losses due to loss of the current position of the institution in the markets in which it operates.
OPERATIONAL RISK	Possibility of suffering losses as a consequence of inadequate processes, systems, technical equipment and staff, or of failures in the aforesaid, as well as of external events.
LEGAL RISK	Possibility of suffering losses arising from uncertainty over or infringements of the law.

- *Determination of the supervisory risk*, which is derived by comparing the level of solvency of the institution with its risk profile. Other relevant factors not explicitly considered in the previous stages also have to be taken into account in this determination, especially certain aspects of corporate governance.

  This latter concept is the basis for designing the specific supervisory processes to apply to the institution and its group: the allocation of resources, the planning of visits, the preparation of meetings with senior management and, in short, the drawing up of a tailored supervision plan for each institution and group.

In this way, by emphasising the analysis of the risk factors of an institution and of the control mechanisms put into practice, the focus of attention of the supervisor shifts from verification of balances, asset quality and compliance with ratios (tasks that certainly must still be carried out), to prevention, by means of dynamic approaches and the performance of prudential supervision activities more closely adapted to the specific situation of each institution and group.

II.7.2. The institutional underpinnings

The efficacy of any system of supervision of CIs also depends on the smooth functioning of the rest of the institutional environment, i.e. on conditions being conducive to effective banking supervision. The list of such institutional underpinnings is long, but the importance of two of them should be highlighted.

The first is good governance of CIs. Good governance is of great relevance to all companies, but is especially important for CIs. The definition and application of rules of good governance should lead to the creation of a corporate culture of prudent risk management, to the design of structures and procedures that facilitate the dedication and participation of the directors, to the introduction of effective and independent internal control systems and, in short, to the adoption by the directors and senior management of certain principles of management transparency, fairness and efficiency, and to the assumption of their responsibilities. These rules make a decisive contribution to the creation of solid and efficient financial systems.

Accordingly, in addition to the role that regulators and supervisors may have in this area, it is the CIs themselves that have to define and put into practice all such measures as may contribute to achievement of the highest ethical standards and levels of quality in corporate governance, promoting transparency in management and in the information supplied to the markets, and the protection of shareholders. The institutions are also responsible for the adequate composition, size and functioning of boards of directors, for the creation of specialised committees thereon, for the involvement of the directors in decision-making, for the preparation of and effective compliance with codes of conduct that enable situations of conflict of interest to be properly addressed and the irregular use of inside information to be avoided and for effective communication between the board and shareholders, markets, auditors and supervisory authorities.

Notable among the specialised committees that contribute to the better governance of CIs, on account of its importance, is the "Audit Committee", which must be made up mainly of non-executive directors. Among its standard functions may be mentioned approving the appointment and dismissal of the external auditor and of the officers in charge of the internal audit department; analysis of internal audit reports, as well as approval of their scope and frequency; promoting the introduction of effective internal control systems; checking that the necessary measures are taken to remedy any shortcomings detected; monitoring the recommendations or requirements made by supervisors or other authorities and sending the board all relevant information provided by internal and external auditors and supervisors.

The second institutional underpinning is market discipline. For this to be able to perform its function efficiently the CIs must at all times supply complete, precise, true, up-to-date and easily comprehensible information. The preparation of the annual accounts and other information is the responsibility of the directors and has to be verified by independent auditors, so that analysts can, in turn, perform their function.

The importance of the market discipline function has been expressly recognised by the Basel Committee on Banking Supervision, since one of the three pillars of the new Capital accord, currently under preparation, is entirely devoted to it.

II.7.3. Supervision on a consolidated basis of international Spanish banking groups

As well as supervising Spanish CIs on an individual basis, the BE supervises Spanish CGs on a consolidated basis. The definition of the scope of consolidation used in Spain is sufficiently broad and enables aggregate solvency to be adequately overseen. There are also additional solvency requirements for non-consolidated mixed groups, i.e. groups containing CIs and insurance companies, that do not consolidate their balance sheets.

In this respect the supervision of Spanish banking groups that have recently expanded significantly, especially in Latin America, has become particularly important. The internationalisation of banks involves a change in the profile of their risks and a need for measures to prevent

a potential crisis in any of the institutions of an international CG having undesired effects on its parent bank and group and, by extension, on the stability of the Spanish banking system.

Accordingly, the BE has defined a framework of good practice for the organisation and management of these banking groups. This framework is based, inter alia, on the following principles that guide supervision on a consolidated basis by the BE, which have been notified to the Spanish parent CIs:

- *Group culture and management information*. The board of directors of the parent institution must establish criteria for organisation, management, internal information system and controls, appropriate to its status as an international group. In this respect, Spanish parent CIs must effectively assume the responsibility of overseeing the management of their subsidiaries. To do this they need comprehensive information and systems based on integrated computer platforms enabling them to monitor their subsidiaries, harmonise their accounts in the consolidation process, analyse their business and control their risks, both at the individual and aggregate levels.

  For these purposes, comprehensive internal audits of each of the institutions of the group shall be carried out by the parent bank, at least once a year, to ensure that the data are reliable and that the internal rules and procedures are being complied with. This shall be in addition to the internal audit performed by each component of the group itself. At the same time, every effort shall be made to ensure that the external auditors are independent and of suitable quality. The important role played by the external auditor of the parent institution and the consolidated group in the process of consolidation shall also be monitored.

  Irrespective of co-operation with local supervisors, supervision on a consolidated basis by the BE shall be carried out primarily from the group's parent institution, paying special attention to knowing and checking the reliability of the information systems established by the parent institution and its control over them, as well as the quality of the subsidiary's assets. Accordingly, the parent institution shall make available to the BE all the necessary information for the latter to be able to carry out its supervision tasks and to reach an opinion on the situation of the group.

- *Prudent accounting policies*. Companies set up in other countries subject to their own legal and accounting rules must harmonise their balance sheets before they can be consolidated with Spanish banking groups. This involves adapting the financial statements of the foreign subsidiaries to Spanish standards by means of the relevant adjustments that shall be properly documented and based on prudent criteria. The prior harmonisation of accounts shall not entail any provisions for bad debts in the individual statements of subsidiary companies being recorded as revenues in the consolidated statements (CBE 4/91, provision 20.ª 7) or, therefore, being offset in the consolidation process.

  Moreover, Spanish banking groups with business abroad shall follow a policy of maximum prudence, speeding up the amortisation of goodwill and making provisions to mitigate any losses arising from unforeseen future events.

- *Group solvency and solvency on an individual basis*. The amount, quality and structure of the group's own funds should be strengthened. As regards its distribution, each bank of a consolidated group shall have in each country sufficient own funds to cover its risks, with sufficient margin for its business to grow and comply with local rules. That

is to say, even if the necessary measurement of the solvency of the groups is carried out on a consolidated basis, appropriate risk management requires that the distribution of own funds among their various components should reflect the distribution of the risk.

- *Group chart.* The chart representing the structure of the group (complete set of holdings in share capital and of voting rights between the various group companies) shall be clear and public.

- *Financial autonomy*. Each credit institution subsidiary of a Spanish banking group must be financially independent of the parent institution and of the other institutions in the group and, therefore, shall manage its own financing and liquidity autonomously. This facilitates the proper valuation of each counterparty and contributes to the financial strength of the group. In other words, each institution shall obtain its financing on the market and shall pay the risk premium corresponding to its individual situation. Likewise, any hedging they decide to provide for their risks shall be obtained on the market without the parent or any other institution in the group being the counterparty.

  Intra-group operations, unless they have a commercial basis (e.g. documentary credit), shall be limited to exceptional situations, and the prices applied shall be market prices.

  Accordingly, it shall be made clear that the strength of the consolidated balance sheet of the group is a result of aggregating the individual strength of each of its components and market knowledge of such circumstance shall be facilitated.

- *Control of liquidity.* Crisis situations highlight the importance of liquidity in bank management and test the mechanisms designed for its control. Consequently, the group shall design adequate contingency plans for its consolidated position in the currencies in which it operates, especially in euro and dollars. At the same time, each banking subsidiary shall have a system that continuously measures its own liquidity, both in local currency and in dollars, with appropriate mechanisms to neet ordinary needs for liquid funds, and with contingency plans for extraordinary circumstances.

III

SUPERVISORY POWERS OF THE BANCO DE ESPAÑA IN AREAS OTHER THAN BANK SOLVENCY

In addition to the powers and conduct of the Banco de España (BE) described in the foregoing chapters relating mainly to the prudential supervision of credit institutions (CIs), the BE is entrusted with the surveillance of other aspects of banking activity. These relate most notably to the rules governing the transparency of banking operations and elements established to protect the legitimate interests of bank customers in their relations with CIs.

Along with these functions and with other auxiliary tasks pertaining to the BE's overall powers as the supervisor of CIs, it is worth commenting on the monitoring and inspection functions the BE performs in relation to other parties and markets whose activity is closely related to the role of CIs in our financial system.

All these powers are generally accompanied, as is stipulated in the rules conferring them, by the regulatory authority required to issue general provisions on the implementation and application thereof, the so-called Circulars of the Banco de España (CBE).

Hereafter, these functions are reviewed, with a discussion of how they have evolved in recent years.

III.1. TRANSPARENCY OF OPERATIONS AND PROTECTION OF CUSTOMERS

This area of the regulation of CIs' activity has several aims, all linked to the stability and efficiency of the credit system:

To increase competition between operators, which is beneficial both to market efficiency and to the efficiency of banks providing services in it. To ensure such competition it does not suffice to establish, as Spanish regulations do, a general principle of freedom for the prices and conditions of the financial operations transacted by CIs. Conversely, together with this principle, the obligation is stipulated in many areas to publicise the basic financial conditions (prices in particular) of these operations. As a result, potential customers may, through prior knowledge and comparison of these conditions, select the offer which, in addition to that being most suited to their requirements, is that which offers the best terms.

To contribute to balancing the contractual position of banks and their customers. Evidently, the aforementioned publicity is also conducive to such balance, by ensuring appropriate information beforehand on the characteristics of the financial product to be bought. But the Spanish regulator, in certain specific aspects of bank operations, has deemed these arrangements insufficient and has added to them with express obligations or constraints in the determination of some

of the attendant conditions in order to avoid, particularly in the case of widely used consumer products, abuse arising from the different contractual positions of the respective parties.

To promote the management of banking institutions based on the observance of good commercial practices, so that the confidence that should preside bank business is not dented and what are known today as legal or reputational risks are reduced.

The BE is also entrusted with supervising compliance with the specific provisions of this area of regulation. These provisions are basically included in CBE 8/1990 of 7 September 1990 (1), which may be viewed as a summary of the regulations in force.

Notably, this set of measures entails the setting of rules of public law compulsory upon CIs, with failure to comply being subject to an administrative penalty. However, the measures do not prejudge or encroach on most legal relationships, of a purely mercantile and private nature, between the bank and its customers (see Annex I for greater details). The BE also has a Complaints Service, with which individuals may lodge complaints about their relationship with banking institutions (see Annex I).

The following headings detail some of the standardised verification or monitoring procedures attributed to the BE in this area. This is without forgetting that a further, most substantial part of these supervisory tasks is conducted during ordinary examinations of banks, where particular attention is paid to compliance with these activity-regulating aspects.

III.1.1. Commission charges

Freedom – practically without exceptions – in setting the prices of bank services also entails the obligation of drawing up a brochure of charges, valuation conditions and chargeable expenses detailing the maximum amounts applicable, the item to which they relate and the terms of their application to the operations and services in which banks habitually engage. This brochure should be available at all times to customers and, at present, access to it may also be had through the BE website. The inclusion of charges in the brochure is, in the case of habitual services, a condition for their applicability to the product or operation concerned.

The BE is responsible for verifying and registering the brochure that includes these charges and changes thereto. Such verification does not, however, include securities operations, as these are the preserve of the CNMV (National Securities Market Commission), unless they refer to securities traded on the Public Debt Book-Entry Market.

Verification is restricted, by legal imperative, to monitoring the transparency of the brochure, i.e. to checking that it reflects maximum prices and the conditions governing their application in an orderly, clear and comprehensible fashion. The BE has also been rejecting those charges which either do not relate to the actual provision of a service requested by the customer, or which, owing to the manifest distance between the amount involved and that habitually applied in the industry, may not be generally applicable and, therefore, not reflect the commercial practice applied by the bank, distorting the basis for the publication of the charges.

In recent years, the changes made by banks to charge brochures have arisen both from their adaptation to new transparency requirements, introduced via the frequent BE circulars updating the content of the above-mentioned CBE 8/1990, and from the charges applied to new services or from amended amounts.

(1) Issued in execution of the Order of 12 December 1989, the legal basis of which is to be found in article 48.3 of Law 26/1988 of 29 July 1988 on the discipline and intervention of CIs (LDI).

TABLE III.1

Commission charges (number)

	Total				Banks				Savings banks			
	1998	1999	2000	2001	1998	1999	2000	2001	1998	1999	2000	2001
Cases examined	1,043	1,314	1,068	855	538	541	522	396	234	333	227	234
Settlements (a)	749	891	779	659	390	359	373	281	176	223	181	193
Acceptances	*384*	*511*	*420*	*307*	*206*	*204*	*194*	*122*	*81*	*131*	*100*	*79*
With objections	*365*	*380*	*359*	*352*	*184*	*155*	*179*	*159*	*95*	*92*	*81*	*114*
Objections formulated	1,674	2,126	2,184	1,857	822	740	1,282	823	493	557	306	692
	Credit co-operatives				Specialised credit institutions				Securities firms			
Cases examined	209	299	247	149	58	136	55	57	4	5	17	19
Settlements (a):	130	203	167	121	49	103	46	48	4	3	12	16
Acceptances	*73*	*112*	*93*	*71*	*23*	*64*	*27*	*26*	*1*	—	*6*	*9*
With objections	*57*	*91*	*74*	*50*	*26*	*39*	*19*	*22*	*3*	*3*	*6*	*7*
Objections formulated	272	671	527	247	82	155	61	78	5	3	8	17

(a) A single settlement may correspond to several cases.

The number of cases processed stands at around one thousand per annum (see Table III.1). Approximately half of the increase in 1999 was due to the transmission of new brochures whose only change consisted of the inclusion in charges of the amounts of the various commissions in euro. Conversely, the figures for 2001 show a containment that is closely related to an express recommendation of the BE: namely, that fresh rises in charges be unconnected to the euro introduction period and to the postponement to 2002 of the adaptation of brochures to amended CBE 8/1990, approved in September 2001, with the aim of avoiding their coinciding with the transmission – in November and December – of the brochures exclusively in euro for their placement on the BE website. Such transmission does not feature among the cases processed during the year, as no express settlement was required.

Over the period as a whole, the weight of brochures submitted by banks diminished, falling to below 50 %, as did, to a lesser extent, that at co-operatives, whereas the related weight at savings banks increased, accounting for 27 % in 2001.

III.1.2. Advertising

The function assigned to the BE in this area is the authorisation, prior to diffusion, of CIs' advertising projects referring to costs or returns for the general public.

Said authorisation, which is unique among our peer countries (where self-regulation usually plays a greater role), is intended to ensure that advertising reflects clearly, accurately and in a manner respectful of competition the essential features of financial offers, and that the calculation of the cost or return offered has been made in keeping with the rules regulating the equivalent annual rate (EAR) formula. This measure seeks to harmonise calculations to ensure the comparability of the different offers.

The number of cases processed until 1997 held very stable, at around one thousand. In the four years since the number has increased forcefully, rising to 2,784 in 2001, broken down as indicated in Table III.2. This is due, in part, to the rate cuts applied in the second half of the 1990s which, from 1997 in particular, saw institutions adopt a much more aggressive strategy in their lending offers (first in mortgages and subsequently in consumer loans).

TABLE III.2

Advertising projects (number)

	Total				Banks				Savings banks				Credit co-operatives				Specialised credit institutions			
	1998	1999	2000	2001	1998	1999	2000	2001	1998	1999	2000	2001	1998	1999	2000	2001	1998	1999	2000	2001
Cases processed	**1,365**	**1,676**	**2,032**	**2,784**	**781**	**965**	**1,197**	**1,555**	**238**	**336**	**367**	**566**	**135**	**109**	**170**	**220**	**211**	**266**	**298**	**443**
BY MANNER SETTLED:																				
Authorised	1,018	1,311	1,540	2,225	555	744	866	1,220	197	269	287	474	117	85	130	188	149	213	257	343
Rejected	50	38	27	26	35	14	21	20	8	16	5	4	ó	1	ó	ó	7	7	1	2
Modified (a)	167	154	248	354	146	102	180	206	5	19	33	63	4	5	7	14	12	28	28	71
Returned (b)	130	173	217	179	45	105	130	109	28	32	42	25	14	18	33	18	31	18	12	27
BY TYPE OF TRANSACTION (c):																				
Lending transactions	936	957	930	1,107	507	468	464	468	148	205	132	219	86	46	68	78	195	238	266	343
Deposit transactions	206	460	685	970	100	315	454	639	70	93	156	246	36	52	75	85	ó	ó	ó	ó
Other	56	105	169	148	28	80	99	113	15	19	46	9	9	6	20	25	4	ó	4	ó
BY ADERTISING MEDIUM (c):																				
Press	316	419	548	870	171	231	328	545	32	40	43	58	12	13	17	23	101	135	160	244
Radio	27	59	26	60	9	37	13	35	3	8	2	ó	5	ó	ó	1	10	14	11	24
Television	56	63	101	94	20	26	79	56	8	5	4	4	2	2	4	3	26	30	14	31
Other	799	981	1,109	1201	435	569	597	584	190	264	285	412	112	89	142	161	62	59	85	44

(a) Modifications, normally in prices, in projects authorised in the same or in previous years.
(b) Relate to projects whose content does not require authorisation, or which have been withdrawn by the applicant.
(c) Up to 2000, this includes projects authorised, rejected and returned. From 2001, only projects authorised feature.

On the deposits side, and in keeping with the heightening degree of competition, the number of applications has grown significantly over the past four years. In 1998 offers focused on deposits the return on which was linked to changes in the levels of indices, stock market indices in particular. In 1999 and 2000, the emphasis was more on traditional term deposits and sight accounts with returns close to those on the interbank market (although the raising of these deposits was confined to Internet or telephone-exclusive channels). And in 2001 the focus shifted to so-called mixed deposits, comprising a short-term deposit with a fixed interest rate and a structured deposit over a substantially longer term, justifying the 42 % increase that year in deposit-advertising authorisations.

In terms of numbers of institutions, 56 % of the cases processed are concentrated in banks, followed by savings banks with 20 %, specialised credit institutions (SCIs) with 16 % and, further back, credit co-operatives with 8 %. The preponderance of banks over savings banks can be explained first, in terms of their greater number, and further, because advertising by the latter is, like that of credit co-operatives, subject to the control of the regional governments. Only campaigns of a wider than regional scope are submitted to the BE's scrutiny.

The media most used are still daily newspapers, accounting for 39 % of authorisations, a figure that has held up – with slight changes – in recent years. The heading "other media", however, encompasses a greater number of authorised projects, given the wide range of media included: posters, leaflets, hoardings, teletext, Internet, weekly newspaper spreads, letters, etc. There was a notable rise in 2001 in Internet-based projects.

As regards settlement of the cases processed, most are authorised, or have their authorisation extended if modifications are involved. Nonetheless, behind this authorisation in many cases are suggestions made during processing with a view to enhancing the transparency of the offer. This is why such a small proportion is expressly rejected: 1.33 % in 2000 and 0.93 % in 2001. Rejections are generally due to content, either because the advertising contains no cost or return for the general public, or because there are references to other non-bank financial instruments routed through the institutions themselves (mutual funds and insurance operations).

In rare instances involving the advertising of offers that have not received the central bank's mandatory authorisation, the BE demands that the institutions withdraw them immediately.

III.1.3. Standard contracts of certain operations with securities

As an exception to the general principle whereby bank contracting is not formalised in previously approved contracts, approval and registration of standard contracts for safe custody deposits and repos is obligatory under the rules governing the workings of the securities markets. This function is normally assigned to the CNMV, but the BE takes responsibility when the contracts cover exclusively instruments traded on the Public Debt Book-Entry Market. The aim of this procedure is to ensure that the contract includes, in a clear and orderly fashion, all the essential characteristics of the operation.

The BE also receives Book-Entry Government Debt contracts of operations considered as financial accounts, with a view to their transmission to the DGTPF (Directorate General of the Treasury and Financial Policy), which is responsible for approval here (2).

Over the past four years, the number of contracts analysed has been very small, since the institutions that operate with the products addressed in these standardised contracts (around one hundred) registered them in 1996. Registrations in the two following years corresponded to new institutions engaging in operations of this nature and to changes in those already registered (see Chart III.1).

III.1.4. Reporting of interest rates on lending operations

For the purposes mentioned at the outset of this section, banks, savings banks, Spanish credit co-operatives and the branches of foreign CIs are obliged to disclose a series of interest rates on their lending operations: their prime rate, the respective rates on current-account and credit-account overdrafts (both are applicable at the maximum rate unless lower rates are contractually envisaged), and the indicative reference rates relating to other financial facilities deemed most habitual or representative. In turn, institutions should report such rates, and changes therein, to the BE, indicating the dates from which they are applicable. The BE has been publishing these rates on its website so that they may be freely consulted by analysts and customers.

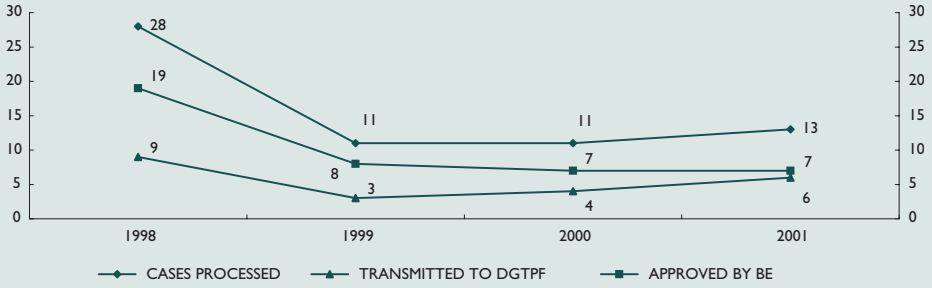
The number of these reports had been falling in recent years, until virtually stabilising in 2001. This pattern is fairly consistent with the greater stability of market interest rates. Nonetheless, the number of reports – 505 in 2001 – remains high, as the reference rates for consumer and mortgage loans, which are frequently updated by some institutions, are included (see Table III.3).

To gauge the public usefulness of these data, Table III.4 draws together the replies made in writing to CIs and to individuals to information requests, essentially in relation to the interest rates obligatorily reported (these consultations also relate occasionally to the commissions reflected in the charges brochures approved by the BE). The table also includes consultations by the courts channelled through the BE Legal Services. It further shows hits on the interest rate database on the BE's website where, as stated, the information contained in the reports is included.

(2) These powers are specified in section 8 of the Ministerial Order (MO) of 25 October 1995 on rules of conduct in the markets and obligatory registrations, and in the MO of July 7 1989 on financial accounts related to Book-Entry Government Debt.

CHART III.1

Standard contracts (number)



III.2. AUXILIARY OR COMPLEMENTARY SUPERVISORY ACTIVITIES

III.2.1. Official registers of supervised institutions

So as to give legal force to and publicise the "vetted access" principle (on which licences to operate are conditional) governing the presence of various institutions operating on our financial markets, and in order to publicise the fact that institutions are subject to supervision by the Spanish central bank, the BE is also responsible for keeping the public records in which, prior to engaging in their activity, the following institutions must be registered:

— All CIs licensed to provide banking services in Spain (banks, savings banks, credit co-operatives, SCIs, foreign branches of CIs, foreign CIs providing services without an establishment), and the representative offices of foreign CIs whose functions in Spain are of a merely commercial or market prospection nature.

— Currency exchange bureaux, the only establishments other than banks licensed to buy or sell foreign banknotes or make transfers abroad.

— Appraisal companies (ACs), to which this activity is confined when what are involved are movable goods or rights in the mortgage market or goods and rights suitable for setting up the assets of real estate investment funds or insurance companies.

— Mutual guarantee (MGCs) and reguarantee companies.

The existence of these Registers does not encroach on those (if any) the regional governments may have set up for the purpose of certification of the institutions over which they have certain supervisory powers. Such institutions are essentially savings banks whose registered offices are in the region and credit co-operatives whose operating scope does not

TABLE III.3

Reporting of interest rates on lending operations (number filed)

	1998	1999	2000	2001
Reports processed	898	619	531	505
Banks	*455*	*346*	*302*	*282*
Savings banks	*163*	*143*	*118*	*115*
Credit co-operatives	*180*	*130*	*111*	*108*

TABLE III.4

Consultations on interest rates and commissions (number)

	1998	1999	2000	2001
Consultations	**1,060**	**757**	**545**	**403**
By institution	660	471	383	319
Banks	*476*	*324*	*238*	*193*
Savings banks	*98*	*81*	*92*	*82*
Credit co-operatives	*7*	*14*	*13*	*9*
Other	*79*	*52*	*40*	*35*
By individuals	67	42	24	24
By corporations	69	52	28	11
By the courts	264	192	110	49
Internet consultations (a)	**15,683**	**20,318**	**14,642**	**15,830**

(a) Number of hits on the related BE website with information on the interest rates reported for institutions' lending transactions.

extend beyond the region in question. Nor do the Registers have any bearing on the more general powers of the Mercantile Registers.

Table III.5 lists the institutions under BE supervision and inscribed in their respective official Registers. The updated details can be viewed on the BE website.

Of the 34 additions in 2001, 8 relate to the branches of Community CIs, 6 to currency exchange bureaux and 5 to SCIs. The deletions were fundamentally in ACs [7], SCIs [7] and representative offices [6]. In 2001, 32 new Community institutions commenced operating without a permanent establishment in Spain, while only four institutions deregistered.

III.2.2. Other information filed with the Banco de España: directors and senior executives, shareholders, agents and statutes

The BE is responsible for keeping the *Register of directors and senior executives* of CIs. It also receives information on the directors and senior management of the other institutions supervised by it. The term "directors and senior executives" covers members of the Board of Directors of the company in question and its senior managers. Moreover, throughout the EU, and as provided for under harmonised Community regulations, those in senior positions of responsibility at CIs should have a recognised commercial and professional standing and reputation, in keeping with the factors envisaged to this end in the regulations.

At present, the most important function of these Registers, which are confidential, is to have at hand updated personal and professional data pertaining to those chiefly responsible for the activity of supervised institutions. This provides an auxiliary and additional component to the exercise of the supervisory and sanctioning powers assigned to the BE.

However, in the case of directors and senior executives of banks and credit co-operatives, the Register is also a specific element for monitoring the restrictions and "incompatibilities" to which such individuals are subject in respect of holding posts at other companies. The BE is responsible for such monitoring in this latter instance, while the regional governments monitor the analogous rules applicable to the directors and senior managers of savings banks. In these cases, inscription in the BE Register shall precede that required in the Mercantile Register, reflecting the need for prior vetting of incompatibilities as a requisite for effectively taking up a senior post.

As at 31 December 2001, almost five thousand directors and senior executives were listed in the related special Registers (see Table III.6).

TABLE III.5

Official registers of institutions as at 31 December (a)

	1998	1999	2000	2001
Institutions with an establishment	**604**	**585**	**579**	**576**
Credit institutions	404	391	371	369
Representative offices	69	67	62	60
Mutual guarantee companies	24	23	23	23
Reguarantee companies	1	1	1	1
Currency exchange bureaux and money transfer agencies (b)	—	10	42	49
Appraisal companies	106	93	80	74
Credit inst. operating without an establishment	**165**	**201**	**248**	**276**
Of which:				
Financial subsidiaries of Community credit institutions	2	2	2	2
Non-Community institutions	—	2	2	2

(a) The number of institutions also includes those that are non-operational and in the process of deregistering.
(b) Does not include foreign currency purchasing establishments.

Also noted in the Registers are the administrative penalties which the officials listed may have incurred in connection with the respective disciplining rules. This explains why other supervisory authorities direct numerous reputation-related inquiries to the Register. The BE also receives confidential information about the shareholders of banks and SCIs, and about the members of credit co-operatives, further to the obligation to report data quarterly on all shareholders or holders of contributions that are deemed to be financial institutions, and on those which, not considered as such, have attributed to their name shares or contributions accounting for a percentage of capital stock of the institution equal to or greater than 0.25 % for banks, 1 % for credit co-operatives and 2.5 % for SCIs (see Table III.7).

This information is intended for the basic supervisory tasks of the BE, it being essential for it to know the shareholder structure of the institutions under its supervision. Further, and most particularly, it makes for the readier exercise of the provisions which bring under BE control the ownership share of the biggest of these institutions, once this exceeds certain thresholds.

The number of shareholders included in banks' reports has fallen in relation to previous years. There has been a particularly significant drop (21 %) in the number of individual shareholders. The presence of foreigners in reported ownership interests has also been on a declining trend. The trend observed at SCIs has been similar to though less marked than that at banks. Conversely, co-operative members have shown greater stability.

TABLE III.6

Register of directors and senior executives (number)

	1998	1999	2000	2001
Directors and senior executives registered	5,604	5,187	5,030	4,946
Additions or deletions in supervised institutions	3,382	3,211	3,513	2,832
Of which:				
Initial additions	*655*	*644*	*767*	*570*
Reincorporations	*307*	*255*	*296*	*260*
Inquiries as to integrity of directors and senior executives	281	580	904	757
Average number of people listed per document	5	6	6	5

TABLE III.7

Register of shareholders (number)

	Banks				Credit co-operatives				Specialised credit institutions			
	1998	1999	2000	2001	1998	1999	2000	2001	1998	1999	2000	2001
Individuals	358	270	209	166	219	222	218	200	66	51	45	37
Corporations	664	606	547	521	228	216	204	217	182	172	154	144
Credit institutions	*130*	*135*	*123*	*113*	*103*	*100*	*91*	*75*	*72*	*69*	*63*	*67*
Other	*534*	*471*	*424*	*408*	*125*	*116*	*113*	*142*	*110*	*103*	*91*	*77*
MEMORANDUM ITEM:												
Spanish	252	649	554	483	446	435	421	416	224	201	179	162
Foreign	270	227	202	204	1	3	1	1	24	22	20	19

CIs operating in Spain (and the currency exchange bureaux licensed to process foreign transfers since early 2002) are also obliged to report to the BE their *agents*, i.e. the resident and non-resident individuals and corporations which they have authorised to operate habitually with their customers, in the name and on behalf of the principal, in the trading and execution of operations typical to their activity.

In turn, Spanish CIs must, with the same periodicity and criteria mentioned above, report to the BE the list of foreign CIs with which it has entered into agency agreements or agreements to provide financial services to customers (3).

The basic aim of such information is to enable the BE to follow, from a supervisory perspective, this new distribution channel for financial products which is complementary to and often replaces the traditional branch-based channel, and which is being massively and increasingly used by many institutions (Chart III.2 shows how, during 2001, it has grown by 21 %). The BE is further able hereby to verify certain obligations imposed on the institutions using such agents. The information received at the BE is not public, although institutions are obliged to include a list of the agents in their service in their annual report.

Finally, as an auxiliary means of control for the BE in respect of the amendment of supervised institutions' statutes [which are usually subject to authorisation by the Ministry of Economy, further to a report by the BE (4)] and, generally, as an additional supervisory instrument, the *Special registers of company statutes* are also the responsibility of the BE, reflecting as they do employer/union pacts that are usually of significance from a prudential and operational perspective. These registers were created further to the obligation for CIs and other supervised entities to report (after those included in their certificate of incorporation) the successive amendments to their statutes.

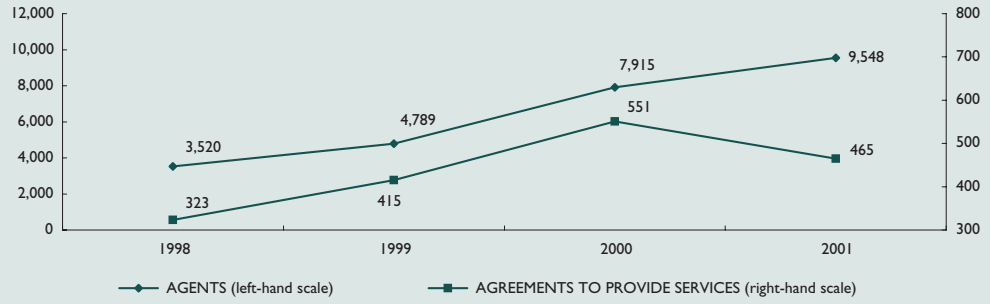
Cases processed involving the amendment of company statutes have held on the same course as in previous years. The biggest number of statutory changes has affected banks and credit co-operatives. In the case of the former, the source of such amendments has largely been due to the mandatory adaptation of statutes to changes in Spanish corporate law in 1998. As regards credit co-operatives, statutory amendments have also been connected to adaptation to the latest amendments to the State and regional rules affecting them.

(3) Article 22 of Royal Decree (RD) 245/1995 of 14 July 1995, and CBE 5/1995 of 31 October 1995.

(4) Banks, savings banks, credit co-operatives, SCIs and MGCs, although the licensing body varies (the related powers are the preserve of regional governments as far as savings banks and co-operatives within their sphere are concerned).

CHART III.2

Agents and agreements to provide services (number)



III.2.3. BE Central Credit Register

Since 1962 the Banco de España has been responsible for managing the Central Credit Register (5) (CCR), whose main aim is to provide reporting institutions (CIs and others) with the data necessary for improving analysis and surveillance of their credit exposures. The CCR also enables the BE to obtain data on institutions' loans and contributes thereby to the smoother and proper exercise by the BE of its banking supervision powers.

Although the content and functioning of the CCR is described in Annex 1, it should be pointed out that, as from a minimum quantitative threshold, the amount of virtually all direct and indirect exposures, whether on or off-balance sheet, incurred by institutions are, along with the related borrowers, reported monthly. And so too are other descriptive data of exposures, particularly those relating to bankruptcies or to the failure of debtors to comply with obligations. The access by each institution to the data recorded in the CCR encompasses the aggregate information on all the risk in the system of the borrowers reported by said institution, or those which, while not reported, have expressly authorised access to their data. Debtors are also entitled to access and rectification under data protection rules, in which connection they can approach the CCR so that it may provide them with the report or reports relating to their exposures as reported by each institution. Nonetheless, the necessary accuracy of the information, combined with the large volume of reported borrowers and exposures, means that a set of the latter, in which a specific impact has arisen, is blocked (the information is included in the reports) while the scope of the impact is being resolved.

At present, over 20 million exposures are recorded at the CCR for an amount of €1.36 billion, relating to over 12 million borrowers, 94 % of which are individuals resident in Spain (see Table III.9).

The number of additions and deletions in respect of borrowers reported by institutions over the past year has fallen, but additions remain on a favourable trend. Although there is some correlation, there is not a perfect correspondence between the difference in additions and deletions and the change in the number of the reported set of different borrowers. This is because the former are an aggregate of the changes in the borrowers of each institution, with the subsequent possibility of borrowers recurring across different institutions. Thus, while the difference between additions and deletions was 947,000 borrowers, the change in the series of

(5) The inception and functioning of this Register was provided for in article 16 of RD-Law 18/1962 of 7 June 1962. The draft bill of the legislation on the reform of the financial system includes a new legal regulation of the Register.

TABLE III.8

Register of company statutes (number)

	1998	1999	2000	2001
Amendments registered	208	204	328	290
Cases processed	64	56	42	39
BY TYPE OF INSTITUTION:				
Banks	19	26	21	13
Savings banks	2			
Credit co-operatives	29	18	17	12
SCIs	8	8	4	6
MGCs	6	4	4	8
PROCESSING CHANNEL:				
Reported to DGTPF	39	45	40	36
Reported to Regional Governments	25	11	2	3

different borrowers was only 627,000. Though moderate, the 6 % increase in different borrowers is in contrast to the over 20 % fall in additions and deletions, which would denote a sharp decline in the rotation of debtors among institutions.

The continuing growth of different borrowers has led to the subsequent increase in the number of exposures (7 %) and amounts reported (11 %), and to a parallel increase in the various categories of reports obtained. The exception here has been those requested by the courts, which are on a declining trend. The rise in average exposures reported highlighted by the discrepancy between the two aforementioned rates is closely related to the buoyancy of the mortgage market for the financing of housing discussed in Chapter I.

III.2.4. Eligibility of hybrid capital instruments as own funds in the solvency ratio

As discussed in Chapter I, included among the elements eligible as own funds are some which meet, albeit to a lesser degree than ordinary capital, certain requirements assimilating them partly to ordinary capital, namely: the capacity to offset losses; long-term or indefinite permanence in the institution; and returns depending, in certain cases, on the existence of sufficient profits. Such characteristics have led these elements to become known as hybrid capital instruments.

These instruments are widely used both by Spanish banks and by institutions in our peer countries. Many such instruments have achieved a degree of uniformity in terms of their basic financial characteristics that provides for their distribution and widespread trading on international markets and, as a result, their habitual placement in institutional investors' portfolios.

The instruments in question are: so-called subordinated financings, the main particularity of which is that, as regards the priority of claims, they are placed behind all common creditors; and preference shares, issued as a capital-like instrument by special-purpose entities that are subsidiaries of Spanish CIs, and which have fewer voting rights in exchange for certain dividend privileges.

Such instruments are freely issued; however, when they are comprised of serial securities, they are subject to the regulations of the securities market on which they are to be traded. Nonetheless, the BE must verify that these instruments meet the regulated conditions envis-

TABLE III.9

Key data of the BE Central Credit Register

	1998	1999	2000	2001
Reporting institutions (number)	435	420	400	397
Exposures admitted (number)	15,543,303	17,270,767	19,006.985	20,265,305
Of which:				
Banks	*6,322,441*	*7,165,923*	*7,740,929*	*8,114,700*
Savings banks	*7,104,127*	*7,832,475*	*8,743,234*	*9,402,126*
Credit co-operatives	*1,041,787*	*1,176,068*	*1,320,935*	*1,448,149*
Amount (€ millions)	887,131	1,045,264	1,224,434	1,354,570
Of which:				
Banks	*487,133*	*563,236*	*659,958*	*673,076*
Savings banks	*309,816*	*370,830*	*457,289*	*530,501*
Credit co-operatives	*36,568*	*44,381*	*53,033*	*62,002*
Different borrowers (number)	9,559,443	10,493,103	11,396,892	12,066,861
Of which:				
Resident individuals	*8,954,192*	*9,845,232*	*10,702,969*	*11,330,480*
Resident corporations	*598,626*	*640,285*	*684,523*	*725,310*
Non-resident individuals	*2,763*	*3,206*	*4,395*	*5,297*
Non-resident corporations	*3,860*	*4,380*	*5,005*	*5,774*
Ineligible borrowers (number)	14,719	13,412	10,782	9,697
Suspended exposures (€ million)	770	938	485	435
Borrowers: additions (number)	4,970,414	5,559,930	6,571,506	5,211,644
Borrowers: deletions (number)	3,520,663	4,299,281	5,356,474	4,264,817
REPORTS (number):				
Automatically	141,329,744	157,271,115	173,217,385	185,632,065
Requested by reporting institutions	944,875	1,155,769	1,321,546	1,647,409
For debtors	30,733	35,877	39,588	45,015
Data Protection Agency	22	9	77	132
Courts	1,278	896	695	443
Other central credit registers	4	8	3	9
Access and rectification rights exercised (number)	14,088	16,870	18,677	19,932

aged in bank solvency rules as a requisite for their eligibility as own funds of the individual institution or of its consolidable group (6).

As is discussed later, most of these instruments are traded on organised markets. However, some issues are still often distributed to customers through institutions' branch networks. In this latter case in particular, the BE insists on the need for customers to be informed about the nature of such securities, which constitute venture capital in the true sense of the term. And, when the interest rates applied do not realistically reflect this fact, the BE warns issuers of the potential reputational risk they may be incurring.

In recent years, the amount of funds raised through these instruments has grown significantly (105 % in 1998, 59 % in 1999 and 16 % in 2000), although it has fallen by almost 6 % in 2001. Currently, these instruments are denominated predominantly in euro (see Table III.10).

In 1998, subordinated debt accounted for 44 % of the total classified as eligible own funds. The proportion reached 80 % in 2001 (virtually all in tradable securities), with a trough of 31 % in 1999. This minimum was the result of the substantial rise in issues of preference shares, as savings banks joined this market segment.

The higher quality subordinated debt such as venture capital (such quality being due to its indeterminate maturity and to the possibility of its use to absorb losses in certain cases

(6) Envisaged in article 8 of CBE 5/1993 of 23 March 1993, on the determination and monitoring of minimum own funds.

TABLE III.10

Issuance by consolidated groups of credit institutions of instruments eligible as own funds (€ million)

	1998		1999		2000		2001	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount
TOTAL	**48**	**5,156.0**	**63**	**8,202.7**	**71**	**9,497.5**	**72**	**8,947.9**
Subordinated debt	**39**	**2,292.8**	**52**	**2,552.7**	**65**	**5,771.8**	**60**	**7,178.8**
Traditional	29	2,290.4	32	2,500.1	48	5,721.0	58	6,853.6
Banks	12	1,393.8	9	801.7	18	4,403.2	22	4,287.3
Savings banks	14	868.8	13	1,591.2	17	1,175.5	17	2,382.6
Credit co-operatives	—	—	2	12.1	5	87.0	2	72.0
SCIs	3	27.8	8	95.1	8	55.2	17	111.7
Of which:								
In pesetas/ecu/€	*24*	*1,702.7*	*32*	*2,500.1*	*44*	*3,535.0*	*58*	*6,853.6*
In $ USA	*3*	*282.3*		*0.0*	*2*	*1,758.7*		*0.0*
Of foreign subsidiaries	*6*	*887.6*	*2*	*620.0*	*11*	*4,151.0*	*12*	*2,626.0*
Loans	*5*	*41.6*	*11*	*140.7*	*14*	*202.4*	*24*	*161.0*
Undated	10	2.5	20	52.6	17	50.8	2	325.3
Banks	—	—	1	50.0	—	—	1	322.6
Credit co-operatives	10	2.5	19	2.6	15	1.7	0.0	
SCIs	—	—	—	—	2	49.1	1	2.7
Of which:								
In pesetas/ecu/€	*10*	*2.5*	*20*	*52.6*	*17*	*50.8*	*1*	*2.7*
Preference shares	**9**	**2,863.1**	**11**	**5,650.0**	**6**	**3,725.7**	**12**	**1,769.1**
Banks	9	2,863.1	6	3,050.0	3	1,325.7	3	729.1
Savings banks	—	—	5	2,600.0	3	2,400.0	9	1,040.0
Of which:								
In $ USA	*4*	*802.9*	—	—	*1*	*324.7*	*1*	*269.1*
In pesetas/ecu/€	*3*	*1,550.0*	*11*	*5,650.0*	*4*	*2,580.0*	*11*	*1,500.0*

without entailing the liquidation of the institution) has traditionally been marginal, and instrumented via contracts between parent companies and subsidiaries. The year 2001, however, saw the first issue targeted on the general public, and this type of debt came to account for 5 % of the total volume of qualified subordinated debt that year.

Offerings of preference shares to end-1998 were targeted almost exclusively on the US market. Their distribution on the Spanish market began in that period (under the trade name of *participaciones preferentes* (preferential equity holdings), bringing about a situation in which all issues of this nature were placed in Spain in 1999.

III.3. PUBLIC DEBT BOOK-ENTRY MARKET

Under the provisions of Law 24/1988 of 28 July 1988 on the Securities Market, the BE is the governing body of the Public Debt Book-Entry Market, which it manages in-house through the Central Book-Entry Service (see Annex 1). Moreover, the same legal text attributes supervisory and inspection powers to the BE over members of this Market, account holders trading on their own behalf in the Central Book-Entry Service, Management Companies, and also over the securities market-related activities of the CIs listed in its official Registers.

As in other cases where supervisory and inspection powers fall to both the BE and the CNMV, the Law on Securities Markets stipulates that both institutions shall co-ordinate their activities pursuant to the principle that oversight of the solvency of the financial institutions concerned shall be for the institution that maintains the corresponding Register and that of the functioning of the securities markets for the CNMV.

TABLE III.11

Public Debt Book-Entry Market: specific inspections

Year	Institutions inspected (number)				Non-market members' outstanding balances	
	Credit institutions	Branches of banks domiciled in EU	Securities firms	Total	€ million	Percentage of system total
1999	5	1	2	8	6,192	2.7 %
2000	7	—	—	7	11,455	4.5 %
2001	4	—	1	5	71,045	28.7 %

Irrespective of the fact that, in the course of general supervision of CIs, attention is paid to their activity on the Public Debt Book-Entry Market, since the creation of this market specific inspection functions have been assigned to a specialised group that has focused essentially on management companies and, most particularly, on their activity recording the outstanding balances of their clientele. The activities of this group in the years 1999-2001 are shown in Table III.11 indicating the non-market member book-entry account outstanding balances corresponding to institutions inspected, along with the relative weight of such balances in the system total.

III.4. MORTGAGE MARKET

Law 26/1988 on the discipline and intervention of CIs attributes to the BE, without prejudice to the functions assigned to the CNMV, the monitoring and inspection of the workings of the mortgage market in accordance with the provisions of Law 2/1981 on the regulation of said market. Such control extends to the conditions of mortgage loans that cover refinancing operations via the issuance of specific mortgage securities and the monitoring of these operations.

The qualifying conditions for loans (7) include most notably the following: that the loan should not exceed a specific percentage (70-80 % in the case of housing) of the rated value; and that the asset to be mortgaged should have been valued, using criteria set in a 1994 MO, by specialised companies or services that must be officially recognised as such (8) by the BE and are subject to BE supervision.

Further, so that customers might compare offers and make a reasoned decision on an operation of such importance for individuals as is taking out a mortgage loan, the MO of 5 May 1994 laid down specific informative obligations for CIs. These included the preparation of an informative brochure and the formulation of a binding offer. The Order entrusts the BE with the specification of official reference indices which, on the basis of their objectivity, may be applied by institutions to floating-rate mortgage loans. So as to increase transparency, the BE is obliged to publish these indices regularly.

III.4.1. Refinancing

The refinancing of loans may be undertaken via the securities envisaged under the attendant Law, namely mortgage-backed securities. The Law defines three types of securities: "cédulas", bonds and collateralised mortgage bonds. "Cédulas" are backed by the institution's

(7) The remaining conditions relate to the effectiveness of the mortgage (first mortgage), the ownership of the assets and the obligation to contract insurance against damage.

(8) Official recognition is likewise necessary so that valuations may be effective on assets that cover the technical provisions of insurance corporations, or that are part of the assets of real estate collective investment undertakings or of pension funds.

overall set of mortgages, provided they have not been specifically earmarked. Bonds are backed by the mortgage loans assigned to this end, and will require an entry in the Property Register in which the mortgage is inscribed. Collateralised mortgage bonds are issued on the basis of a specific loan (or portion thereof).

A proportion of around 5 % of the balance sheet value of the mortgage loan has been refinanced through the issuance of mortgage market securities. This refinancing proportion rose to 5.9 % in 1999, when issues of mortgage "cédulas", particularly those aimed at the international market, grew significantly. The securitisation of loans on the balance sheet is done mainly through the issuance of "cédulas" and collateralised mortgage bonds, given their greater flexibility.

Paving the way for the issuance of collateralised mortgage bonds was Law 19/1992 of 17 July 1992. This legislation provided for the grouping together and subsequent assignment to mortgage securitisation funds of collateralised mortgage bonds effectively ceding the risk on shared loans. These closed-end funds issue mortgage-backed bonds: fixed-income securities, usually long-term, that also incorporate the risk of the underlying loans. Set against collateralised mortgage, these bonds have two advantages: they dilute the risk of individual loans (given that each share corresponds to a specific loan), and they are more versatile, since they permit the generation of securities bearing different levels of risk and return aimed at different investors, through the issuance of different tranches duly subordinated in respect of the credit risk they incorporate. Mortgage-backed bonds are usually graded by a rating agency, which smoothes their placement on the market. Mortgage securitisation funds and the issuance of the aforementioned bonds are supervised by the CNMV.

Mortgage securitisation has developed significantly, particularly since 1998, and has brought a long-term, private, fixed-income instrument onto the market, broadening the limited array of securities of this nature. Another reason for growth here is the fact that removal of loans from the balance sheet reduces capital requirements, while the originating institution does not lose contact with the final customer, since it continues to administer the loan (and to receive, accordingly, the related return on the Fund). However, the ultimate aim of securitisation has occasionally been solely to provide institutions with fixed-income securities to act as collateral so that they might improve their liquidity position in the market and their access to ECB tenders.

If, along with the positions that remain on the balance sheet, regard is had both to the collateralised mortgage bonds grouped together for the issuance of mortgage-backed bonds and to their related mortgage loans removed from the balance sheet, then the refinancing ratio of the total mortgage credit managed by CIs was 9.4 % in 2001, down from a peak of 9.8 % in 1999 (9), almost 4.5 points more than would be the case considering only balance-sheet positions (see Chart III.3).

III.4.2. Official reference indices

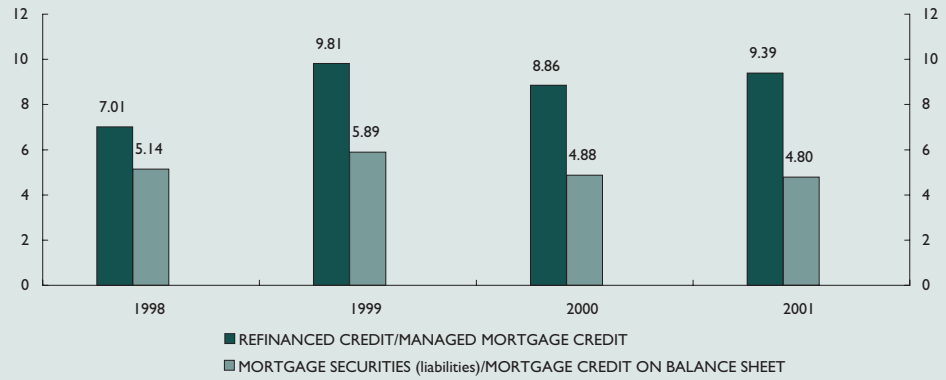
Pursuant to the implementation of the MO of 5 May 1994, the BE defined six official rates (10). The use of these rates offers advantages for CIs, which do not have to inform customers individually of changes therein. Customers also benefit, identifying the characteristics

(9) The mortgage securitisation operations referred to here have been conducted exclusively under the terms of Law 19/1992. Nonetheless, mortgage loans, like any other asset or credit right, can also be securitised under RD 926/1998.

(10) The exact definition of these indices is in CBE 8/1990.

CHART III.3

Refinanced mortgage credit



of these rates thanks to their transparent, reliable and timely preparation. And so too do the markets, insofar as use is conducive to the concentration of the reference indices of variable-rate operations.

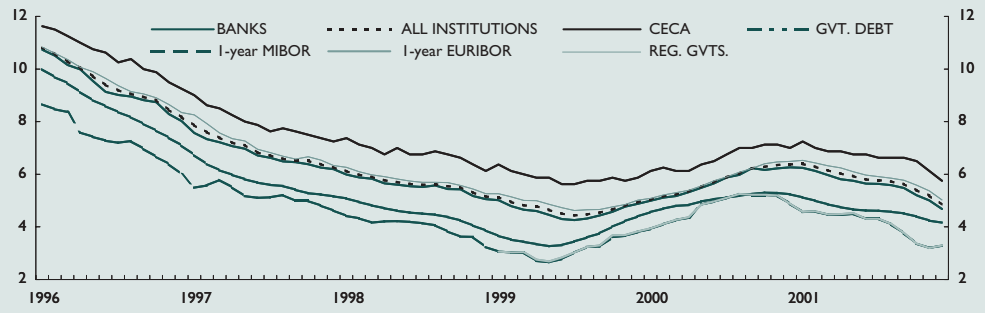
Three of the above-mentioned rates express the average cost on the market of a mortgage loan transaction for the purchase of private housing, and they refer to banks, to savings banks, or to total institutions. The other rates denote an average rate for mortgage and consumer loans at savings banks (the so-called CECA rate); the internal rate of return on public debt at a term of between two and six years; and the cost for institutions of financing themselves at one year on the interbank market (Mibor/Euribor).

In recent years, competition among CIs has largely been in the field of mortgage credit, in general, and – hereunder – in variable rates, in particular. The urge to offer products that immediately reflected cuts in interest rates (see Chart III.4), and the advisability of correlating financial revenue with financing costs are factors that justify the choice of the Mibor/Euribor as the preferred benchmark for the period. Nonetheless, the use of benchmark indices of mortgage lending operations are also widely accepted, their advantage being the greater long-term stability of the index and its closer relatedness to the typical returns on these operations.

CBE 7/1999 of 29 June 1999, in acknowledgement of the leading role the Euribor would assume following the foreseeable displacement of the Mibor, had already recognised

CHART III.4

Official reference rates



the monthly average of the one-year Euribor as an official index, following the European Banking Federation's definition. Shortly afterwards, the MO of 1 December 1999 abrogated the one-year Mibor as an official rate for loans entered into as from 1 January 2000. The need to continue publishing the Mibor to give continuity to loans indexed to it has led to the replacement of the one-year Mibor by the corresponding Euribor in the daily series used to calculate averages on days when there are no operations at this term on the Madrid interbank market. In sum, a process of gradual displacement between these two fundamental mortgage market references has been under way.

III.4.3. Appraisal companies

RD 775/1997 of 30 May 1997, which regulates the current arrangements applicable to ACs and to CIs' appraisal services, made a demand for greater organisational, staff and financial resources as a requisite for obtaining or retaining official approval to perform appraisals. The intention here was to promote the professionalisation of the sector and, thereby, the quality of valuations. These are essential not only to the mortgage market but also to undertakings for collective investment in real estate assets and insurance companies.

This has given rise to a re-organisation of the sector, with a sizable reduction in the number of participants in recent years. Hence, of the 171 companies registered as at 31 December 1996, of which only 123 were operational, 71 remained as at end-2001. Virtually all the deletions in 2000 and 2001 were at the request of the companies themselves.

The turnover of these institutions continued to grow significantly during 2001 (see Table III.12). The number of appraisals made was up 8 % on the previous year, while the rise in unit values provided for a 23 % increase in the figure (millions of euro) for the appraisals performed. Individual housing units are the main item of appraisal, accounting for 78 % of the total, although they represent only 36 % of the amount rated. Completed residential buildings, meanwhile, accounted for 3 % of total appraisals but 25 % of the rated value for the year. The breakdown of other appraisals was into commercial premises, offices, industrial premises and other buildings, and land. The main users of the appraisals performed are savings banks and banks, accounting for 48 % and 35 % of the total, respectively.

The BE's supervision of appraisal companies and services has been geared to verifying effective compliance with official recognition and approval requirements (exclusivity of activity, effectiveness of capital stock, professionalism of appraisers, public liability insurance, resources, etc.); to certifying adaptation to the applicable regulations (11) of the appraisal reports and certificates issued, for the purposes envisaged in mortgage market legislation; to reviewing compliance with all other applicable rules (internal controls, official records, appraisals file, etc.); and, lastly, to analysing the information reported to the BE (Register of directors and senior executives, statements required under CBE 3/1998, Annual Reports and other information).

III.5. OTHER INSTITUTIONS UNDER THE SUPERVISION OF THE BANCO DE ESPAÑA

III.5.1. Mutual guarantee and reguarantee companies

MGCs are open-end capital companies specialising in the extension of unsecured guarantees by bank-guaranteed backing or other legally acceptable means (other than suretyship insurance) to their shareholders. They usually operate in a specific territory or business sector.

(11) MO of 30.11.94.

TABLE III.12

Appraisal companies and services: key data

	1998	1999	2000	2001 (a)
Operational appraisal companies (number)	95	85	75	71
Appraisal services (number)	5	4	3	3
Of which:				
Banks	*2*	*1*	*1*	*1*
Savings banks	*2*	*2*	*1*	*1*
Credit co-operatives	*1*	*1*	*1*	*1*
Number of appraisers	7,111	7,013	7,275	7,515
Of which:				
Associate appraisers	*534*	*666*	*588*	*573*
Number of appraisals (000s)	866	980	985	1,005
Of which:				
Housing	*668*	*758*	*719*	*788*
Commissioned by banks	*336*	*389*	*348*	*354*
Commissioned by savings banks	*405*	*438*	*438*	*478*
Appraisals performed (amount in € million)	148,291	193,340	226,051	272,708
Of which:				
Housing	*59,666*	*75,919*	*82,791*	*100,615*
Commissioned by banks	*50,155*	*69,597*	*74,215*	*83,543*
Commissioned by savings banks	*68,585*	*85,176*	*102,413*	*126,031*
Appraisal companies				
Total assets (€ million)	*82.8*	*86.1*	*87.4*	*96.1*
Results (€ million)	*8.3*	*10.3*	*9.3*	*15.3*
ROE (%)	*27.8*	*32.5*	*25.3*	*38.7*

They came into being in 1978 with a view to smoothing the access of SMEs to bank financing. In 1988 they were classified as institutions subject to prudential supervision by the BE, and at present their legal regime is governed by Law 1/1994 of 11 March 1994 and its implementing regulations.

Since April 2000, the risks guaranteed by MGCs have been treated the same as those backed by CIs. Said risks are weighted at 20 % for the purposes of the capital requirements on financial institutions subject to compliance with the solvency ratio (12).

The outstanding risk of MGCs held at a growth rate of over 11 % in 2001, enabling total commissions revenue to be maintained with a reduction in unit costs (see Table III.13). The profit generated by these institutions is usually very small, as a result both of their mutual-society origins (commissions revenue is usually of a similar amount to operating expenses) and of the practice of neutralising profits at the close of each year through the provisioning of a fund (technical provisions fund) that contributes to bolstering the institution's solvency.

The number of patron members (usually regional or local governments and institutions, savings banks and other territorial- or sectoral-based private institutions) has held very stable, accounting for 1 % of total members. Conversely, the number of participating members has been growing at a rate of approximately 5 % per annum over the past five years, albeit on a slightly declining trend since 1998.

Also underpinning the activity of MGCs are the subsidies they receive from their public patrons. Such subsidies are usually of several types (operating, profit, directly to MGCs or to the members backed by the commissions to be paid, and to own funds) and generally take the

(12) MO of 13 April 2000, which transposes the Community regulations and amends the MO of 30 December 1992, on the solvency of CIs.

TABLE III.13

Mutual guarantee companies: key data

	1998	1999	2000	2001
Operational entities (number) (a)	21	21	21	21
Patron and participating members (number)	50,849	55,244	58,598	61,341
Of which: participating members	*50,190*	*54,566*	*57,913*	*60,648*
Outstanding risk on guarantees (€ million)	1,434	1,737	1,989	2,210
Of which: technical	*358*	*460*	*555*	*572*
Reguaranteed risk (€ million)	638	769	935	1,026
Doubtful assets and risks/total risk (%)	5.20	3.95	4.06	3.97
GUARANTEES EXTENDED DURING THE YEAR (€ million)				
Applications	1,075	1,148	1,157	1,208
Number extended	836	893	913	959
Number formalised	750	825	855	950
Reguarantees formalised	331	389	329	332
Results (€ million)	–1.2	–0.4	–0.3	0.7
Return on average total risk (%)	–0.08	–0.02	–0.01	0.03
ROE (%)	–1.28	–0.38	–0.22	0.49

(a) There are 23 in the Register, but 2 of these are inactive and are in the process of being liquidated and wound up.

form of special contributions to capital or to the technical provisions fund. In addition, in the case of the principal institutions, the support of public patrons is strengthened by the re-guaranteeing of operations in a percentage range of between 25 % and 40 %.

MGCs also have a reguaranteeing system with the State-owned company Compañía Española de Reafianzamiento, S.A. (CERSA), which covers between 30 % and 75 % of financial backing operations. This system is free of charge and, in addition to giving financial backing to MGCs' operations, it is intended to promote the proper management of the risks assumed and improve their quality. If the MGC does not meet the risk management quality standards required, CERSA may demand that it disburse a compensatory premium for the greater risk assumed in the reguarantee.

Given the characteristics outlined, BE supervision has focused on the analysis of risks per guarantee extended and on the firmness and continuity of the commitments entered into by patron members, whether through subsidies or reguarantee contracts.

III.5.2. Currency exchange bureaux

In 1998 (13) a new legal regime was established for the licensing of and engagement in currency exchange and foreign transfer processing activities. The regime further governed the mechanisms for regularising the position of incumbents that had been engaging in these activities. The term for such was one year from the regime coming into force, with the attendant supervisory powers assigned to the BE.

In the period spanning the years 1999 and 2000 most of the sector was thus reordered to adapt it to the new, more demanding regulatory framework. Inter alia, the new regulation amended licensing and registration arrangements, moving from a system under which each establishment was individually licensed to operate to one under which authorisation is given to

(13) RD 2660/1998 of 14 December 1998 on foreign currency exchange in establishments open to the public other than CIs, issued further to the provisions contained in Law 13/1996 of 30 December 1996 on fiscal, administrative and social measures.

CHART III.14

Currency exchange bureaux and money transfer agencies. Key data

	1998	1999	2000	2001
AUTHORISED PROPRIETORS (number):				
Currency purchasing	5,043 (a)	1,850	2,939	2,928
Currency buying and selling	19 (b)	6	15	14
Transfers by resident foreign workers	40 (c)	3	24	32
Transfers (all)	1	3	3	
CURRENCY TRANSACTIONS (€ million):				
Purchases from customers	3,702	4,045	4,595	4,609
Sales to customers	132	228	37	0
Purchases from other currency exchange bureaux	60	114	106	147
Sales to other currency exchange bureaux	84	78	100	160
Sales to credit institutions	3,540	3,847	4,561	4,592

(a) Relates to the number of premises, not proprietors, since authorisation under the previous regulations was to each establishment.
(b) Of these only 11 applied for the new authorisation, 8 being authorised.
(c) Of these only 22 obtained authorisation.

a proprietor, who can freely open premises under the obligation of communicating this to the BE. Another significant amendment refers to proprietors seeking to engage in the buying and selling and/or processing of transfers, activities which are confined to public limited companies with a sole corporate purpose and capital requirements that grow commensurately with the activities they wish to perform. Conversely, buying and selling currency logically does not come under the roof of a sole corporate purpose, but may be undertaken as an accessory activity, for reasons of complementarity, by sole proprietors in certain sectors of activity (hotel and catering, travel agencies, etc.).

Progress was made in 2001 in the implementation of the rules applicable to currency exchange bureaux with the approval of CBE 6/2001 (14) of 29 October 2001. On the basis of the activity in which it is wished to engage, this Circular specifies the procedure for obtaining authorisation, the information that has to be reported to the BE, the rules on the transparency of operations and customer protection (particularly regarding the processing of transfers and the disclosure of the exchange rates and commissions applied), and the development of the figure of the agent for transfers. Nonetheless, in the light of the experience gained, it might be necessary in the near future to tighten institutional regulations even further, mainly in the sensitive area of companies processing foreign transfers.

Admittedly, it might be deducted from Table III.14 that the operations of these establishments have been focused on the purchase of banknotes and traveller's cheques from customers, which are in turn then sold in the main to the EU. But it should be borne in mind that, until mid-2002, and according to the provisions of the aforementioned Circular, appropriate information on the volume of transfers processed by licensed establishments will not be available. Only after that date will overall statistics on this area be at hand.

Supervision by the BE has been marked by the regulatory changes indicated, some of which will only be effective as from 2002. The on-site examinations performed have been aimed at gathering knowledge on the activity of these establishments, the procedures followed, their internal controls and compliance with transparency rules vis-à-vis customers, which has helped improve the implementation of rules in and knowledge of the sector. If anomalies are observed in the field of money-laundering operations, the SEPBLAC (Commission for the Prevention of Money Laundering and Monetary Offences) (15) is duly informed.

(14) Using the authorisation contained in aforementioned RD 2660/1998 and in the subsequent MO of 16 November 2001.
(15) See the related SEPBLAC Annual Report for the year 2001 (in Spanish only).

IV

INTERNATIONAL ACTIVITIES IN THE BANKING SUPERVISION AND REGULATION AREA

IV.1. BANCO DE ESPAÑA PARTICIPATION IN INTERNATIONAL BANKING SUPERVISION AND REGULATION FORA

IV.1.1. Introduction

The Banco de España (BE) participates actively in all international fora of which it is a member and where bank regulators and supervisory authorities meet to discuss banking policy, prudential regulation and supervisory matters bearing on credit institutions (CIs).

Most of the BE's international work in the supervisory area is related to its participation in working groups reporting to two European institutions, the European Commission (EC) and the European Central Bank (ECB), and, outside Europe, in those that report to the Basel Committee on Banking Supervision (BCBS). Also of some importance is its participation in another two international working groups: the OECD Financial Markets Committee and the group of central bank statisticians reporting to the Bank for International Settlements (BIS) in Basel.

The EC instituted the so-called Banking Advisory Committee (BAC) in 1977, under the terms of the First Banking Co-ordination Directive. The Committee is made up of high-ranking representatives drawn from the banking supervisory authorities, central banks and ministries for the economy of the Member States. Present as observers are the chairman of the "Groupe de Contact" (GdC) and a representative of the ECB.

The basic aim of the BAC is to assist the EC in drawing up new legislative proposals for the Council on prudential supervision in the EU banking industry. It also acts as a forum for discussion and advises on any matter relating to banking supervision and regulation in the EU. It is also the remit of the BAC to amend specific technical aspects of banking directives through the so-called comitology procedure. The BAC also helps the EC in matters pertaining to the transposition of banking directives into national legislation, examining whether this is consistently done or whether greater specificity is required. In this connection it is assisted by the Working Group on the Interpretation and Application of the Banking Directives (GTIAD). Finally, supervisory and regulatory authorities have to inform the BAC on specific decisions in the banking supervision area, such as, for instance, bilateral co-operation protocols entered into with third countries or the licensing of third countries' institutions.

In October 1998 the ECB set up the Banking Supervision Committee (BSC) as one of the Committees of the European System of Central Banks. The forerunner of this Committee was a sub-committee of the Committee of European Community Central Bank Governors created in 1989, which operated in the European Monetary Institute as from 1994. The BSC is made up of representatives from Europe's central banks and, if responsibility for prudential

supervision is not the central bank's preserve, from the banking supervisory authorities. The EC and the chairman of the GdC have observer status.

Its tasks, laid down in article 105 of the Treaty on European Union, are to assist the ECB with regard to the prudential supervision of CIs and the stability of the European financial system, focusing chiefly on macroprudential aspects. To comply with its basic remit, the BSC analyses macroprudential issues, studies developments in banking and financial systems and provides for a smooth exchange of information between the European System of Central banks and banking and financial supervisors. Finally, the BSC assists in the preparation of the opinions issued by the ECB on draft national or EU bank regulations.

Also worthy of mention is the GdC, the longest-standing EU banking supervision group which was created in 1972. Although it does not report formally to any superior body, its role and existence are acknowledged in the banking directives. Its members are drawn from each of the banking supervision agencies of the 15 Member States; Norway, Iceland and Liechtenstein, which belong to the European Economic Area (EEA), are present as observers, along with a representative of the EC.

The GdC is intended to be a body where supervisors can exchange information on individual cases relevant to banking supervision, review regulatory developments in Member States' supervisory systems, and prepare comparative reports from the perspective of banking supervisors on regulatory and supervisory issues. It may prepare such reports on its own initiative or upon the request of the BAC or the BSC.

As regards international institutions outside the scope of the Community, the BCBS was set up at the close of 1974 by the central bank governors of the G-10 countries. The BIS provides the BCBS with the necessary material and organisational support, including the secretariat, but that does not entail a hierarchical reporting link between the two. At present, the members of the Committee represent 13 countries: the 11 making up the G-10 plus Spain and Luxembourg. This means that 9 EU Member States participate (Belgium, France, Germany, Italy, Luxembourg, the Netherlands, Spain, Sweden and the United Kingdom), along with Canada, the United States, Japan and Switzerland. Moreover, the EC and the ECB have observer-status at meetings. Each country is represented by its central bank and also by the authority responsible for the prudential supervision of CIs.

The conclusions of the BCBS do not formally have, nor were intended to have, any legal force. Rather, the Committee formulates minimum requirements, guidelines and recommendations as to sound supervisory and bank management practices. Nonetheless, the resolutions and conclusions published by the BCBS greatly influence the regulations ultimately applicable to banks. That is due to the importance of the institutions sitting on the Committee and to their commitment that such resolutions and conclusions should ultimately have legal force in their respective jurisdictions.

Commencing 1996 the *Joint Forum* was set up under the auspices of the BCBS, the International Organisation of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors (IAIS). The Joint Forum is made up of banking, securities or insurance supervisors representing the 13 Member States. The countries are the following: Australia, Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Spain (CNMV), Sweden, Switzerland, the United Kingdom and the United States. The EC attends meetings as an observer. The active presence of the BE in the Joint Forum began in 2002, when it assumed the chair in representation of the BCBS.

BOX IV.1

Recent developments in European supervisory structures

The internationalisation of financial markets, the introduction of the euro, the growth of new financial products and the marked tendency towards consolidation and conglomeration have led to reconsideration in Europe of the suitability of the current arrangements for maintaining financial stability, the management of financial crises, and the implementation and maintenance of the legislation governing European financial services. In step with the need to eliminate the remaining obstacles to the establishment of integrated financial markets in the EU, all these developments led to various initiatives relating to regulation in the securities markets and to the analysis and reconsideration of the supervisory structure in the banking and insurance industries. Broadly, these initiatives are as follows:

— In the securities area, in July 2000 European Finance Ministries asked a group of experts of international renown to study and, if necessary, table proposals for improving the regulatory framework for the EU securities market. The resulting *Lamfalussy Report* (so called after the chairman of the group) reached the conclusion that significant benefits could be had by establishing an integrated financial securities market, but that such integration would be hampered by the current regulatory framework, which is excessively slow, rigid, complex and not readily adaptable to the pace of change of the global financial market. Moreover, existing rules and regulations have not been consistently applied in the EU, thereby jeopardising the prospect of a level playing field. Consequently, the Report put forward a four-level proposal:

  • Level 1 (which should be agreed upon through the usual co-decision procedure between the European Parliament and the Council of Ministers) consists of a high-level framework or principles containing solely the essential elements of a regulation, but which also specifies less essential elements to be agreed on in level 2;

  • Level 2 will be implemented through the so-called comitology procedure, by means of the interaction of national regulators and the EC, in a formal regulatory committee that defines, proposes and decides upon the non-essential details (but nevertheless still with legal force) defined at level 1;

  • Level 3, where a committee of regulators will act to improve the consistency of the daily transposition of and compliance with the legislation agreed upon in levels 1 and 2; and

  • Level 4, whose aim is to reinforce compliance with EU standards, overseeing proper transposition.

The four levels would be complemented by a greater degree of consultation and transparency among the different bodies and institutions involved.

— In the banking industry, even prior to the creation of the Lamfalussy Group, the Economic and Financial Committee that reports to the European Finance Ministers (ECOFIN) established an ad hoc working group on financial stability in autumn 1999. In its report of April 2000, the *Brouwer Group* reached the conclusion that the institutional agreements in place (committees) provided a consistent and flexible base to safeguard financial stability in Europe, although their workings in practice needed to be improved. For instance, the report recommended reinforcing inter-sectoral co-operation at the international level, and called for efforts to be made to achieve greater convergence in supervisory practices. At no point did the report address crisis management. Nonetheless, this matter was tackled in a subsequent report by the Brouwer Group published in April 2001. This report arrived at the conclusion that it was necessary to reinforce international co-ordination and co-operation to ensure effective crisis management in the EU. In this connection, it made a series of recommendations. Among others, the Brouwer Group recommended lifting any legal obstacles still hampering the exchange of information among supervisors, with central banks, payment system supervisors and deposit guarantee system managers, at both the international and inter-sectoral level, in order to tackle effectively issues relating to crisis management.

— Although the two Brouwer reports concluded that major changes to the structure of European banking supervision are not needed, the application of its recommendations was subject to a subsequent review by the Economic and Financial Committee, with a report to ECOFIN. Furthermore, the subsequent Lamfalussy Report has strongly influenced deliberations in the other two industries (banking and insurance). Though this latter report focuses on the resolution of problems in the securities industry, the EC has announced its intention to consider whether the analysis and the solutions proposed by this report, with its four-level standards, would be applicable to the other industries, particularly in relation to the future regulatory capital arrangements stemming from Basel II.

At present, therefore, study is under way as to how the conclusions of the Lamfalussy Report should be applied, both in banking and insurance business. This means that the structure of European banking and insurance committees will in all likelihood be changed in the future.

The Joint Forum studies aspects of common interest to the three financial sectors involved. At first it focused exclusively on matters relating to the supervision of financial conglomerates (structure, capital adequacy, etc.). Subsequently, it broadened its remit to the analysis of other matters of common interest to supervisors in the three industries (risk management, corporate governance, etc.).

As regards the other working groups, the Financial Markets Committee (FMC) is the OECD vehicle for all matters pertaining to financial markets and services, excluding insurance activity. The FMC is made up of representatives from the regulatory and supervisory agencies (Finance Ministries and Central banks) of the Member States. The FMC is mandated by the Council to study measures aimed at improving the workings of national and international financial markets. It attempts to adjust its activities rapidly to changing circumstances and to the interests of market regulators and agents. The documents studied by the FMC or the findings of its work are, insofar as their dissemination is considered to be of great interest, published in the four-monthly review *Financial Market Trends*.

Finally, the BIS releases two sets of international banking statistics compiled using a uniform methodology agreed upon by the participating countries. First there is the local set, whose statistics are constructed from a Balance of Payments and National Accounts perspective, and which are therefore useful for studying countries' debt and the possible consequences of the currencies used in monetary control. The consolidated banking statistics are the second set. These are constructed from a banking supervision perspective and are useful for analysing the credit exposure of banking systems. Both types of statistics are released by the BIS in its *BIS Quarterly Review*.

A broad-based description follows of the work conducted in the main fora of banking regulators and supervisors, how these are structured into specialised working groups and the participation of the BE therein.

IV.1.2. Banco de España participation in the European Commission's groups

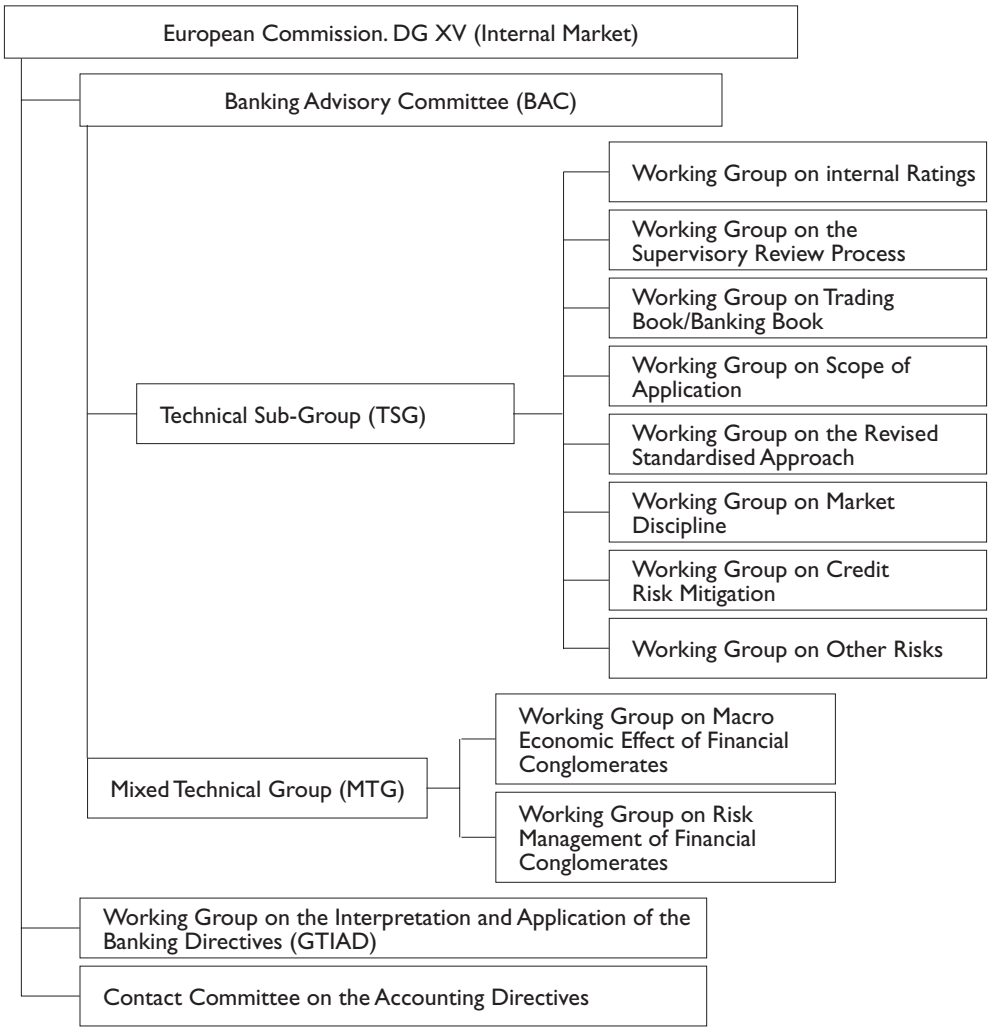
During 2001 the main work of the BAC focused on the preparation for the EC of prudential legislation relating to the review of the provisions on capital adequacy, to accounting standards and to the regulation of financial conglomerates in the EU.

In relation to capital adequacy, the EC has decided to include the recommendations that should arise from the BCBS as closely as possible in Community regulations, extending them to all CIs and investment companies, irrespective of their size. The decision is reasonable in that it is conducive to a level playing field. And further, as commented, 9 EU countries sit, in turn, on the BCBS. To meet this objective, the BAC has set up a technical subgroup (TSG) to which 8 working groups report. Each of these studies a specific aspect of the capital review being undertaken in Basel: the scope of the Accord, review of the standardised approach to credit risk, internal ratings-based approach to credit risk, credit risk mitigation, definition of trading books and banking books, other risks, supervisory review (Pillar 2) and transparency (Pillar 3). In addition to their technical monitoring of the work conducted in the BCBS, these working groups are also charged with drawing up an initial Community directive draft, which may differ from the new Basel Capital Accord in those areas which have been deemed not to conform to the specificities of European financial systems.

Turning to accounting regulations, the BAC set up an ad hoc working group to analyse the draft standard drawn up by the International Accounting Standards Board (IASB) and other

BOX IV.2

List of European Commission committees involved with regulation and banking supervision



accountancy regulators, in which it was proposed applying fair value (a concept developed in the standards) to all financial instruments, in view of its great importance for European CIs. Likewise, as a result of the draft Regulation drawn up by the Commission and the Parliament, whereunder it will be obligatory for all companies – including CIs – whose securities are listed on a regulated European market to apply directly International Accounting Standards (IAS) on preparing their consolidated financial statements, the BAC has decided to create a Sub-Committee on Accounting and Auditing to advise it on these areas. In addition, owing to the great significance supervisors attach to participating from the outset in the drafting of standards, the BAC will be accorded observer status in the Group of Technical Experts advising the European Advisory Group on Financial Information. A further place will be set aside for the BAC on the future EU Accounting Regulation Committee, whose functions will include the approval or rejection of IAS for their application in the EU.

With regard to the regulation of financial conglomerates in the EU, the EC set up a Mixed Technical Group (MTG), which reports to the banking, securities and insurance supervisory committees. Two working groups report to the MTG: one is engaged in the study of

capital adequacy, and the other in identifying inter-sectoral European financial groups and in analysing their significance in financial markets. In mid-2001, the EC presented a draft Directive for the regulation of financial conglomerates, and the BE participated actively in the EU Council Working Group that is preparing this Directive, chairing it in the first half of 2002. In that period a political agreement was reached on the Directive's content (see the box on regulatory changes in 2001 in Chapter II).

During 2001 the BE took part in 61 meetings of the BAC and the groups reporting to it, in 5 meetings of the group on the directive for conglomerates which reports to the Council, and in 8 meetings of the groups on accounting directives, which also report to the Council. Box IV.2 shows the organisation chart of the working groups reporting to the EC.

IV.1.3. Banco de España participation in groups reporting to the European Central Bank

The BSC is one of the Committees of the European System of Central Banks. The BSC has set up six working groups (see Box IV.3). The two groups most active in 2001 were those studying changes and developments in specific structural aspects of European financial and banking systems, and that analysing macroprudential aspects potentially affecting the stability of EU financial systems.

The Working Group on Developments in Banking, in addition to annually monitoring changes in national banking structures (size, capacity, etc.), has conducted studies on disintermediation, internationalisation and new technologies, among other areas. The Working Group on Macroprudential Analysis conducts regular analytical work on the soundness and stability of the banking industry in the EU, through the surveillance of macroprudential indicators based on aggregate data for national banking systems. It prepares two reports a year (in the spring and autumn) in this connection, and has also released specific reports, including most notably the analysis conducted in 2001 on the behaviour of provisions in relation to the business cycle.

The Task Force on Crisis Management was instituted in 2001. The other three groups, which address country risk, credit registers and early warning systems, were less active during the year.

As well as the four meetings of the BSC proper, the BE participated in 2001 in 34 meetings of the groups reporting to the BSC, 7 of which relating to the three least active groups.

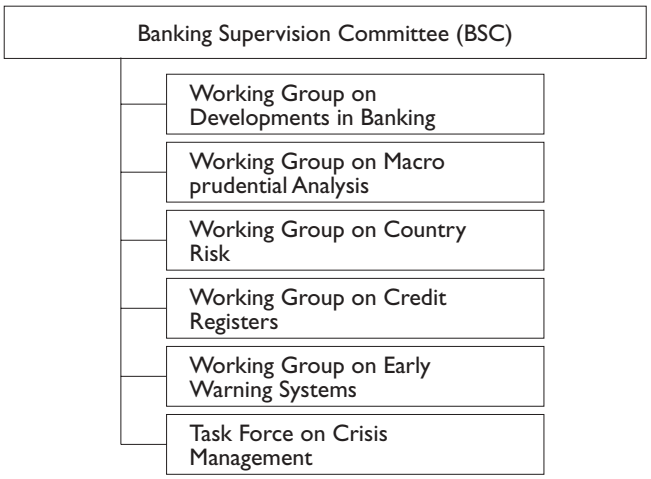
IV.1.4. Banco de España participation in the Groupe de Contact

The BE representative in the GdC has been chairing this group since 2000. As chairperson of the GdC this representative has also participated in the meetings of the BAC, the BSC and in other international fora. The BE participated in the 7 meetings held by this group in 2001.

The work of the GdC in 2001 focused particularly on developing the key elements for attaining the level of convergence needed for the future application of the so-called Pillar 2 of the new Basel Accord (supervisory review). Close co-operation was maintained with the EC and with the TSG, which is working on the application of this Pillar and its incorporation into a Community directive.

BOX IV.3

List of European Central Bank BSC groups



IV.1.5. Banco de España participation in the Basel Committee

The BE became a member of the BCBS on 1 February 2001. It has since participated in virtually all the working groups reporting to the BCBS. This decision has meant a considerable increase in the presence of BE representatives in international working groups. Testifying to this is the fact that, of the 212 banking supervision-related meetings in which the BE took part in 2001, almost half (85) were meetings of the BCBS or its working groups.

Currently, the work to which the BCBS is devoting most resources is the forging of a new Basel Capital Accord (Basel II), which involves a far-reaching revision of the 1988 Accord. This original agreement instituted a capital-measurement system needed to cover, essentially, credit risk, setting a ratio of 8 %. It has been progressively implemented not only in the BCBS member countries, but also in virtually all countries where international banks have an active presence.

The new proposals that will replace the 1988 Accord are based on three pillars. Pillar I refers to the minimum capital requirements to cover credit, market and operational risks. Pillar 2 is intended to give a bigger role to the supervisory review of risks and to entities' internal controls. Finally, Pillar 3 is based on market discipline, through the publication of the relevant information. To take decisions on the new Capital Accord, the BCBS created a high-level group called the Task Force on the Future of Capital Regulation. This group, in turn, set up 7 technical groups on various aspects of the new Accord: the review of the standardised approach and of credit risk mitigation techniques; the internal rating-based approach for credit risk; the treatment of operational risk; the treatment of securitisation; Pillar 3 or market discipline; an impact study of the proposals delivered; and finally, the overall calibration of the Accord (see Box IV.4).

Furthermore, the BCBS maintains both specific-end groups and standing groups, which are convened according to ongoing requirements and circumstances.

Notable among these is the Accounting Task Force, which was created by the BCBS in view of the importance of accounting and auditing for banking supervision. This group pays particular attention to accounting standards issued by the IASB and to auditing standards published by the International Federation of Accountants (IFAC), it has observers at both institutions and it participates actively in the drafting stage of such standards, offering its opinion on their potential

impact on CIs, and particularly on financial stability. This group also draws up the recommendations the BCBS publishes on what it considers sound auditing and accounting practices in banking. The treatment of loans and credit, including loan loss coverage, is a good example of this work. In 2001 the group devoted particular attention to the IASB proposal to value and disclose all financial instruments in the balance sheet at their fair value. In the end this proposal was not accepted, with the current mixed model being maintained with certain amendments to the current standards IAS 32 and 39 (on the accounting treatment of and information relative to financial instruments). The study of this matter will be the focus of much of the group's work in 2002.

Another important working group is the Core Principles Liaison Group, which seeks to disseminate the BCBS's work in order to promote best banking practices throughout the world and not only among its members. In this respect, the BCBS has always encouraged contact and co-operation between its members and other countries' supervisory authorities.

The BE has had an active presence in all the working groups reporting to the Task Force on the Future of Capital Regulation and in the other six working groups.

IV.1.6. Banco de España participation in other international working groups

In addition to the groups described above, which account – as stated – for the core work of its international activity in the supervisory area, the BE participated in 2001 in other working groups, including most notably the FMC of the OECD. Sitting on this body are representatives of the Directorate General Regulation and the Directorate General Economics, Statistics and Research. This group met three times in 2001 with BE participation.

There was also significant activity during the year in the central bank statisticians' group which reports to the BIS. The BE took part in three meetings of this group. The aim of the meetings has been to improve consolidated statistics, bearing in mind the new approach proposed by the Committee on the Global Financial System, which includes the ultimate obligor and derivatives.

IV.2. BILATERAL RELATIONS WITH OTHER SUPERVISORS

IV.2.1. Supervision of foreign credit institutions in Spain

As at 31 December 2001 there were 56 branches of foreign CIs in Spain, 48 of which were institutions of EU countries. The presence of subsidiaries of foreign CIs was also notable.

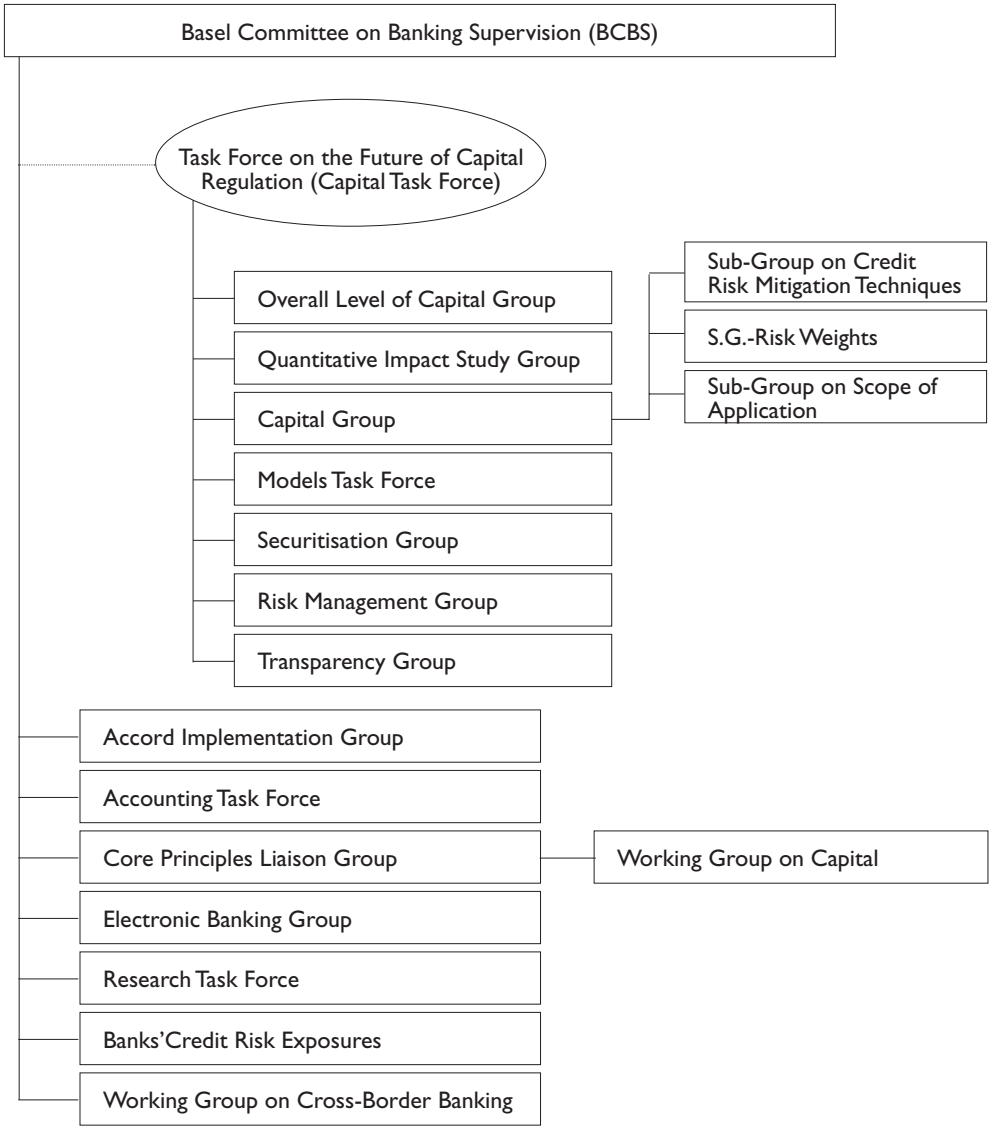
As the subsidiaries of foreign CIs are for legal purposes Spanish institutions, they are subject to supervision by the BE. Nonetheless, if the supervisor of the parent or the supervisor of the consolidated group wishes to conduct and examination of a subsidiary in Spain, the BE poses no obstacle. From a formal standpoint, the supervisor in question notifies the BE of its intention beforehand and, in many cases, a prior meeting is held. There may also be meetings after the examination to discuss the results.

Under *branches*, a distinction should be drawn between those of CIs belonging to the EES and those of other countries.

Following the adoption of the Second Banking Co-ordination Directive (2BCD) [Directive 89/647/EEC of 15 December 1989, now included in the Codified Banking Directive (Directive 2000/12/EC of 20 March 2000)] establishing the principle of mutual recognition, the opening of branches of EU institutions does not require prior authorisation in Spain, but

BOX IV.4

List of Basel Committee groups



communication to the BE by the competent authority in the home country, i.e. that in which the institution is incorporated. The 2BCD also established the principle that the supervision of branches is the responsibility of the home country, whereby examinations are conducted by the competent authorities of the home country, whether directly or via auditors. However, as regards the liquidity of such branches, the related competence is retained by the host country, i.e. that where the branch is established. As with subsidiaries, there will be prior notification from the home-country supervisors when it is intended to examine a branch in Spain and meetings with Spanish supervisors before the examination begins and after its completion.

The opening of branches of third countries is subject to prior authorisation in Spain. Such authorisation is the competence of the Ministry of Economy, following a prior report issued by the BE. Although branches are a part of a credit institution that is devoid of legal personality, the opening of branches of third countries is subject to most of the rules governing the authorisation of CIs. In this case the BE does have supervisory competence and conducts

examinations, albeit without standing in the way of examination by the authority under whose national jurisdiction the institution is incorporated.

IV.2.2. Co-operation protocols

The BE is signatory to seven bilateral co-operation protocols with EU countries where branches of some importance for either side are established. These protocols arose as the practical application of the supervisory, co-operation and reporting rules laid down in the 2BCD. Consequently, they were part of the implementation of the Directive, in principle, and as such their scope of application was branches.

The protocols specify how notifications should be made in the event of opening a branch, the content of the notification and co-operation in the supervision of liquidity and market risks, and they further determine the reporting requirements of the host-country supervisor. Likewise included is the communication and co-operation procedure to be followed by supervisors for conducting examinations in the host country, as described above. A communication procedure for the event of a crisis is also in place. Further, as envisaged in the protocols, meeting are held between the competent authorities signatory to each of the bilateral protocols. Apart from the monitoring of and exchange of information on branches and subsidiaries, these meetings address legislative changes bearing on institutions or changes in supervisory procedures.

Nonetheless, and despite the fact that the scope of application of the protocols is branches, they all mention the importance of collaborating in the monitoring of reciprocal subsidiaries and lay down general co-operation principles.

In addition to the protocols entered into with competent authorities of EU Member States, the BE is a signatory to seven other protocols of co-operation with the authorities of the Latin-American countries where the most important subsidiaries of Spanish banking groups are to be found.

On signing these protocols, the BE has sought to define the respective supervisory responsibilities and to ensure that the parent institution has at hand all the information it requires for the managerial control of its subsidiaries. Furthermore, they should allow the BE to perform its attendant supervisory functions on a consolidated basis.

Lastly, it is worth highlighting the international efforts to draft protocols that help bring about greater co-operation and co-ordination in the field of supervision. In the EU, the EC is authorised to negotiate and sign framework protocols on behalf of EU countries with third countries, which can then be used as a basis for the signing of bilateral protocols between these third countries and EU Member States. In this connection, the EC has signed a protocol of collaboration with the Federal Reserve and the OCC, two of the supervisory authorities in the United States.

The BCBS has also made an effort in this respect, drafting a protocol that may act as a model for the signing of protocols between different countries.

Finally, with the increasing proliferation of international groups, consideration is currently being given to the signing of multilateral protocols, like those seen already in the securities and insurance sectors under the aegis of FESCO (the Forum of European Securities Commissions) and of IAIS (International Association of Insurance Supervisors), respectively.

ANNEX I

BASIC REGULATORY STRUCTURE OF THE SPANISH BANKING SYSTEM

The dispersed regulatory framework to which the activity of credit institutions (CIs) is subject can be divided into three areas: taking up of the business of credit institutions, pursuit of such business and possible corrective measures (including those applicable in the event of crisis).

Before briefly discussing each of these areas, it should be pointed out that CIs are traditionally defined as undertakings whose business is to receive deposits or other repayable funds from the public and to grant credits or undertake similar transactions for their own account (1). What distinguishes them from other financial intermediaries is that deposit-taking is their exclusive preserve (while all financial intermediaries can issue securities under securities market regulatory and disciplinary rules) (2).

Credit institutions – commonly known as banking or deposit institutions – include banks, savings banks and credit co-operatives (3) which, notwithstanding their different commercial features, operate under a practically identical regime. Specialised credit institutions (SCIs) are also considered as CIs, although their more specialised credit activity may not be funded through deposit-taking (4).

Directives 2000/28/EC and 2000/46/EC of the European Parliament and of the Council, both of 18 September 2000, have recently extended the traditional definition of credit institution to a new type of financial institution, namely electronic money institutions, whose main activity is the issuance of means of payment in the form of electronic money. These Directives are pending transposition into Spanish law (5).

I. FRAMEWORK REGULATING THE TAKING UP OF THE BUSINESS OF CREDIT INSTITUTIONS

A quick look at our more recent past shows that the first relaxation of the prohibition on setting up banks, which had been in force in Spain from 1940 (period known as the "bank-

(1) Article 1(1) of Royal Legislative Decree 1298/1986 of 28 June 1986 on the adaptation of the law regulating credit institutions to Community law, which transposes the equivalent provision laid down in article 1(1) of Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions. This Directive, hereinafter the "Banking Directive", is a codification of several banking Directives, now repealed (73/183/EEC, 77/780/EEC, 89/299/EEC, 89/646/EEC, 89/647/EEC, 92/30/EEC, 92/121/EEC, together with their amendments).

(2) Article 28(2)*(b)* of Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions (LDI).

(3) The Official Credit Institute is also considered as a credit institution. However, as it is a State Finance Agency, it is regulated under a special regime.

(4) First additional provision to Law 3/1994 of 14 April 1994 and section 4 of the seventh additional provision of RDL 12/1995 of 28 December 1995.

(5) Part of the transposition is contained in the Bill on Reform of the Financial System *(Boletín del Congreso de los Diputados,* 8 March 2002).

ing *status quo"),* occurred in the 1960s, as part of the economic liberalisation that took place at that time. The first announcement of the liberalising course that was to be followed in subsequent years was Law 2/1962 of 14 April 1962 on credit and banking. Another significant step in this process was the nationalisation, in 1962, of the Banco de España (BE), which was made responsible for supervising private banks.

While the above-mentioned Credit and Banking Law distinguished between commercial and industrial banks, its subsequent implementing provisions tended to blur this distinction. This was clearly reflected in Decree 2246/1974 of 9 August 1974, the most direct antecedent of the current regulation on the establishment of banks. Under this provision, the setting up of a credit institution was subject to authorisation, but this was still granted only on a discretionary basis, applying the criterion of economic needs of the market.

Another major milestone in this liberalisation, since it fostered competition, was the entry of foreign banks into Spain in 1978, although their activity was subject to a restrictive structural and operational regime, which only began to become more flexible in 1986 when Spain joined the European Community.

Savings banks were naturally also affected by the reforms. Originally established as public or private charitable foundations, linked to the pawnbroking institutions created in Spain in the 18th century, their role as financial intermediaries was enhanced by the 1962 Credit and Banking Law and confirmed by subsequent developments. In 1971 they were placed under the supervision of the BE; in 1975 the creation of new savings banks was regulated (some of these provisions are still in force); and in 1977, they became subject to the same regulatory treatment, insofar as their operations are concerned, as banks. Moreover, regional governments gradually assumed powers over savings banks as well as over credit co-operatives, as laid down in the Spanish Constitution of 1978.

More recently, Spain's accession to what is now known as the European Union (EU) has determined the latest legislative changes in the conditions for taking up the business of credit institutions in our country.

First, the regulations on the establishment of credit institutions were adapted to the provisions of Council Directives 73/183/EEC of 28 June 1973 and 77/780/EEC of 12 December 1977. The former required the abolition of restrictions which prevented institutions from establishing a presence or providing services in other Member States under the same conditions as national institutions. The latter directive, known as the First Banking Co-ordination Directive (1BCD), established a single definition of credit institution and harmonised conditions for authorisation (separate own funds, two persons who effectively direct the business of the credit institution and who are of sufficiently good repute and have adequate experience, a programme of operations). The granting and possible revocation of authorisation were regulated, thus preventing the application of the "economic needs" criterion (6).

Subsequently, in 1994 and 1995 (7) Spanish law was adapted to Council Directive 89/646/EEC of 15 December 1989, known as the Second Banking Co-ordination Directive (2BCD),

(6) Part of these Directives having been transposed through Royal Legislative Decree 1298/1986 of 28 June 1986, in 1987 the conditions for the taking up of the business of credit institutions were incorporated into the various regulations on the establishment of each type of entities then in force, harmonising the authorisation process for national and foreign banks. Notwithstanding, under the transitory regime provided for Spain in the Annex to the 1BCD, the criterion of economic need could be applied until 31 December 1992.

(7) Law 3/1994 of 4 April 1994 adapting Spanish law on credit institutions to the 2BCD and introducing other changes in the financial system, and Royal Decree 1245/1995 of 14 July 1995 on the establishment of banks, cross-border activities and other issues relating to the legal regime of credit institutions.

which extended the harmonised conditions for authorisation (initial capital of € 5 million and suitability of shareholders that have qualifying holdings) and established the principle of a single licence or passport to operate throughout the Community. The 2BCD also regulated the taking up of the business of credit institutions through the acquisition of qualifying holdings.

The description of the regulatory process which has led to the current legislation on the taking up of the business of credit institutions shall now be followed by a short analysis of the current provisions regulating the establishment of the various types of CIs in the Spanish banking system, the control procedures applicable to shareholding changes and the regulation of cross-border activities.

1.1. Establishment of new institutions

Banks

Under the relevant provisions of Royal Decree 1245/1995 of 14 July 1995, based on article 43 of Law 26/1988 of 29 July 1988 on the discipline and intervention of credit institutions (LDI) (8) the establishment of Spanish banks is subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE. The Royal Decree defines the procedure to be followed and the conditions to be complied with to obtain and retain authorisation to operate as a bank (see Box A.I.1).

BOX A.I.1

Requeriments for the establishment of new credit institutions

Banks: the establishment of new Spanish banks, as well the merger of existing ones, is subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE, under the following conditions:

Corporate conditions
— Public limited company incorporated through the simultaneous formation procedure.
— Initial capital: € 18 million.
— Corporate purpose limited to the specific activities of credit institutions.
— No special advantages or remuneration to founders.
— Registered office and effective management of business within national territory.

Viability of business project
Administration and general management
— Board of Directors composed of at least five members.
— Professional reputation (as specifically required).

Organisation
— Good administrative and accounting organisation.
— Adequate internal control procedures to ensure sound and prudent management.

Shareholders
— Suitability of shareholders possessing qualifying holdings (5 % or more of capital or voting rights).

Membership of Deposit Guarantee Fund

Savings banks: both State law and provisions issued by regional governments that have assumed powers over the establishment or merger of savings banks with registered office within their territory set out requirements similar to those listed above, with the exception of the shareholder structure (there are no shareholders in savings banks which are foundations).

Credit co-operatives: State law and regional provisions are based on substantive criteria similar to those listed above, although lower and different initial capital requirements are applied, depending on the territory within which these banks propose to operate. Power to grant authorisation is vested in the competent regional body when the credit co-operative intends to be established within the territory of the region concerned or will have its registered office there as the result of a merger.

Specialised credit institutions: substantive conditions and procedures relating to the establishment or merger of specialised credit institutions are very similar to those applicable to banks, although with lower initial capital requirements, owing to their more specialised corporate purpose.

The monitoring of shareholders with qualifying holdings in a credit institution is not limited to the establishment of the institution, but extends to all the successive changes in the shareholder structure that take place over the whole life of the entity.

(8) As amended by Law 3/1994 of 14 April 1994.

Shareholder suitability is assessed on the basis of several factors, such as reputation, the possession of adequate assets to fulfil obligations, the institution's exposure to non-financial activities of the proposed shareholders, transparency of group structure, as well as the existence of any "close links" that may prevent the effective exercise of supervision (9).

European Community criteria are tightened under Spanish law inasmuch as Spanish law requires a higher number of persons to effectively direct the business, requires a higher amount of initial capital, sets a lower threshold for the level of shareholdings to be subject to monitoring, and introduces additional factors to assess suitability (adequate assets and involvement in non-financial activities).

When a new bank is to be controlled by a natural or legal person authorised in another EU Member State, before issuing its opinion the BE shall consult the supervisory authorities concerned. When it is to be controlled by a natural or legal person established or authorised outside the EU, the applicant may be required to provide additional guarantees and authorisation may be suspended, refused or limited if EU credit institutions are not granted comparable treatment in respect of competitive opportunities or effective market access in the applicant's home country.

In order to reinforce the initial stability of new banks, Spanish law, unlike Community law, lays down certain periods during which their activities are subject to restrictions. Specifically, during the first three years they shall not distribute dividends and during the first five years they shall not extend credit to shareholders, directors or senior officials (or related companies), nor shall any non-financial corporation (or group) hold, directly or indirectly, more than 20 % of the capital or a controlling interest in the bank.

Finally, mergers between banks are also subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE (10).

Savings banks

The establishment of savings banks is regulated by RD 1838/1975 of 3 July 1975, subsequently adapted to reflect Community law, with the exception of conditions applicable to the shareholder structure, since savings banks have no shareholders. The provisions laid down in the aforementioned Royal Decree are similar to those for banks in respect of initial capital, programme of operations, management and effective direction of business within the national territory, etc. Both establishment and merger are subject to authorisation by the Minister of Economy, on the basis of an opinion from the BE.

Nevertheless, having regard to the distribution of powers laid down in the Spanish Constitution, to Law 31/1985 of 2 August 1985 on the regulation of the basic rules relating to the governing bodies of savings banks, and to the construction criteria of the Constitutional Court (11), regional governments have assumed extensive powers over savings banks established within their territory. Under these powers, which are laid down in their respective statutes of autonomy, regional governments have issued a wide range of provisions. Specifically, the establishment or merger of savings banks that have or propose to have their head office within their territory are subject to authorisation by the regional Department of Economy or similar authority.

(9) This last criterion was laid down in Directive 95/26/EC (known as the "Post-BCCI Directive"), amending the 1BCD, and was incorporated into Spanish law through the first additional provision to Royal Decree 692/1996 of 26 April 1996.

(10) Article 45*(c)* of the Banking Law of 31 December 1946.

(11) In particular, judgments of the Constitutional Court 48 and 49/1988 of 22 March 1988.

As a result, a complete description of the conditions for the establishment or merger of savings banks would need to take into account the detail of the above-mentioned regional provisions, which goes beyond the objective of this report. However, it should be noted that, whatever the competent authority may be, the Constitutional Court has resolved that authorisation shall in all cases require a prior opinion from the BE (12).

Credit co-operatives

At the State level, the legal regime for this type of credit institution, including establishment or merger conditions, is regulated by Law 13/1989 of 26 May 1989, implemented by RD 84/1993 of 22 January 1993. To these provisions should be added those that may be issued by regional governments that have assumed powers in this field, as well as the general law on co-operatives (13), which is applicable when higher-level sectoral regulations do not apply.

This regulation incorporates the conditions for the taking up of the business and the reasons for refusing authorisation, which are similar to those applicable to banks, with the exception of a number of features derived from their corporate regime. Specifically, credit co-operatives are subject to lower initial capital requirements which, within the limits established by Community law, differ according to the territory within which they intend to operate and to the total number of inhabitants of the municipalities included in such territory.

Regional governments have also assumed powers over credit co-operatives within the framework of State law, although to a lesser extent than with savings banks. However, the establishment or merger of credit co-operatives is subject to authorisation by the Minister of Economy, except when the proposed establishment or merger is limited to the regional territory (14).

Specialised credit institutions

Legally provided for since 1994, and successors to the former *entidades de crédito de ámbito operativo limitado,* specialised credit institutions are regulated by RD 692/1996 of 26 April 1996 as far as their establishment and merger are concerned.

The above-mentioned Royal Decree lays down substantive conditions and procedures on the taking up of business, which are very similar to those applicable to banks, including consultation of the supervisory authority of the home country when the institution is to be controlled by legal or natural persons established in another EU Member State. However, these companies are subject to lower initial capital requirements, owing to their more specialised corporate purpose (which is limited to the performance of several types of credit operations, the management or issuance of credit cards and the provision of guarantees) and to the fact that they are not allowed to receive deposits from the public.

1.2. Qualifying holdings

As mentioned above, the suitability of shareholders is not only assessed at the time of the establishment of a credit institution but also whenever any change is made in the shareholder

(12) Judgments of the Constitutional Court 1/1982 and 48/1988.

(13) Law 27/1999 of 16 July 1999 on co-operative banks and relevant regional provisions.

(14) Judgments of the Constitutional Court 134/1992 of 5 October 1992 and 275/2000 of 16 November 2000 on the distribution of powers.

structure of already authorised entities. Although there were legal precedents for the monitoring of suitability, the provisions now in force, which date back to 1994 and are laid down in Title VI of the LDI and article 18 of RD 1245/1995 of 14 July 1995, are in line with Community law.

These provisions are based on the definition of qualifying holding, i.e. a direct or indirect holding in an undertaking which represents 5 % or more of the capital or of the voting rights (quantitative criterion) or which, even if falling below this proportion, makes it possible to exercise a significant influence over the undertaking (qualitative criterion). It is assumed that a significant influence is exercised when the holding allows for the appointment or removal of a member of the credit institution's board of directors.

Any natural or legal person who proposes to acquire a qualifying holding or to increase the proportion of an existing holding shall be required to inform the BE, in particular if, as a result of the acquisition, the institution would become subject to the control of the acquirer.

The BE shall have a maximum of three months from the date of the notification to oppose such a plan, if it is not satisfied as to the suitability of the acquirer assessed in the light of the conditions described in section 1.1 above. If as a result of the acquisition the credit institution would become subject to the control of a legal or natural person authorised in another EU Member State, prior consultation with the supervisory authorities of the home Member State is required. If control would be exercised by a legal or natural person established outside the EU, the acquisition could be subject to limitations, suspension or refusal.

Failure to comply with the obligation to provide prior information, or the acquisition of holdings before the BE has taken a decision or despite its opposition, may result in sanctions and the suspension of the exercise of the voting rights attaching to the improperly acquired shares.

Credit institutions shall inform the BE on becoming aware of any transfers of holdings in their capital that exceed 1 % of the same. They shall also report their shareholder structure to the BE on a regular basis.

1.3. Cross-border activities

Cross-border activities covering both foreign credit institutions operating in Spain and Spanish credit institutions operating abroad are regulated in Chapters I and II, Title V, of LDI, implemented by Title II of RD 1245/1995 of 14 July 1995.

1.3.1. Activities of foreign credit institutions in Spain

Credit institutions authorised in another EU Member State

Under Community law, the authorities of an EU Member State may not prevent credit institutions authorised in another Member State from operating within their territory. This principle of single license, or Community passport, is based on the existence of harmonised conditions required to obtain authorisation and pursue the business of credit institutions (basically relating to the supervision of their solvency on a consolidated basis by the authorities of the home country).

The activities subject to mutual recognition are listed in Box A.I.2 and constitute the core banking business which corresponds to the principle of universal banking. The sole significant exception is that CIs are not allowed to engage directly in insurance activities.

BOX A.1.2

Activities subject to mutual recognition

- Acceptance of repayable funds from the public.
- Lending.
- Factoring and financial leasing.
- Payment transactions, payment services and transfers.
- Issuing and administering means of payment (e.g. credit cards, travellers' cheques and bankers' drafts).
- Guarantees and similar commitments.
- Intermediation on interbank markets.
- Trading for own account or for account of customers in transferable securities and financial instruments.
- Participation in securities issues and intermediation for own account or for account of the issuer in the placement and underwriting of such issues.
- Advice and services to undertakings on capital structure, industrial strategy, mergers and acquisitions and related matters.
- Portfolio management and advice.
- Safekeeping of securities evidenced by physical documents and administration of securities evidenced by book entries.
- Credit reference services.
- Safe custody services.

On receipt by the BE of a communication from the supervisory authority of the home Member State with the relevant information, EU credit institutions may commence the above-mentioned activities in Spain.

Credit institutions not authorised in another EU Member State

As these CIs do not benefit from Community harmonisation, the establishment of branches of such institutions in Spain is subject to authorisation according to the same procedure as that applicable to the establishment of new Spanish banks, with certain differences derived from the fact that the branches do not have an independent legal status. In this case, authorisation may be refused not only as a result of failure to comply with the prescribed conditions but also on the basis of the principle of reciprocity.

Representative offices

This category, which is not regulated under Community law, includes representative offices of foreign credit institutions, whatever their nationality, operating in Spain. Their activities are restricted to the provision of information and to marketing in the banking, financial or economic areas and their establishment is subject to authorisation by the BE.

1.3.2. Activities of Spanish credit institutions abroad

Activities in another EU Member State

In accordance with the single licence principle, whenever the BE is notified that a Spanish credit institution proposes to establish a branch or to exercise the freedom to provide services

within the territory of another EU Member State, the BE shall communicate that information to the supervisory authority of the host Member State.

This notwithstanding, the BE may oppose the establishment of the proposed branch if the programme of operations presented includes activities that the credit institution is not authorised to undertake or if the BE has reason to doubt the adequacy of the administrative structure or the financial situation of the credit institution, taking into account the activities envisaged.

Whenever a Spanish credit institution intends to establish a subsidiary or acquire a qualifying holding or a controlling interest in an EU entity, the host Member State shall apply the relevant harmonised provisions, which are equivalent to those laid down in Spanish regulations, after consulting the BE in its capacity as home supervisory authority.

Activities in a non-EU Member State

Without prejudice to the requirements to be fulfilled in the host country, the establishment of branches is subject to authorisation by the BE under the same conditions as discussed above. The BE may oppose such plan if it considers that the branch shall not be subject to effective control by the supervisory authority of the host country or if there are legal or other impediments preventing or hindering its supervision. As regards freedom to provide services, credit institutions are only required to inform the BE of their intention.

The creation of a subsidiary or the acquisition of a holding in an existing credit institution are subject to authorisation by the BE. Such authorisation may be refused if it is considered that, in the light of the financial situation of the institution or its management capacity, the plan may adversely affect the credit institution, the effective supervision of the group may not be ensured or the activity of the controlled institution is not subject to effective control by the national supervisory authority.

2. REQUIREMENTS FOR THE PURSUIT OF THE BUSINESS OF CREDIT INSTITUTIONS

2.1. Reserve requirements

Until 31 December 1998 the definition and implementation of monetary policy fell within the competence of the BE. This task included the possibility of requiring CIs to hold minimum reserves calculated as a percentage of reimbursable funds, which could vary in scope and amount and was called the cash ratio.

Since 1 January 1999, the date on which Spain adopted the single currency in Stage Three of Economic and Monetary Union, this function has been assumed by the European System of Central Banks (ESCB), as provided for in the Treaty establishing the European Community (15) and the Statute of the ESCB and of the European Central Bank (ECB) (16).

The regulations concerning the minimum reserve system now in force were issued pursuant to article 19 of the Statute. Under these regulations, CIs are required to hold minimum

(15) Articles 105 and following of the consolidated version of the Treaty establishing the European Community.
(16) Protocol annexed to the Treaty on European Union.

reserves in reserve accounts with the national central banks of the countries where they are established. Therefore, the required percentage of funds accepted by CIs in each Member State shall be held in accounts with the respective national central banks.

Council Regulation (EC) No 2531/98 of 23 November 1998 (17) established the basis for minimum reserves (which mainly include liabilities of the institution resulting from the acceptance of funds and from off-balance-sheet items), the reserve ratios (which shall not exceed 10 %, though different reserve ratios may be set for specific categories of liabilities) and the sanctions which may be imposed in cases of non-compliance with reserve requirements (18).

Regulation (EC) No 2818/98 of the European Central Bank of 1 December 1998 specified the institutions subject to reserve requirements, the liabilities included in the reserve base (deposits, debt securities issued by the institution and money market paper), the reserve ratio (0 % for specified transactions with maturity over two years and 2 % for all other liabilities included in the reserve base), the allowance to be deducted from the amount of each institution's reserve requirements (€ 100,000), the maintenance period and the remuneration on such holdings. The Regulation permitted, under certain conditions, the indirect holding of minimum reserves through an intermediary also subject to the same requirements.

2.2. Solvency ratio

2.2.1. Historical background and current regulations

The first Spanish regulations in this field, issued in 1962, established the so-called "guarantee ratio", whereby individual institutions were required to maintain own funds in excess of a given percentage of their borrowed funds. However, the concept of own funds was rather imprecise, and different definitions applied to different institutions. Moreover, the ratio did not cover the whole amount and range of risks incurred and it ignored the existence of financial groups.

Substantial progress was achieved with Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting requirements for financial intermediaries, and its implementing provisions, which embodied the main lines of the regulations in force. These provisions extended the definition of own funds to include subordinated debt (19), introduced a risk weighting system with differing ratios according to the various types of assets and commitments, and imposed the same requirements on all CIs, which were also required to ensure compliance on a consolidated basis.

The following step was the full adaptation of regulations to the Community solvency Directives adopted since 1989 (20), which set out the basic common standards to be transposed to national legislation, although more stringent provisions than those laid down in these Directives may be applied to national CIs.

(17) Recently amended by Council Regulation (EC) No 134/2002 of 22 January 2002, which extended to two months the period for the ECB Governing Council to take a decision on the review procedure for the imposition of sanctions.

(18) The infringement procedure is described in section 3.1 of this Annex.

(19) From a legal viewpoint, subordinated debt ranks after unsecured credits in the assignment of loans on a priority basis [article 20(1)(g) of Royal Decree 1343/1992 of 6 November 1992].

(20) Council Directive 89/299/EEC of 17 April 1989 on the own funds of credit institutions, Council Directive 89/647/EEC of 18 December 1989 on a solvency ratio for credit institutions, Council Directive 92/30/EEC of 6 April 1992 on the supervision of credit institutions on a consolidated basis, Council Directive 92/121/EEC of 21 December 1992 on the monitoring and control of large exposures of credit institutions (incorporated into the Banking Directive) and Council Directive 93/6/EEC of 15 March 1993 on the capital adequacy of investment firms and credit institutions.

The current regulatory framework is based on Law 13/1992 of 1 June 1992 on the own funds and the supervision of financial institutions on a consolidated basis, which amended Law 13/1985 in respect of CIs and also dealt with the parallel regime applicable to securities firms, insurance companies and groups incorporating both. As far as CIs are concerned, the Law was implemented by lower-level provisions (21) down to the level of detail established by the Banco de España Circular CBE 5/1993 of 26 March 1993 on the calculation and control of minimum own funds, issued pursuant to the powers conferred on the BE under higher-level comprehensive regulations.

2.2.2. Scope of application. Consolidated institutions and consolidated groups of credit institutions

The regulations apply to consolidated groups and subgroups of CIs, as well as to individual institutions not included in a group. The provisions do not apply to the Spanish branches of credit institutions authorised by other EU Member States since prudential supervision is entrusted to the home country. The regulations do apply to Spanish branches of non-EU credit institutions, although they may be exempted if they fulfil specific requirements.

In order to ensure the adequate distribution of risks within the group, Spanish regulations incorporate individual capital requirements for subsidiaries included in a consolidated group or subgroup. However, these requirements may be less stringent than the consolidated ones, depending on the parent company's participating interest.

The regulations address the scope of consolidation (22) from a two-fold perspective: activity and degree of control. With respect to activity, all types of intermediaries usually undertaking financial activities (with the exception of insurance companies), as well as special purpose vehicles, whose activity is an extension of the business of a financial institution or consists of providing ancillary services to the group, are eligible for consolidation. As regards control, the regulations refer to article 4 of Law 24/1988 of 28 July 1988 on the Securities Market (LSM), which established the principle of the management unit determining the origin of consolidation, it being understood that these circumstances occur when the prerequisites set out in mercantile regulations (23) are fulfilled or when the majority of the directors of the controlled institution are senior managers of the controlling institution or of other entities controlled by the latter.

As for the structure of consolidated groups and subgroups of credit institutions (CGs), Spanish law, in line with Community law, refers to vertical consolidation (where the group parent company is a Spanish credit institution or a Spanish company holding shares or other equity in CIs), though it goes further than this, dealing also with cases in which the parent company is a Spanish non-financial holding company and other cases of "horizontal" consolidation (groups with a non-consolidated parent company).

Although only rules applicable to CGs or to individual CIs are discussed herein, it should be pointed out that these CIs may be incorporated into groups whose parent company is an investment firm or a holding company basically oriented towards securities (in which case there will be a consolidated group of investment firms) or into groups which include non-credit financial institutions (called other consolidated groups of financial institutions). All these cases

(21) Royal Decree 1343/1992 of 6 November 1992 and Ministerial Order of 30 December 1992.

(22) The consolidation procedures are described in detail in provisions 18 to 22 of CBE 4/1991 of 14 June 1991 on CI accounting.

(23) Article 42(1) of the Commercial Code.

are subject to specific more stringent rules, which encompass not only the solvency requirements applicable to the CIs included in the group but also the specific requirements imposed upon the other financial institutions of the group.

Finally, both Community and Spanish law exclude the consolidation of insurance companies with CIs or investment firms. However, under Spanish law, groups including such companies – non-consolidated mixed groups of financial institutions – are required to apply a net aggregation system to the own funds and solvency requirements of the institutions or consolidated groups included in the aforementioned groups, in accordance with the requirements laid down in their own regulations, subject to certain adjustments (24).

2.2.3. Own funds

Broadly in line with Community law, Spanish regulations distinguish between two types of funds, tier 1 and tier 2 funds, according to the extent to which they fulfil the typical functions of capital (capacity to absorb losses and indefinite availability to the institution). A series of items are deducted from these funds in order to ensure that they are used within the scope of the above-mentioned functions, to avoid double counting of own funds and to reduce the risk of contagion from other non-financial activities.

Box A.1.3. enumerates the eligible own funds for the calculation of the solvency ratio of an individual credit institution, as well as the main deductions applicable.

In a CG, consolidation reserves and paid-up minority interests in subsidiaries are also included, while consolidated goodwill is deducted. Moreover, special eligibility conditions are set for preference shares and subordinated debt issued by foreign subsidiaries.

For the final calculation of eligible own funds, the following two relative limits, aimed at ensuring the quality of CI or CG own funds, shall be applied: tier 2 capital shall not exceed tier 1 capital, and lower quality subordinated debt shall not exceed one half of tier 1 capital.

2.2.4. Capital requirements

Pursuant to the general principle of solvency regulations, institutions are required to hold a sufficient amount of eligible own funds to cover the sum of the requirements arising from each type of risk incurred in the pursuit of their business. Broadly in line with Community law, the risks to be covered, as well as their measurement method and minimum coverage requirements are as follows:

Credit risk

Credit risk is the risk that the counterparty will fail to fulfil its obligations to the institution in due time and form. As a general rule, credit institutions are required permanently to maintain at 8 % the ratio of capital to assets and off-balance-sheet items to which weightings have been allocated according to their risk level. Three basic types of weightings are applied:

(24) In addition to individual credit institutions, the BE has supervisory powers over consolidated groups and subgroups of credit institutions, consolidated groups of financial institutions and non-consolidated mixed groups when the parent company is a credit institution or when supervisory powers are attributed to the BE by the Minister of Economy.

BOX A.1.3

Banking solvency regulations

In line with international, and in particular EU, practices and regulations, the basic principle of Spanish banking solvency regulations issued since 1985 has been that CGs and individual CIs which do not belong to a group should permanently hold sufficient own funds to cover risks incurred in the pursuit of their business.

Eligible own funds for the coverage of risks and deductions applicable to individual CIs are listed below. A number of items (e.g. consolidation reserves, minority interests in subsidiaries, etc.) should be added in the case of CGs.

Tier 1 capital

— Paid-up capital, participating interests in savings banks and endowment capital of branches of non-EU foreign institutions.
— Disclosed reserves (self-generating, share premia, reserve fund for participating interests). Profit for the financial year brought forward.
— Fund for general banking risks.

Deductions

— Losses of the previous and current financial years. Intangible assets.
— Own shares and transactions or commitments on such shares.
— Claims on third parties for the purchase of own shares and on corporate staff when individually in excess of € 30,000.
— Shares held by non-consolidated subsidiaries up to the amount of financing received from the parent company or guaranteed by the latter.

Tier 2 capital

— Asset revaluation reserves and reserves arising from mergers.
— Welfare funds in the form of real estate (only savings banks and credit co-operatives).
— Non-voting shares.
— Subordinated debt of indeterminate duration, whose principal is used to absorb losses, leaving the CI in a position to continue trading.
— Other subordinated debt with a maturity of at least five years.

Other deductions

— Qualifying holdings in CIs or financial institutions and other venture capital issued by these institutions.
— Other holdings or venture capital in financial institutions, when they exceed 10 % of the own funds of the holding company.
— Excess qualifying holdings in non-financial corporations.
— Shortfall in specific provisions.
— Other risk assets that the institution may decide to deduct.

Moreover, for the final calculation of eligible own funds, the two following relative limits shall be applied: tier 2 capital shall not exceed tier 1 capital, and lower quality subordinated debt shall not exceed one half of tier 1 capital. Likewise, tier 1 capital shall predominantly be made up of capital and reserves, which limits the eligibility of preference shares.

Risks which should be covered are basically the following:

— Credit risk on asset and off-balance-sheet items or commitments and derivatives, defined as the risk that the counterparty will not fulfil its obligations to the institution in due time and form.
— Foreign-exchange risk on foreign-exchange positions, i.e. the possibility of losses arising from movements in exchange rates.
— Market risk on the trading book (the most recently included), i.e. the possibility of losses in securities and other positions taken by institutions with the intention of benefiting in the short term from interest rate or price movements.

As a general rule, credit institutions are required to maintain permanently a ratio of 8 % of risk-weighted items, according to weighting rules established by law.

If this requirement is not satisfied, apart from the disciplinary actions which may be taken and from the obligation to prepare and implement a programme ensuring return to compliance, the distribution of profits to shareholders will be restricted or prohibited, depending on the shortfall in coverage.

Furthermore, there are certain limits on risks relating, on the one hand, to tangible assets and positions in a single currency (neither being envisaged in Community law) and, on the other, to qualifying holdings in non-financial corporations and large exposures, the latter in order to avoid undesirable concentrations in a single institution or group in excess of 25 % of own funds (20 % in the case of exposure to the institution's own group).

a) Asset items are risk-weighted taking into account the nature of the debtor according, inter alia, to the economic sector to which it belongs and to the collateral securing the assets.

In relation to economic sector, debtors are divided into three main groups: central government (zero weighting), CIs (20 % weighting) and private sector (100 % weighting). As far as collateral is concerned, asset items carrying explicit guarantees are subject to the weighting attributed to the ultimate obligor or guarantor, if this is more favourable than the weighting attributed to the direct obligor. As for other guarantees, which are described in detail in the regulations, differing weightings are applied according to the type of collateral provided (asset items secured by collateral in the form of securities are subject to, with slight differences, the weighting assigned to the issuer, whereas a 50 % weighting is applied to loans secured by mortgages on residential property.

RD 1419/2001 of 17 December 2001 extended to securities issued by local authorities the regime applying to government debt in respect of the solvency ratio level (zero weighting) and large exposures.

b) Off-balance-sheet items and commitments incorporate credit risk to the extent that they may give rise to a cash disbursement by the institution. This risk is measured in two steps: first, the item is multiplied by a reducing ratio (0 %, 20 %, 50 % or no reduction) measuring the probability that this disbursement may take place; second, the value obtained is weighted according to the weighting allocated to the counterparty, as set out for asset items.

Both off-balance-sheet and asset items are calculated at book value net of specific provisions.

c) Specific criteria are established for transactions that do not incur direct credit risk but do give rise to the risk that the counterparty may not meet the terms of contracts that would yield profits to the institution. This may occur with transactions on interest rates or exchange rates (swaps, options, etc.), with the exception of those traded on organised markets, under certain conditions. Here again, the risk is measured in two steps: first, the principal amount is multiplied by a percentage measuring the current and future replacement cost of the transaction; second, the value obtained is multiplied by the weighting allocated to the counterparty, the maximum weighting being 50 %, even for the non-financial private sector.

Foreign-exchange risk on positions in currencies

Credit institutions are required to hedge with own funds 8 % of their overall net position in currencies to cover possible losses arising from exchange rate movements in their open positions in each currency. The net position in a currency is the difference between assets (including accrued income and purchase commitments) and liabilities (including accrued costs and sale commitments). The net overall position in currencies is the higher of the total equivalent value in national currency of net long positions and of net short positions.

Market risk in the trading book

CIs and CGs with a trading book are required to hold capital against market risk, the latest risk to be included in solvency regulations (25). According to the definition set out in

(25) As laid down in Directive 93/6/EEC. Although transposition was not required until 31 December 1995, the content of this Directive was incorporated into Spanish law in 1993 in respect of investment firms and in 1994 in respect of CIs and CGs.

accounting regulations (26), the trading book includes, as a rule, debt instruments and equities and derivatives which are held or taken on by the institution with the intention of benefiting in the short term from price or interest rate movements.

Market risk and its capital coverage are determined, according to the standardised approach laid down in Community law, on the basis of the calculations and weightings applicable to price risk on positions in the various instruments, settlement/delivery risk, credit risk and counterparty risk arising from the trading book.

Recently, RD 1419/2001 of 17 December 2001 (27) extended the definition of trading book to include positions in gold, treated in a similar fashion to foreign-exchange positions, and allowed institutions to develop their own risk-management internal models for the calculation of capital requirements for market risk and foreign-exchange risk, subject to authorisation by the BE. The implementing Banco de España Circular has not yet been issued.

2.2.5. Limits on exposures

There are four prudential limits on exposures of which the first two are not included in Community law:

— Limit on net tangible fixed assets, which may not exceed 70 % of own funds.

— Limit on positions in a foreign currency, which may not exceed 5 % of own funds, unless authorised by the BE. This limit is applicable at the individual unconsolidated level.

— Limits on qualifying holdings in non-financial corporations, in line with Community law. A qualifying holding is a holding which represents 10 % or more of the capital or which makes it possible to exercise a significant influence over the management of the undertaking. The higher of the two following amounts shall be deducted from own funds: the total amount of qualifying holdings in excess of 60 % of own funds or the individual amount of each qualifying holding in a single undertaking or group in excess of 15 % of own funds.

— Limits on large exposures, also in line with Community law (28). A large exposure is an exposure incurred to a single client or group of connected clients (including the credit institution's own group in respect of the unconsolidated portion) the value of which exceeds 10 % of own funds. Subject to full or partial exemptions for given risks, two limits are set: individual exposure to a single client or group of connected clients shall not exceed 25 % of own funds (20 % for exposures to the credit institution's own non-consolidated group) and total large exposures shall not exceed 800 % of own funds.

2.2.6. Consequences of non-compliance with solvency regulations

In addition to the obligation to inform the BE of any non-compliance, and present a specific programme ensuring return to compliance, and regardless of possible sanctions, credit

(26) Rule 8 of Banco de España Circular 4/1991 of 1 June 1991.

(27) Transposition of Directive 98/31/EC of 22 June 1998 amending Directive 93/6/EEC of 15 March 1993.

(28) Article 49 of the Banking Directive. In line with Commission Recommendation 87/62/EEC, Spanish law had established earlier a 40 % limit on own funds for exposures to a single client or group of connected clients. This limit remained effective until 31 December 1993.

institutions' freedom is automatically restricted in two aspects: profit distribution is affected insofar as, if the shortfall in eligible own funds exceeds 20 % of minimum requirements, individual or consolidated credit institutions shall be required to assign total profits or net surplus to reserves. If the shortfall falls below the above-mentioned percentage, at least 50 % (or more, if required by the BE) shall be allocated to reserves (29). Furthermore, the establishment of new offices shall be subject to authorisation by the BE or, where appropriate, by the regional government, on the basis of an opinion from the BE.

2.3. Accounting

In Spain, the power to establish accounting standards and rules and financial statement formats for CIs and CGs is vested in the Ministry of Economy and Finance, which has delegated this responsibility to the BE (30). The accounting rules laid down in the Commercial Code, the Companies Act and specific regulations applicable to CIs are implemented and adapted to CIs by BE provisions.

Specifically, CBE 4/1991 of 14 June 1991 on accounting rules and financial statement formats, updated and amended by subsequent circulars, is the accounting framework for CIs and CGs and for branches of foreign CIs operating in Spain. All matters which are not explicitly included in the aforesaid Circular shall be regulated by the General Chart of Accounts and its implementing provisions and the Regulations on the Presentation of Consolidated Annual Accounts.

CIs and CGs are required by the BE to present two types of financial statements:

— Public financial statements: with information to third parties on the economic and financial position of the institution.

— Confidential financial statements: with more detailed information to be reported to the BE. This information shall be used for supervisory purposes and for the compilation of monetary, financial or economic statistics.

Since statistical data are necessary for the fulfilment of the tasks entrusted to the ECB, in particular the conduct of monetary policy, CIs are required to provide specific financial information permitting the ECB to draw up on a regular basis an aggregated balance sheet for euro area financial intermediaries as a whole.

The accounting principles and rules on which CI and CG financial statements are based have traditionally been aimed not only at providing information to third parties, like the statements of any other firm, but also at supplying the BE with extensive information on their financial position and at restricting transactions which may increase solvency or liquidity risk. For this reason, the principle of prudence shall prevail in the event of conflict between specific regulations or of lack of such regulations.

Finally, CI financial statements shall be drawn up on a consistent basis so that monetary authorities may obtain aggregate data allowing the adequate conduct of monetary policy and the compilation of statistics.

(29) In the case of savings banks, which are always required to assign 50 % of profits to reserves, the allocation of this or a higher percentage is subject to possible investments or charitable activities that may be exceptionally authorised by the Minister of Economy, as laid down in article 11 of Law 13/1985 of 25 May 1985.

(30) Article 48(1) of the LDI and Ministerial Order of 31 March 1989.

In its definition of general accounting principles for CIs and CGs, the BE considers that the purpose of the balance sheet, profit and loss account, annual report and other supplementary financial statements is to provide a true and fair view of the credit institution in respect of its financial position, results and exposures.

The achievement of this objective and the application of accounting standards or rules should be based on the following *accounting principles: prudence, historic cost, accrual, consistency, recording and no on- or off-balance sheet netting.*

Given the operational peculiarities of CIs and CGs, CBE 4/1991 deals extensively with certain accounting treatments, particularly in relation to credit risk, trading book, mobilisation of financial assets and derivatives.

Credit risk is addressed both as regards solvency risk and country risk.

As far as solvency risk is concerned, three types of provisions are required depending on the condition of the debtor:

a) A general provision amounting to 1 % of credit risks (0,5 % for certain types of risks) shall be set up.

b) Specific provisions must be made for loans which have been classified as doubtful, with the objective of covering the potential losses arising from the transaction or the client. These provisions depend on the sector to which the debtor belongs, the length of time that the loan has been considered doubtful and existing collateral.

c) Statistical loan loss provisions, whose amount may be estimated according to the standardised model proposed in CBE 4/1991 or to internal models developed by institutions subject to authorisation by the BE, shall be set aside to cover transactions which have not yet been specifically identified as doubtful assets but in which experience shows that this risk may exist. This type of coverage started to be applied on 1 July 2000, date of entry into force of CBE 9/1999 of 17 December 1999 under which it was established (31).

As for country risk, i.e. the risk arising from total claims on a single country other than business risk, under CBE 4/1991 countries are classified into six categories or groups to which different minimum coverage requirements are applied depending on the degree of risk.

Investment in and management of securities, whether aimed at benefiting from short-term movements or at making steady investments, are included in CBE 4/1991, which recognises four types of portfolios to which different valuation methods are applied: trading book, available for sale portfolio, held-to-maturity portfolio and permanent holdings portfolio.

Fund raising operations through the securitisation of financial assets are recognised either through the writing-off of a transferred asset, or as a liability, provided given requirements are fulfilled, in particular that all the transferor's rights are passed on to the transferee. With respect to this type of transaction, the Circular addresses the accounting treatment of financial asset transfers, rediscount of bills, asset holdings, repurchase agreements and securities lending.

CBE 4/1991 also regulates the accounting treatment of derivatives. When derivatives are considered as hedging instruments against risks arising from other transactions which have al-

(31) Subsequently, Banco de España Circular 4/2000 of 28 June 2000 clarified the definition of net endowment to the statistical provision, excluding changes in the general provision from its calculation.

ready been recognised, the recognition of profits or losses on derivatives shall match the results of the hedged items. When derivatives are considered as non-hedging financial instruments, if they are quoted on an organised market, they shall be recorded immediately; if not, they shall be valued on a monthly basis and solely resulting losses shall be recorded in the profit and loss account. Final results shall be recognised upon settlement.

CIs often create legally independent corporations whose purpose will be to engage in specific activities, such as management of investment funds, cards, etc., or to operate in different geographical areas. As a result, to fulfil the disclosure obligations laid down in the Commercial Code, as well as supervisory capital requirements, CIs are subject to overall consolidation of their financial statements with those of the financial institutions constituting with them a management unit, as defined in the LSM, excluding (as provided for in article 6 of RD 1343/1992) insurance companies, which shall be valued according to the equity method. Jointly managed financial institutions are subject to proportional consolidation. By contrast, non-financial corporations which are included in the economic group of a credit institution, as well as corporations over which, though not included in the economic group, a significant influence is exercised shall be valued according to the equity method and shall appear separately in the consolidated balance sheet under a specific heading.

Pursuant to the latest updating of CBE 4/1991, amended by CBE 5/2000 of 19 September 2000, the accounting treatment of credit institutions' staff pension schemes was adapted to RD 1588/1999 of 15 October 1999 which endorsed the Regulation on the implementation of corporate staff pension schemes in respect of employees and beneficiaries. Furthermore, CBE 4/2001 of 24 September 2001, relating to the information on holdings included in the basis for the calculation of contributions to the Deposit Guarantee Fund (DGF) and on secured amounts, stresses the need for credit institutions to assert careful control in relation to custody accounts.

2.4. Transparency of transactions and customer protection

2.4.1. Former and current regulations

Sectoral regulations aimed at improving bank customer protection were developed in parallel with the interest rate and commission fee liberalisation process, which started in 1981 and culminated in a Ministerial Order of 3 March 1987. This provision, together with its implementing BE Circulars, was the most direct predecessor of current regulations, which replaced strong interventionism with a new stance based on the general principle of freedom of prices for banking products and services supported by a wide array of consumer protection regulations.

Current regulations are based on article 48(2) of the LDI whereby, without prejudice to the principle of freedom to conclude agreements that must govern the relationship between parties, the Minister of Economy is empowered to issue regulations intended to protect the legitimate interests of credit institutions' customers, whether lenders or borrowers (32).

Accordingly, the MO of 1987 was superseded by MO of 12 December 1989, which reinforced and improved the principles established in the former, extending them to all CIs. In turn, the BE was specifically empowered to implement this Ministerial Order, thus issuing CBE 8/1990 of 7 September 1990, as successively amended, which incorporated some of the provi-

(32) Provisions issued by regional governments under the powers conferred upon them in this field shall not offer a lower customer protection level than that provided by central government regulations.

sions laid down in other general regulations (33) in order to ensure the comprehensive applicability of the Circular.

As for Community law, which is not very extensive in this field, the consumer credit Directive (34) and Commission Recommendation of 30 July 1997 concerning transactions by electronic payment instruments and in particular the relationship between issuer and holder were, to a large extent, also incorporated into CBE 8/1990.

CBE 3/2001 of 24 September 2001 amending CBE 8/1990, which will be discussed in more detail in the following sections, basically encompassed two issues. In the first place, the Circular incorporated Community provisions (35) laid down in Law 9/1999 of 2 April 1999 regulating the legal regime of transfers between EU Member States, MO of 16 November 2001 implementing the law, and other provisions relating to transfers in general. In the second place, it embodied several provisions regulating operations carried out through electronic channels, in particular the Internet.

2.4.2. Transparency and customer protection

Among the provisions aimed at ensuring that the customer may receive adequate information to adopt well-founded decisions on the banking product or service concerned, the following should be pointed out:

Effective cost or yield of transactions

The regulations incorporate a definition of effective cost or yield, allowing the comparison of prices applied by institutions offering the same financial product: the equivalent annual rate (EAR), i.e. the rate equalling on an ongoing basis the current value of amounts received and paid on all items between the parties throughout the transaction and in annualised terms. This rate must be included in various types of documents, such as contracts, settlement documents and others.

Subject to technical details relating to specific transactions, the items which are, as a rule, included in or excluded from the EAR are listed in Box A.1.4.

Price of foreign exchange transactions

Without prejudice to the principle of pricing freedom, credit institutions shall publish the exchange rates applied on their retail foreign currency or banknote exchange transactions (under € 3,000), as well as relevant charges and commission fees.

Price of variable interest rate transactions

Certain precautions are established with respect to the reference indices that may be used by credit institutions to set the price of transactions, when this varies over time. Objec-

(33) Specifically, Law 7/1995 of 23 March 1995 on Consumer Credit, Law 2/1994 of 30 March 1994 on the Subrogation and Modification of Mortgage Loans and MO of 5 May 1994 on the Transparency of Financial Conditions for Mortgage Loans.

(34) Council Directive 87/102/EEC of 22 December 1986 for the approximation of the laws, regulations and administrative provisions of the Member States concerning consumer credit, which was transposed, together with its successive amendments, into the Consumer Credit Law.

(35) Directive 97/5/EC of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers.

BOX A.1.4

Items included in or excluded from the EAR

1. *Items included*

   — Nominal interest rate on the transaction.

   — Commission fees on credit transactions (review, commitment and others) and on deposit transactions (account maintenance).

   — Life insurance premia, when imposed by the institution as a condition for granting credit.

2. *Items excluded*

   — Credit subsidies; tax allowances.

   — Commission fees or charges for non-compliance with contract conditions.

   — Fund transfer commission.

   — Facility fee.

   — Valuation charges.

   — Insurance and guarantee charges, with the exception of those appearing under items included.

   — Record checking, notary and registry charges.

   — Withholding and other taxes.

tive prices must be applied. Thus, interest rates published or applied by the credit institution or its group may not be used as a benchmark by these institutions. Moreover, in order to provide standardised benchmarks for these transactions, the BE prepares and publishes on a monthly basis a series of indices or official benchmark rates which, though not compulsory, are widely accepted and include both long-term benchmarks (average interest rates on mortgage loans) and short-term interbank indices [Mibor (36) and Euribor].

Customer information prior to conclusion of the contract

To provide guidance to the market and the public at large, credit institutions are required to publish a number of interest rates: prime rate, overdraft rates on current accounts and credit accounts, as well as reference rates on other commonly granted financial facilities, in particular consumer credit and housing loans.

On the other hand, pricing freedom implies an obligation on credit institutions to make available at all times to customers a prospectus specifying the maximum commission fees which may be charged, the transactions for which they are payable and the conditions governing their application. The prospectus shall also set out the charges payable for transactions and services usually provided by the credit institution. The publication of the above-mentioned rates in the prospectus is considered, as a rule, a condition for their applicability. Therefore, the application of less favourable conditions or of charges for services whose rates are not specified is subject to disciplinary sanctions. For the sake of transparency, the prospectus shall be clear and readily understandable, this requirement being subject to prior approval by the BE and by the National Securities Market Commission in the case of stock market transactions.

(36) Under Order of 1 December 1999, the Mibor, which is expected to be calculated according to a new formula, is not considered as an official index for loans arranged as from 1 January 2000. These provisions were incorporated into CBE 8/1990 through CBE 1/2000 of 28 January 2000.

Under the new regulations the prospectus must include a specific section setting out the general conditions applicable to foreign transactions.

More stringent transparency conditions prior to conclusion of the transaction are applied to mortgage loans. Credit institutions are required to provide information on, inter alia: changes in the benchmark index over the previous two years (in the case of variable-rate loans), transaction costs payable by the customer, the maximum amount of the loan in relation to the appraisal value, the funds payable on account and the terms for contracting the services of third parties.

This information, including at least the points listed in Box A.1.5, shall be displayed on the notice board, in full view of the public, at all the business premises of the credit institution.

Credit institutions engaged exclusively in telephone banking shall communicate the above-mentioned information in writing to their customers, at least on a quarterly basis. When the possibility of carrying out transactions through the Internet is offered, credit institutions shall make available on their website their identification details, the information displayed on the notice board, the prospectus specifying commission fees and the valuation rules applicable.

In certain transactions credit institutions are required to present to the customer a binding offer, undertaking to maintain the conditions of the offer for a given period. This obligation extends, inter alia, to consumer credit when the customer has requested a binding offer and, in general, to mortgage loans regulated by MO of 5 May 1994. Customers may also request a written offer setting out the specific conditions applicable to credit transfers governed by Law 9/1999 of 12 April 1999.

Compulsory delivery of contracts and minimum information requirements

In certain cases, credit institutions are required to deliver a written contract to the customer, as specified in Box A.1.6.

As a rule, together with the contract the institution shall make available to the customer information on the commission fees, charges payable and valuation rules applicable to the agreed transaction. This document shall be sent by electronic means or in writing and shall fulfil the minimum information requirements set out for this purpose. The institution shall keep the customer's acknowledgement of receipt.

Without prejudice to the parties' freedom of contract, the regulation defines minimum information requirements for banking contracts (37) which, in general terms must include information on the interest rate, payment period, commission fees and charges payable, the EAR, etc., whereas the information to be included in mortgage loan contracts is set out in more detail in specific regulations.

Information subsequent to conclusion of the contract

The customer shall be informed of any changes in interest rates or commission fees in good time. As a rule (with the exception of permanent agreements), the communication shall be personally addressed in writing to the customer.

(37) Credit institutions' securities market contracts are regulated under MO of 25 October 1995.

BOX A.1.5

Information to be displayed on the notice board

1. Prime rate, overdraft rates on current accounts (distinguishing between customers and others) and credit accounts. Other benchmark rates.
2. Indication of exchange rates on transactions with banknotes and foreign currencies and conversion rates for euro legacy currencies, with relevant commission fees.
3. Indication of the availability of a prospectus specifying the whole range of commission fees and valuation rules (also on the BE's website).
4. Changes in interest rates on certain transactions (permanent agreements, variable-rate securities).
5. Reference to the Complaints Service of the BE and, where appropriate, to the credit institution's ombudsman.
6. Reference to the regulations on the transparency of banking transactions and customer protection.
7. Indication of the availability of a prospectus on mortgage loans.
8. Information required under securities market transparency regulations.
9. Indication of customers' right to request binding offers, where appropriate.
10. Indication of customers' right to receive an offer with the specific conditions applicable to cross-border credit transfers within the EU.

The customer shall also receive information on the settlement of lending and borrowing transactions and services. Additionally, the requirement to provide information on the settlement of credit transfers has recently been introduced. The relevant obligations (for instance, on current account statements) and minimum information requirements in respect of settlement are laid down in CBE 8/1990.

The information subsequent to conclusion of contracts may be supplied by electronic means, if so requested by the customer or if the contract has been concluded electronically and includes this condition.

2.4.3. Other protection regulations

As an exception to the principle of pricing freedom, certain limits have been established in relation to the ordinary transactions of a wide range of customers. Thus, the maximum commission fee for prepayment or creditor subrogation on variable-rate mortgage loans shall be 1 % of the prepaid or subrogated amount, unless a lesser rate has been agreed in the contract (38). Likewise, the maximum commission fee for prepayment of loans regulated by the Consumer Credit Law shall not exceed 1.5 % of the prepaid capital under variable-rate contracts and 3 % under fixed-rate contracts. There are also limits on the interest rate applied to current account overdrafts (39).

Within this framework, under Regulation (EC) No 2560/2001 of the European Parliament and of the Council of 19 December 2001 on cross-border payments in euro, charges lev-

(38) Law 2/1994 of 30 March 1994.

(39) The upper limit set out in article 19(4) of the Consumer Credit Law is the interest rate giving rise to an EAR which does not exceed 2.5 times the legal rate of interest.

BOX A.1.6

Compulsory delivery of contract

1. Opening of current and savings accounts, as well as issuance or renewal (when new conditions are established) of relevant electronic payment instruments.
2. When the contract amount is lower than € 60,000, on loans and credits, including commercial discount (excluding overdrafts on current and credit accounts, unless requested by the customer), term deposits, bank and similar commercial paper and repurchase agreements on financial instruments traded on organised markets.
3. Financial leasing transactions.
4. Non-standardised or customised transactions.
5. Transactions requiring standard contracts, as provided for under MO of 25 October 1995 (specific government debt transactions, portfolio or securities management contracts) and MO of 7 July 1989 on government debt financial accounts.
6. When the credit institution and the customer agree that services may be requested or used through phone-banking.
7. When requested by the customer.

ied by an institution in respect of electronic payment transactions and credit transfers in euro up to the amounts specified therein shall be the same whether the transaction is carried out between or within EU Member States. This Regulation shall be implemented with effect from 1 July 2002 for electronic payment transactions and 1 July 2003 for credit transfers.

For the purposes of accrued interest, the value date for transactions credited or debited to customer accounts does not normally coincide with the transaction execution date or the drawdown date. Consequently, the time lag allowed (maximum for credits and minimum for debits) is established according to the type of transaction and credit institutions are required to make every effort to credit or debit customer accounts without delay.

Advertising of transactions or services provided by CIs is subject to Law 34/1988 of 11 November 1988 on Advertising and to approval by the BE or by regional governments within their field of competence, when cost or yield is explicitly or implicitly referred to. The reason for establishing this requirement (which in no event implies recommending the product or service advertised) is to ensure that advertising reflects in a clear and precise form, and in relation to competitors, the main characteristics of the transactions, in particular the obligation to inform on the EAR.

— The function of the Complaints Service of the Banco de España, created in 1987, is to receive and process complaints related to specific transactions lodged by customers in respect of CI activities which may involve the infringement of rules of conduct and good banking practices and customs (40).

The regulations define the complaints filing, processing and resolution procedure. In this respect, it is worth noting that claimants are required to lodge the complaint in the first place

(40) Article 9 of MO of 12 December 1989 and Chapter II of CBE 8/1990. Pursuant to Order of 16 November 2000 on the regulation of certain aspects of the legal regime of currency-exchange bureaux and their agents, the field of competence of the Complaints Service has recently been extended to customer complaints against currency-exchange bureaux authorised to conduct transactions with foreign banknotes and traveller's cheques and to arrange cross-border credit transfers.

with the credit institution's ombudsman, if any, and that the Complaints Service issues a non-binding report which is notified to the parties concerned. An extensive Annual Report is made available by the Complaints Service on the BE's website.

2.5. Other banking regulations

Expansion: establishment of branches and business pursued through agents

Branches may be freely established within Spanish territory (41) subject to possible statutory restrictions and, as mentioned above, the limits which apply in the event of non-compliance with capital requirements.

Another form of expansion is to pursue business through agents, i.e. persons granted power of attorney by the institution to carry out standard banking transactions with its customers on its behalf. Among the LDI-based conditions regulating the relationship between CIs and their agents (42), the following should be highlighted: the responsibility for compliance with regulatory and disciplinary rules in respect of activities undertaken by the agent rests with the principal credit institution; under exclusive agency terms, the agent must represent a single institution or group; the agent must unequivocally identify the principal credit institution in all relationships with customers.

Incompatibilities associated with holding the position of senior official

Under the regulations applicable to each type of credit institution, members of the board, or similar body, and senior managers, or similar officials, shall not be allowed to hold similar positions in other CIs or companies (43).

As far as banks are concerned, under a regulation dating back to 1968, senior officials are prohibited, in general, from holding a similar position in other banks and from being on more than four boards of directors of public limited companies. Subject to an overall limit of eight posts, the aforementioned prohibition does not apply to positions held in family companies, as defined for these purposes; in firms in which the bank has qualifying holdings; and in "related" banks (currently to be interpreted as referring to banks within the same group). A specific restriction is applied to positions with general executive powers (managing director and senior managers) which are not compatible with any other position and require full-time commitment. Regulations applicable to savings banks and credit co-operatives set out similar restrictions for senior officials.

Central Credit Register of the BE

The Central Credit Register of the BE (CCR) was created in 1962 (44), when the BE was entrusted with the task of establishing a service dealing with credit transactions carried out by banks, savings banks and other credit institutions. Pursuant to OM of 13 February 1963, the BE

(41) Article 30 bis of the LDI.

(42) Article 30 bis of the LDI and article 22 of RD 1245/1995 of 14 April 1995. In addition to the conditions laid down in these provisions there are those applicable under securities regulations when the activities pursued by agents include transactions falling under such regulations.

(43) With respect to savings and co-operative banks, the regulations issued by regional governments within their field of competence are also applicable.

(44) Article 16 of Decree-Law 18/1962 of 7 June 1962, updated in the Bill on the Reform of the Financial System.

has been issuing the provisions regulating the operation and scope of this service, the latest being CBE 3/1995 of 25 September 1995, which sets out the current regime.

The institutions required to report exposures to the CCR on a monthly basis are Spanish CIs, in respect of their entire business (including that of their foreign branches and special purpose vehicles), and foreign CIs, in respect of their activities in Spain. The BE, the Deposit Guarantee Fund and mutual guarantee companies are also reporting institutions.

In general terms, direct exposures arising from credit, money or off-balance-sheet transactions, including debt securities, as well as indirect exposures to guarantors of direct exposure transactions, are required to be reported, where these are above a minimum amount specified under CBE 1/2001 of 30 March 2001 (45).

Each reporting institution may access CCR aggregate data on the total risk incurred in the system by the borrowers in relation to which it has reported exposures, or data on the risk incurred by borrowers which have expressly authorised access to their data. The information supplied which is, in any event, subject to professional secrecy, is intended as an instrument to help improve the analysis and monitoring of exposures, for the purpose of ensuring the solvency of credit institutions.

Finally, it should be pointed out that, under article 56 of Law 39/1988 of 28 December 1988 regulating Local Finance, the BE co-operates with the Ministry of Economy in the operation of the Central Credit Register for Local Authorities (46), which is under the responsibility of the Ministry, by providing the relevant information received by the CCR.

3. CORRECTIVE MEASURES

The supervisory framework described above is supplemented by: a regime for the imposition of sanctions to which CIs are subject; the supervisory powers conferred upon the BE, under which it is authorised to intervene in the management of institutions facing exceptionally serious problems by placing them under administration or replacing their directors; and measures aimed at the protection of depositors and investors and the management of banking crises through the action of the Deposit Guarantee Fund (DGF).

Most of the following legal provisions were urgently adopted to manage the crisis which affected the Spanish banking system between 1978 and 1984.

3.1. Regime for the imposition of sanctions

The LDI consolidated for the first time the formerly dispersed infringement provisions applicable to CIs.

The power to impose sanctions laid down in the LDI is established for cases of statutory infringements classified as very serious, serious or minor (irrespective of the concurrence of possible serious or minor offences under criminal law). Minor infringements are defined on a residual basis, i.e. as breaches which are not expressly specified. Very serious and serious in-

(45) In general, the minimum amount for which exposures are to be reported is € 6,000 in respect of the entire business in Spain and € 60,000 in any other country for direct exposures to residents, and € 300,000 for direct exposures to non-residents.

(46) Recently regulated under RD 1438/2001 of 21 December 2001.

fringement generally refer to similar situations, as set out in the regulations applicable to CI's activities, although very serious infringements are characterised by aggravating circumstances.

Liability for infringements falls on CIs, including branches of foreign CIs, their senior officials and, in certain cases, persons possessing qualifying holdings in such institutions. Additionally, any physical or legal persons, other than credit institutions, undertaking activities restricted to CI's are also liable to the extent set out in the LDI.

The procedure is governed, with certain special characteristics, by RD 2119/1993 of 3 December 1993 on the infringement procedure applicable to institutions operating on financial markets. The power to institute proceedings and to impose sanctions in respect of minor or serious infringements is vested in the BE and the resolution of very serious infringements rests with the Ministry of Economy, with the exception of revocation of authorisation to operate as a credit institution, where the power is vested, in general, in the Council of Ministers.

Depending on the seriousness of the infringement, and after applying statutory evaluation criteria, sanctions applicable to credit institutions range from private warning to fines of varying amounts and, finally, revocation of authorisation or, in the case of branches of Community institutions, a ban on the undertaking of any new operations within Spanish territory. Sanctions applicable to managers or administrators who are responsible for the infringement include warning and fines, as well as suspension from duty and disqualification for holding similar positions in the same or any other credit institution (47).

Subject to the above-mentioned procedure, savings banks and credit co-operatives in the field of competence of regional governments are also subject to the infringement procedure established at the regional level in relation to infringements in respect of which the power to impose sanctions is not reserved to the central government under article 149(1)(11) of the Spanish Constitution (48). In the case of serious or very serious infringements, the resolution proposed by the competent regional body must be approved by the BE.

Finally, as from 1 January 1999, Spanish CIs are subject to the powers of the ECB to impose sanctions in the event of non-compliance with minimum reserve requirements (49).

3.2. Administration and replacement of directors

Measures such as placing a credit institution under administration or replacing its directors, formerly set out in the extinguished RDL 5/1978 of 6 March 1978, have now been incorporated into the LDI. Both measures refer to the possibility of intervening in the ordinary management of the institution when, as laid down in the law "a credit institution faces exceptionally serious problems affecting its capital adequacy, stability, liquidity or solvency", and where it is impossible to infer the true situation of the institution from its accounts. The time limit for these measures is conditional on resolving the situation which gave rise to such remedial action. The choice of the action to be taken depends on the assessment of the specific situation, at the discretion of the BE within its technical field of competence.

(47) Certain aspects of the infringement procedure are updated in the Bill on the Reform of the Financial System.

(48) Statutory infringements related to the solvency of credit institutions, as specified in article 42 of the LDI, are reserved to the central government. See judgment of the Constitutional Court 96/1996 of 30 May 1996.

(49) See article 7 of Council Regulation (EC) No 2531/98 of 23 November 1998 relating to the sanctions and the specific procedure applicable in cases of non-compliance with minimum reserve requirements, as well as Council Regulation (EC) No 2532/98 of 23 November 1998 and European Central Bank Regulation (EC) No 2157/1999 of 23 September 1999 on the powers of the European Central Bank to impose sanctions.

The reasons for which these measures, which are of a prudential and exceptional nature and are not to be considered as sanctions, are adopted must be stated. Although these actions have frequently been associated, either simultaneously or subsequently, with insolvency proceedings or with the intervention of the DGF, they may also be applicable to a credit institution, as has already occurred in practice, where such circumstances do not concur.

The decision to place a credit institution under administration or to replace its directors rests exclusively with the BE and may be adopted ex officio or at the request of the institution concerned. Notification of the reasoned decision shall be given to the Ministry of Economy. The credit institution shall be heard in both cases, except if the measure has been requested by the institution or when the delay that such hearing would imply might seriously jeopardise the effectiveness of the action or the economic interests of the parties concerned.

When a credit institution is placed under administration, the proceedings and agreements adopted by any of its bodies as from the date of publication of the administration resolution in the Official State Gazette shall not be valid and may not be executed unless they are expressly authorised by the administrators appointed in the resolution, with the sole exception of those related to actions brought or appeals lodged against the resolution or the conduct of administrators. Likewise, any powers of attorney or proxies granted before the administration resolution is made public may be revoked by the administrators.

When the directors of a credit institution are replaced, they are substituted by provisional directors who shall assume the powers of the institution's managing body and also the functions of administrators in relation to General Meeting resolutions, over which they shall therefore have the power of veto.

Finally, several regional governments are also conferred certain powers in respect of administration and replacement of directors of savings banks established within their territory.

3.3. Deposit guarantee funds

DGFs, one for each type of credit institution, were set up in the late seventies (50). Their institutional framework and basic functions have remained broadly unchanged, though their legal regime has been updated on several occasions, in particular as a result of the transposition of the relevant Community legislation.

Each DGF is run by a management committee composed of four representatives of the BE, one of whom is the chairman and has the casting vote, and four representatives of member institutions, all of whom are appointed by the Minister of Economy.

Further to the transposition of Community regulations on deposit-guarantee schemes (51), membership of DGFs, which had previously been voluntary, became compulsory

(50) The Bank Deposit Guarantee Fund was set up under RD 3048/1977 of 11 November 1977 and was afforded legal personality by RDL 4/1980 of 28 March 1980. The Savings Bank DGF was created under RD 2860/1980 of 4 December 1980 and was invested with legal personality by RDL 18/1982 of 24 September 1982, under which the Co-operative Bank DGF was also set up with legal personality and full capacity. There is no deposit guarantee fund for specialised credit institutions, since they are not allowed to take deposits,

(51) Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit-guarantee schemes, which was transposed into Spanish law, together with other changes to the regulation of these DGFs, through the seventh additional provision to RDL 12/1995 of 28 December 1995. The common implementing provisions applicable to the three DGFs were laid down in RD 2602/1996 of 20 December 1996.

for all Spanish credit institutions, as well as for branches of CIs located in countries outside the EU, when their deposits in Spain are not covered by a deposit-guarantee scheme in their home country or when the latter must be supplemented to reach the level and scope of cover offered by the Spanish one. As for branches situated within the EU, membership of Spanish DGFs is optional, depending on the harmonisation of the level of protection provided throughout the Community. When membership of the relevant DGF is compulsory, failure to join the scheme or exclusion from the same for specified reasons may entail the revocation of the authorisation to operate as a credit institution.

DGFs were initially financed jointly by the BE and member institutions. However, in 1996 it was established that the cost of financing such schemes would fall entirely on the latter, with an annual contribution of up to 0.2 % of the guaranteed deposits (currently the rate is much lower) (52). This notwithstanding, extraordinary contributions by the BE may be allowed by law.

From the outset, two basic functions have been assigned to DGFs: provision of deposit guarantee and management of banking crises, including participation in any insolvency proceedings which may affect a credit institution.

With respect to the general guarantee function of DGFs, the guarantee provided covers deposits received from each depositor by the credit institution in Spain and in the EU up to the amount of € 20,000. However, certain deposits are excluded from guarantee, such as debt securities issued by the institution and bearer certificates of deposit, as well as, as a form of sanction, deposits taken in breach of the law or subject to unusual financial conditions which have helped to aggravate the institution's financial situation.

The scope of the guarantee provided has recently been extended to investors who have entrusted securities or other financial instruments to credit institutions in connection with investment business (53), in order to cover the risk of temporary unavailability that may arise from the insolvency or suspension of payments of the intermediary in its securities and financial instruments business. Cover for each investor is provided separately from the guarantee afforded for deposits and up to the same amount.

In this respect, two regulations were issued in 2001. RD 848/2001 of 3 August 2001 on investor-compensation schemes (54) introduced partial changes into the regulatory regime of DGFs laid down in RD 2606/1996 of 20 December 1996 in order to incorporate the extended scope of the guarantee. Pursuant to the powers delegated to the BE, CBE 4/2001 of 24 September 2001 set out the valuation standards to be applied to the various types of securities and instruments included in the calculation of annual contributions to DGFs, as well as the information that member institutions are required to report on an annual basis to the BE for the calculation of such contributions.

The two cases covered by the guarantee are the declaration of insolvency and the admission of petition for suspension of payments of the institution concerned (or suspension of the

(52) Pursuant to two ministerial orders of 14 February 2002, the ratio to be applied has been set at 0.6 per thousand for banks, 0.4 per thousand for savings banks and 1 per thousand for co-operative banks.

(53) Pursuant to Directive 97/9/EC of the European Parliament and of the Council of 3 March 1997 on investor-compensation schemes, transposed into Spanish Law, in respect of investment business carried out through CIs, under the thirteenth additional provision to Law 37/1998 of 16 November 1998 on the Reform of the Securities Market, which introduced a new article 2 ter in RDL 18/1982 of 24 May 1982.

(54) This RD refers to investor-compensation schemes operating both through investment firms and CIs, for which similar broad standards are established, though in the case of CIs the guarantee is provided through the existing DGFs.

restitution of securities or financial instruments). Further to the transposition of Community legislation, other cases covered by the guarantee are those in which, even though no such judicial proceedings have been initiated, deposits have not been repaid or securities and financial instruments have not been returned and the BE determines that the institution is unable to fulfil these obligations in the near future.

With regard to their second basic function, i.e. the management of banking crises, DGFs play a markedly different role to other European bodies which are solely responsible for providing the aforementioned guarantee. Indeed, they may adopt preventive and reorganisation measures aimed at improving the institution's viability within a reasonable period of time in order to overcome the crisis situation. These measures must be adopted within the framework of an action plan agreed by the institution and formally approved by the BE, this being the only direct intervention by the BE in the management of the crisis, although their adoption may coincide with or follow the placing of the institution under administration or the replacement of its directors.

One of the technical standards to be taken into account when adopting preventive or reorganisation measures, which is expressly referred to in the above-mentioned regulations, is the evaluation of the cost of financing such assistance, compared with the potential cost to the DGFs of payment under the guarantees if these measures were not adopted.

There is an extensive list of possible measures, ranging from direct financial assistance (non-returnable, guarantee, loans under favourable conditions, purchase of non-profitable or impaired assets, etc.) to capital restructuring, including measures aimed at facilitating merger with or acquisition by other sound institutions or the transfer of the business to another institution, as well as capital increases subscribed by the DGF. In this case, holdings acquired must be sold within a year under the procedure concerned.

Finally, it should be pointed out that DGFs play a significant role when institutions are subject to insolvency proceedings and that in cases of suspension of payments two of the administrators appointed by the judge are taken from lists presented by the DGF to which the institution belongs or has belonged. The direct administration of the institution is assumed in accordance with the Law on Suspension of Payments and the administrator is the DGF itself. In the case of a declaration of insolvency, the functions of commissioner, receiver and trustees are assumed by the DGF concerned.

Where CIs are subject to insolvency proceedings with cross-border effects within the EU, Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions requires the principles of unity and universality to be applied to the credit institution, including branches located in other Member States. This means that the authorities of the home Member State shall alone be empowered to adopt reorganisation measures or open winding-up proceedings in respect of a credit institution, including branches established in other Member States in which their decisions are recognised. In turn, unless otherwise provided, these measures and proceedings shall be in compliance with the laws applicable in the home Member State.

3.4. Revocation of authorisation

Subject to the regulations issued by regional governments within their field of competence over savings banks and credit co-operatives, at the national level the entire list of grounds for revocation of authorisation to operate as a credit institution is set out in article 57 bis of the Banking Law of 31 December 1946, as successively amended.

The grounds for revoking authorisation include initial or subsequent absence of activity, obtaining the authorisation through false statements or by irregular means, failure to fulfil authorisation conditions, capital inadequacy, lack of security that obligations shall be honoured or exclusion from a DGF. The authorisation may also be revoked as a result of an infringement procedure. Foreign branches whose authorisation has been withdrawn by their home country authorities shall not be allowed to continue to operate in Spain.

The Council of Ministers is the authority responsible for deciding on revocation of authorisation, on the basis of a proposal by the Minister of Economy. However, the latter is specifically empowered to take this decision in the event of exclusion from the DGF and, in the case of branches, when the authorisation of the credit institution has been revoked in its home country.

Revocation of authorisation implies by law the winding up of the institution concerned and the opening of a liquidation period in accordance with the applicable company regulations. When winding up is not the consequence of revocation of authorisation (for instance, in the case of voluntary winding up), the Minister of Economy may decide that winding-up proceedings should be initiated if the number of persons affected or the financial situation of the institution make it advisable (55).

4. OTHER REGULATIONS APPLICABLE TO CREDIT INSTITUTIONS

4.1. Activities on securities markets

The LSM established the current legal framework for financial activities related to the issuance and trading of securities on regulated markets, as well as the rules applicable to specialised entities, mainly securities dealers. Likewise, the Law expressly recognised that the greater part of these financial activities could be carried on by banks, savings banks and credit co-operatives. However, since membership of stock exchanges was restricted to securities dealers, it was common practice for banking groups to become members by setting up specialised subsidiaries.

This restriction was abolished by Law 37/1998 of 16 November 1998, amending the LSM for the purpose of transposing the Investment Services Directive (56). As a result, all CIs can normally carry on all the activities considered as investment services (both core and non-core services), provided that their legal status does not prohibit such activities, and they can also become members of regulated markets. This also applies to foreign CIs, distinguishing between Community and non-Community institutions.

Accordingly, CIs are governed by the LSM and its implementing provisions, whereby they are subject to the supervision and inspection of the CNMV, which is also assigned the powers to impose sanctions. It should be pointed out that co-operation between the BE and the CNMV is required by law (57) for the purpose of co-ordinating the action of both institutions within their respective fields of competence. Specifically, when the infringement has been committed by a credit institution, disciplinary sanctions are to be imposed on the basis of an opinion from the BE.

With regard to regulated markets, under the LSM the BE is the governing body of the Public Debt Book-Entry Market, dating back to 1987, and runs the Public Debt Book-Entry System, which publishes an annual report with relevant information on this market.

(55) Article 38 of the LDI.

(56) Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field.

(57) The institutional interrelationship is reflected in the composition of the governing bodies of both institutions. Thus, the Vice-president of the CNMV and the Deputy Governor of the BE are ex officio members of the Governing Council of the BE and of the Council of the CNMV, respectively.

4.2. Payment and securities settlement systems

The BE is the manager of two of the payment and settlement systems regulated by Law 41/1999 of 12 November 1999 on payment and securities settlement systems, i.e. the aforementioned Public Debt Book-Entry System (58) and the SLBE (Banco de España Settlement Service, formerly called the Money Market Telephone Service) (59).

The SLBE is a clearing and settlement system providing credit transfer services and ensuring the execution and settlement of transactions carried out by member institutions on money and public debt markets and in other environments. Furthermore, it is one of the components of the TARGET system through which NCBs' real time gross settlement systems and the ECB's payment mechanism are interlinked.

4.3. National Electronic Clearing System

The SNCE (National Electronic Clearing System) was set up under RD 1368/1987 of 18 September 1987, which entrusts the administration and management of the system to the BE. The SNCE ensures the electronic clearing and settlement of documents and other means of payment between member institutions (CIs operating in Spain and the BE).

The SNCE, which is considered as a clearing house pursuant to the Law on Negotiable Instruments and Cheques, currently ensures the clearing of most commercial bills, other payment orders and credit transfers intermediated by CIs, as a result of the virtual disappearance of conventional clearing channels. The SNCE is regulated by the BE (60), assisted by an advisory committee composed of representatives of member institutions.

4.4. Foreign transactions

The liberalisation of foreign transactions brought about by RD 1816/1991 of 20 December 1991, implemented by MO of 27 December 1991, replaced former controls and restrictions by a series of reporting requirements aimed at monitoring transactions for statistical and fiscal purposes. Reporting requirements apply to both individuals involved in the transactions and CIs ensuring payments and receipts between residents and non-residents and providing credit transfer services. Most of the information is transmitted through the BE in accordance with the procedures laid down in the circulars issued by the BE pursuant to the delegation of powers set out in the mentioned RD.

In particular, CIs are required to report on the accounts held in Spain by non- residents. Account holders must be identified and their condition as non-residents must be specified and periodically confirmed. Furthermore, CIs are required to report on a regular basis on banknote stocks and changes in same, balances and movements of accounts held by non-resident creditors in such institutions, interbank transfers and clearing on non-residents' accounts, etc.

4.5. Money laundering

Law 19/1993 of 28 December 1993 on certain measures for the prevention of money laundering transposed into Spanish law the minimum harmonised conditions set out in Direc-

(58) The Bill on the Reform of the Financial System introduces changes in respect of securities clearing and settlement systems.

(59) Regulated under CBE 11/1998 of 23 December 1998. See also CBE 5/1990 of 28 March 1990, CBE 7/1995 of 31 October 1995 and CBE 4/1997 of 29 April 1997.

(60) See mainly CBE 8/1988 of 14 June 1988, which incorporates the rules applicable to the SNCE.

tive 91/308/EEC of 10 June 1991. The purpose of the Law and its implementing Regulation was to prevent and combat the use of CIs, financial intermediaries and other reporting institutions to launder proceeds from drug trafficking, terrorism and organised crime.

For this purpose, the Law set up the Commission for the Prevention of Money Laundering and Monetary Offences, attached to the Ministry of Economy and composed of representatives of different judicial and administrative authorities operating in this field. The Commission is assisted by a Secretariat and an Executive Service (the SEPBLAC) attached to the BE. The Law also laid down two basic requirements (and the relevant infringement procedure) for reporting institutions: the obligation to identify customers and to report to the SEPBLAC any fact or transaction in respect of which there may be indications or certainty that they are related to the laundering of proceeds from the aforesaid activities or which have reached the threshold set out as a warning signal for this purpose.

Directive 2001/97/EC of 4 December 2001, amending Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, has broadened the range of reporting institutions and underlying criminal activities.

ANNEX II

SANCTIONING PROCEEDINGS

The legal definition of sanctionable conduct is a logical consequence of sectoral administrative regimes that make the taking up and pursuit of a particular economic activity subject to compliance with a number of requirements, this being the case of the regulatory and disciplinary rules for credit institutions (CIs).

When the degree to which such rules are respected has been checked using the supervisory powers assigned by law to the Banco de España (BE), the possible infringements detected constitute the grounds for subsequent sanctioning proceedings. The latter are governed by the principles of definition and legality common to the general sanctioning activity of general government.

1. BASIC NOTES ON SANCTIONING PROCEDURE

Without prejudice to the specific provisions of Law 26/1988 of 29 July 1988 on the Discipline and Intervention of Credit Institutions (LDI), the administrative sanctioning procedure is regulated by Law 30/1992 of 26 November 1992 on General Government and the Common Administrative Procedure, as amended by Law 4/1999 of 13 January 1999 and Law 24/2001 of 27 December 2001 on Fiscal, Administrative and Social Measures, as well as by Royal Decree 1398/1993 of 4 August 1993, which approved the Regulation of the procedure for exercising the sanctioning power, and Royal Decree 2119/1993 of 3 December 1993 on the sanctioning procedure applicable to financial market participants.

In accordance with the provisions of Article 2(1) of Royal Decree 2119/1993 of 3 December 1993, sanctioning procedures shall be conducted and resolved within a period of one year. It should be pointed out that this period applies to the sanctioning proceeding itself from the moment it is formally commenced. Accordingly, it does not cover the prior inspection period, when possible irregularities are detected. Both the overall one-year period and sub-periods can be extended under the provisions of Article 49(1) of Law 4/1999 of 13 January 1999, with the parties concerned being notified of the decision adopted. That said, the sanctioning procedure shall in no event last for more than eighteen months.

As regards the appeals system, appeal against the sanctioning decisions of the BE lies to the Ministry of Economy. In the case of sanctions for very serious infringements, which the Minister or Council of Ministers (in the case of the sanction of revocation) are able to impose, appeal lies to the same body. In the case of sanctions imposed by the BE or the Ministry of Economy, when administrative proceedings have been exhausted the defendants may file a contentious-administrative appeal with the Contentious-Administrative Division of the *Audiencia Nacional*.

2. STATISTICS ON PROCEEDINGS

2.1. Proceedings conducted during the period 1997-2001

Table A.2.1 shows the total number of disciplinary proceedings commenced over the last five years.

Part I of the table shows the disciplinary proceedings, conducted under the sanctioning regime for CIs, which is regulated in Title One of the LDI, affecting each type of CI: banks, savings banks, credit co-operatives and specialised credit institutions. A proceeding conducted against a member of the board of directors of a CI in respect of infringements for which that CI has already been sanctioned is also included.

Part II refers to the proceedings conducted against supervised institutions other than CIs. During this five-year period these have affected mutual guarantee companies (MGCs) and appraisal companies (ACs).

It should be noted that Article 67 of Law 1/1994 on SGRs provides that this type of institution, as well as those who hold administrative or management posts therein, shall be subject to the disciplinary rules contained in the LDI, to the extent that they are applicable to the characteristics and activity of such institutions.

As regards ACs, their sanctioning regime is regulated in Additional Provision Ten of Law 3/1994, which adapts Spanish law on credit institutions to the Second Banking Co-ordination Directive and introduces other amendments relating to the financial system. As regards their activity and nature it refers to the LDI, with the necessary amendments and adaptations.

This part includes those proceedings for loss of approval to render appraisal services and for revocation of the authorisation of mutual guarantee companies, notwithstanding that they are proceedings of a non-disciplinary nature.

Part III refers to proceedings conducted under the provisions of Title II of the LDI, which provides for the commencement of proceedings against natural or legal persons who, without

TABLE A.2.1

Proceedings by type of institution

INSTITUTIONS	1997	1998	1999	2000	2001	TOTALS
I. Banks	6	8	8	2	2	26
Credit co-operatives	1	2	4	4	5	16
SCIs	1		1	3	1	6
Directors and senior executives of institutions	1					1
II. ACs				1		1
MGCs		1				1
AC revocations				3	1	4
MGC revocations	2					2
III. Use of names or pursuit of activities reserved for CIs	4	2	4	2	2	14
IV. Advertising	1	2				3
V. Non-compliance with ECB minimum reserve requirements			5	6	7	18
TOTALS	**17**	**18**	**24**	**22**	**18**	**99**

having obtained the required authorisation and without being entered in the relevant registers, pursue within Spanish territory activities that only CIs are legally authorised to carry on or use the generic names reserved for CIs or any other that may lead to their being confused with CIs.

Part IV covers those proceedings conducted under the provisions of Article 15 of Law 13/1994 of 1 June 1994 on Autonomy of the Banco de España, which regulates the use in advertising of banknotes and coins which are or have been legal tender, and of their reproductions. It defines advertising that uses such material without BE authorisation as an administrative infringement sanctionable by a fine of up to ESP 100 million (€ 601,012.1).

Lastly, Part V covers proceedings relating to non-compliance with the minimum reserve requirements established by the Governing Council of the ECB pursuant to Article 19 of the Statute of the ESCB and of the ECB. These procedures are conducted in accordance with Council Regulation (EC) No 2531/98 of 23 November 1998 and Regulation (EC) No 2818/1998 of 1 December 1998 of the ECB on the application of minimum reserves, as well as Council Regulation (EC) No 2532/98 of 23 November 1998 and ECB Regulation (EC) No 2157/1999 of 23 September 1999 on the powers of the European Central Bank to impose sanctions, so that the powers, both to commence proceedings and to resolve them, lie with the ECB.

2.2. Disciplinary proceedings conducted during the period 1997-2001, classified by type of infringement

The information in Table A.2.2. supplements that in Table A.2.1, since it shows the total number of infringements sanctioned in proceedings commenced during the five-year period 1997-2001, classified on the basis of their seriousness, in accordance with the provisions of Article 3 of the LDI.

In addition, it provides information in relation to proceedings that have been brought against directors and senior executives of CIs. In fact, in accordance with Article 1 of the LDI, the infringement of regulatory and disciplinary rules gives rise to administrative liability both on the part of the CIs and the persons holding directorships or management posts therein, when

TABLE A.2.2

Proceedings by type of infringement

Year	Number of proceedings	Infringement			Proceedings dismissed	Reserved name (art. 29, LDI)	ACs (RD 775/97)	Non-compliance with ECB minimum reserve
		Very Serious	Serious	Minor				
1997	17 Proceedings against institutions	2	11		1	5	2	
	11 Proceedings against particular directors of such institutions		1	9		2		
1998	18 Proceedings against institutions		14		2	2		
1999	24 Proceedings against institutions		15	1	3	2		5
	1 Proceeding against particular directors of such institutions						1	
2000	22 Proceedings against institutions	4	15	5		2	3	6
	76 Proceedings against particular directors of such institutions		20	80	24			
2001	12 Proceedings against institutions	1	6	1			1	7
	19 Proceedings against particular directors of such institutions		13	18		3		

serious or very serious infringements are attributable to their wrongdoing or negligence. In such cases, according to Article 21 of the LDI, sanctions imposed on the CIs and the persons holding directorships or management posts therein, which arise from the same infringement, shall be imposed by a single resolution in a single procedure.

The supplementary nature of the information in Table A.2.2. stems from both these aspects since, in sum, a single proceeding gives rise to several persons being found liable for infringements and, on occasions, each being liable for various infringements.

ANNEX III

CONSOLIDATED GROUPS OF CREDIT INSTITUTIONS AND INDIVIDUAL INSTITUTIONS DECEMBER 2001

EXPLANATORY NOTE

The following is a list of Spanish consolidated groups of credit institutions (CGs) and of individual Spanish credit institutions that do not belong to any CG. They are listed under the headings of banks, savings banks and credit co-operatives and specialised credit institutions, the consolidated groups (which are classified in accordance with the nature of the parent institution) being shown first. The code on the left is the number of the institution in the Banco de España's register of institutions.

BANKS

		CONSOLIDATION METHOD APPLIED (1)
GRUPO ATLANTICO		
0008	BANCO ATLANTICO	11
8916	ATLANTICO SERVICIOS FINANCIEROS	11
(INSTITUTIONS: 2)		
GRUPO DEUTSCHE SAE		
0019	DEUTSCHE BANK S.A.E.	11
0205	DEUTSCHE BANK CREDIT	11
(INSTITUTIONS: 2)		
GRUPO BSCH		
0049	BANCO SANTANDER CENTRAL HISPANO	11
0011	ALLFUNDS BANK, S.A.	11
0030	BANCO ESPAÑOL DE CREDITO	11
0036	SANTANDER CENTRAL HISPANO INVEST	11
0038	BANESTO BANCO DE EMISIONES	11
0073	PATAGON INTERNET BANK, S.A.	11
0083	BANCO ALICANTINO DE COMERCIO	11
0086	BANCO BSN BANIF	11
0091	BANCO DE ALBACETE	11
0100	BANCO DE VITORIA	11
0109	BANCO DEL DESARROLLO ECONOMICO E	11
0224	HBF BANCO FINANCIERO,S.A.	11

(1) Consolidation method applied:
11.—Global consolidation method
22.—Proportionate consolidation method

4757	BSCH LEASING S.A.	11
4797	BSCH MULTILEASE	11
8206	HIPOTEBANSA	11
8236	HISPAMER SERV.FINANCIEROS	11
8314	BANSANDER DE FINANCIACIONES	11
8490	SANTANA CREDIT	11
8906	BSCH FACTORING Y CONFIRMING	11
8910	BANESTO FACTORING	11
(INSTITUTIONS: 20)		
GRUPO PARIBAS		
0058	BNP PARIBAS ESPAÑA, S.A.	11
0225	BANCO FIMESTIC	11
8512	UNION DE CREDITOS INMOBILIARIOS	11
8791	BNP-CONSUMO	11
8798	EUROCREDITO	11
8914	BNP PARIBAS LEASE GROUP, S.A.	11
(INSTITUTIONS: 6)		
GRUPO MAPFRE		
0063	BANCO MAPFRE	11
4837	MADRID LEASING CORPORACION	11
8793	FINANMADRID	11
(INSTITUTIONS: 3)		
GRUPO PASTOR		
0072	BANCO PASTOR	11
8620	PASTOR SERVICIOS FINANCIEROS	11
(INSTITUTIONS: 2)		
GRUPO POPULAR		
0075	BANCO POPULAR ESPAÑOL	11
0004	BANCO DE ANDALUCIA	11
0024	BANCO DE CREDITO BALEAR	11
0082	BANCO DE CASTILLA	11
0095	BANCO DE VASCONIA	11
0097	BANCO DE GALICIA	11
0216	BANCO POPULAR HIPOTECARIO	22
0229	BANCOPOPULAR-E, S.A.	11
8903	HELLER FACTORING ESPAÑOLA	22
(INSTITUTIONS: 9)		
GRUPO SABADELL		
0081	BANCO DE SABADELL	11
0043	BANCO HERRERO	11
0118	BANCO DE ASTURIAS	11
0185	SABADELL BANCA PRIVADA, S.A.	11
0230	ACTIVOBANK, S.A.	22
4719	BANSABADELL LEASING	11
8211	BANSABADELL HIPOTECARIA	11
8225	SOLBANK LEASING, E.F.C.	11
8789	BANASTURIAS LEASING, E.F.C.	11
8909	BANSABADELL FACTORING	11
(INSTITUTIONS: 10)		
GR. BANK OF AMERICA		
0088	BANK OF AMERICA	11
(INSTITUTIONS: 1)		
GRUPO BANCOVAL-DEXIA		
0094	BANCOVAL	11

0231	DEXIA BANCO LOCAL, S.A.	11
(INSTITUTIONS: 2)		

GRUPO ZARAGOZANO

0103	BANCO ZARAGOZANO	11
8905	BANZANO GROUP FACTORING	11
(INSTITUTIONS: 2)		

GRUPO CAIXA GERAL

0130	BANCO LUSO ESPAÑOL SA	11
0048	BANCO SIMEON	11
0089	BANCO DE EXTREMADURA	11
(INSTITUTIONS: 3)		

GRUPO BANKPYME

0142	BANCO DE LA PEQUEÑA Y MEDIANA EM	11
4753	EDAMLEASING	11
8734	MULTIAHORRO	11
(INSTITUTIONS: 3)		

GRUPO BBVA

0182	BANCO BILBAO VIZCAYA ARGENTARIA	11
0009	FINANZIA, BANCO DE CREDITO	11
0035	BBVA PRIVANZA BANCO	11
0057	BANCO DEPOSITARIO BBVA	11
0113	BANCO INDUSTRIAL DE BILBAO	11
0121	BANCO OCCIDENTAL	11
0129	BBVA BANCO DE FINANCIACION	11
0132	BANCO DE PROMOCION DE NEGOCIOS	11
0227	UNOE	11
1004	BANCO DE CREDITO LOCAL DE ESPAÑA	11
8310	SOC.VENTAS CREDITO BANCAYA	11
8321	FINANZIA TRUCKS	11
8908	BBVA FACTORING	11
(INSTITUTIONS: 13)		

GRUPO B.FINANZAS

0186	BANCO DE FINANZAS E INVERSIONES	11
(INSTITUTIONS: 1)		

GRUPO CHASE

0222	THE CHASE MANHATTAN BANK CMB	11
(INSTITUTIONS: 1)		

GRUPO UBS

0226	UBS ESPAÑA	11
(INSTITUTIONS: 1)		

INSTITUTIONS ONLY CONSOLIDATED WITH OTHERS NOT SUBJECT TO BANCO DE ESPAÑA SUPERVISION OR PROPORTIONATELY

0042	BANCO GUIPUZCOANO	11
0061	BANCA MARCH	11
0065	BARCLAYS BANK, S.A.	11
0078	BANCA PUEYO	11
0079	BANCO INVERSION S.A.	11
0112	BANCO URQUIJO	11
0122	CITIBANK ESPAÑA SA	11
0128	BANKINTER	11

0131	BANCO ESPIRITO SANTO S.A.	11
0138	BANKOA	11
0188	BANCO ALCALA	11
0198	BANCO COOPERATIVO ESPAÑOL, SA	11
0200	PRIVAT BANK	11
0211	S.E. BANCA DE NEGOCIOS PROBANCA	11
0217	BANCO HALIFAX HISPANIA	11
1000	INSTITUTO DE CREDITO OFICIAL	11

(INSTITUTIONS: 16)

INSTITUTIONS THAT ARE NOT CONSOLIDATED AND SHOW OWN FUNDS ON AN INDIVIDUAL BASIS

0003	BANCO DE DEPOSITOS
0021	BANCO CONDAL
0031	BANCO ETCHEVARRIA
0123	BANCO DE HUELVA
0125	BANCOFAR
0136	BANCO ARABE ESPAÑOL
0151	THE CHASE MANHATTAN BANK, SUC.
0155	BANCO DO BRASIL
0161	BANKERS TRUST COMP.
0169	BANCO DE LA NACION ARGENTINA
0191	EUROBANK DEL MEDITERRANEO
0214	ARAB BANK, PLC, SUCURSAL ESPAÑA
0219	BANQUE MAROCAINE
0220	BANCO ESFINGE
0223	GENERAL ELECTRIC CAPITAL BANK
0228	BANCO CDC URQUIJO
0232	BANCO INVERSIS NET, S.A.
0233	IBERAGENTES POPULAR BANCA PRIVAD

(INSTITUTIONS: 18)

SAVINGS BANKS

GRUPO CAJA CATALUÑA

2013	CAIXA D ESTALVIS DE CATALUNYA	11
4779	LEASING CATALUNYA	11
8915	FACTORCAT	11

(INSTITUTIONS: 3)

GRUPO M.P. CORDOBA

2024	CAJA DE AHORROS Y MP DE CORDOBA	11
8612	COMERCIANTES REUNIDOS DEL SUR	11

(INSTITUTIONS: 2)

GRUPO CAJA MADRID

2038	CAJA DE AHORROS Y M.P. DE MADRID	11
0099	ALTAE BANCO SA	11

(INSTITUTIONS: 2)

GRUPO CAJA ASTURIAS

2048	CAJA DE AHORROS DE ASTURIAS	11
0115	BANCO LIBERTA, S.A.	11

(INSTITUTIONS: 2)

GRUPO CAJA BALEARES		
2051	CAJA DE AHORROS Y MP DE BALEARES	11
4838	SA NOSTRA DE INVERSIONES	11
(INSTITUTIONS: 2)		
GRUPO CAJA CANTABRIA		
2066	SANTANDER Y CANTABRIA	11
4819	BANCANTABRIA INVERSIONES, SA SAF	11
(INSTITUTIONS: 2)		
GRUPO C.SAN FERNANDO		
2071	CAJA DE AH. PROV. SAN FERNANDO	11
8596	UNION CTO., CREDIFIMO	11
(INSTITUTIONS: 2)		
GRUPO BANCAJA		
2077	BANCAJA	11
0069	BANCO DE MURCIA	11
0093	BANCO DE VALENCIA	11
(INSTITUTIONS: 3)		
GRUPO CAIXA VIGO		
2080	CAIXA DE AFORROS DE VIGO OURENSE	11
0046	BANCO GALLEGO	11
(INSTITUTIONS: 2)		
GRUPO IBERCAJA		
2085	IBERCAJA	11
4832	IBERCAJA LEASING Y FINANCIACION	11
(INSTITUTIONS: 2)		
GRUPO KUTXA		
2095	BILBAO BIZKAIA KUTXA	11
4809	ADEFISA LEASING	11
(INSTITUTIONS: 2)		
GRUPO CAJA PENSIONES		
2100	C.AH.PENSIONES BARCELONA, CAIXA	11
0133	BANCO DE EUROPA	11
4767	CAIXALEASING	11
8209	HIPOTECAIXA	11
8221	CORPORACION HIPOTECARIA MUTUAL	11
8776	FINCONSUM	11
8788	FINANCIACAIXA 2	11
(INSTITUTIONS: 7)		
GRUPO CAJA GUIPUZCOA		
2101	CAJA DE AHORROS Y M.P. DE GUIPUZ	11
0059	BANCO DE MADRID	11
8811	GRUPO DE S. HIPOTECARIOS ON-LINE	11
(INSTITUTIONS: 3)		
GRUPO UNICAJA		
2103	UNICAJA	11
0184	BANCO EUROPEO DE FINANZAS	11
(INSTITUTIONS: 2)		
GRUPO SALAMANCASORIA		
2104	C.A. DE SALAMANCA Y SORIA	11
4782	CREDIDUERO	11
(INSTITUTIONS: 2)		

INSTITUTIONS ONLY CONSOLIDATED WITH OTHERS NOT SUBJECT TO BANCO DE ESPAÑA SUPERVISION OR PROPORTIONATELY

2000	CONFEDERACION ESPAÑOLA DE CAJAS	11
2010	M.P.Y CAJA GENERAL DE BADAJOZ	11
2018	CAJA DE AHORROS MUNICIPAL BURGOS	11
2030	CAIXA D ESTALVIS DE GIRONA	11
2031	CAJA GENERAL DE AHORROS GRANADA	11
2032	CAJA DE AHORRO P. DE GUADALAJARA	11
2037	CAJA DE AHORROS DE LA RIOJA	11
2041	CAIXA D ESTALVIS DE MANRESA	11
2042	CAJA DE AHORROS LAYETANA MATARO	11
2043	CAJA DE AHORROS DE MURCIA	11
2052	INSULAR DE CANARIAS	11
2054	CAJA DE AHORROS Y MP DE NAVARRA	11
2059	CAJA DE AHORROS DE SABADELL	11
2065	CAJA GENERAL AHORROS DE CANARIAS	11
2073	CAIXA D ESTALVIS DE TARRAGONA	11
2074	CAIXA D'ESTALVIS DE TERRASSA	11
2081	CAIXA D ESTALVIS DEL PENEDES	11
2086	CAJA DE AHORROS DE LA INMACULADA	11
2090	CAJA DE AHORROS DEL MEDITERRANEO	11
2091	CAJA DE AHORROS DE GALICIA	11
2094	CAJA DE AHORROS Y M.P. DE AVILA	11
2096	CAJA ESPAÑA	11
2097	CAJA DE AHORROS DE VITORIA-ALAVA	11
2098	M.P.Y CAJA DE A. HUELVA-SEVILLA	11
2105	CAJA DE CASTILLA LA MANCHA	11

(INSTITUTIONS: 25)

INSTITUTIONS THAT ARE NOT CONSOLIDATED AND SHOW OWN FUNDS ON AN INDIVIDUAL BASIS

2017	CIRCULO OBRERO DE BURGOS
2040	CAJA DE AHORROS COMARCAL MANLLEU
2045	ONTINYENT
2056	COLONYA - C.ESTALVIS DE POLLENSA
2069	CAJA DE SEGOVIA
2092	CAJA PROVINCIAL DE JAEN
2099	CAJA DE AHORROS M.P. EXTREMADURA

(INSTITUTIONS: 7)

CREDIT CO-OPERATIVES AND SPECIALISED CREDIT INSTITUTIONS

GRUPO LAB. MONDRAGON

3035	CAJA LABORAL MONDRAGON	11
4788	AROLEASING	11

(INSTITUTIONS: 2)

GRUPO LICO

4713	LICO LEASING	11

(INSTITUTIONS: 1)

GRUPO RENAULT

8345	RENAULT FINANCIACIONES	11
4726	ACCORDIA ESPAÑA E.F.C.	11

(INSTITUTIONS: 2)

GRUPO TARCREDIT

8640	TARCREDIT, E.F.C.	11
4784	TRANSOLVER FINANCE	11

(INSTITUTIONS: 2)

GRUPO PRYCA CONTINEN

8795	FINANCIERA PRYCA	11
8797	SERV. FINANCIEROS CONTINENTE	11
8815	FINANDIA E.F.C.	11

(INSTITUTIONS: 3)

GRUPO SCANIA

8813	SCANIA FINANCE HISPANIA EFC	11

(INSTITUTIONS: 1)

INSTITUTIONS ONLY CONSOLIDATED WITH OTHERS NOT SUBJECT TO BANCO DE ESPAÑA SUPERVISION OR PROPORTIONATELY

3008	CAJA R. DE NAVARRA,SDAD.COOP.CTO	11
3025	CAIXA DE C. DELS ENGINYERS	11
3058	CAJA RURAL INTERMEDITERRANEA	11
3084	CAJA R.VASCA	11
3159	CAIXA POPULAR CAIXA RURAL S COOP	11
3171	CAIXA DELS ADVOCATS-CAJA ABOGADO	11
3172	CAJA CAMINOS, COOP. DE CTO.	11
3183	CAJA DE ARQUITECTOS, COOP.CTO.	11
8807	ARALAR, E.F.C. S.A.	11

(INSTITUTIONS: 9)

INSTITUTIONS THAT ARE NOT CONSOLIDATED AND SHOW OWN FUNDS ON AN INDIVIDUAL BASIS

3001	CAJA R. DE ALMENDRALEJO
3005	CAJA R. CENTRAL
3007	CAJA R. DE GIJON
3009	CAJA R. DE EXTREMADURA
3016	CAJA R. DE SALAMANCA
3017	CAJA R. DE SORIA
3018	CAJA R. S. AGUSTIN FUENTE ALAMO
3020	CAJA R. DE UTRERA
3021	CAJA R. DE ARAGON, COOP. CREDITO
3022	CAJA R. DE FUENTEPELAYO
3023	CAJA R. DE GRANADA
3029	CAJA DE CREDITO DE PETREL
3045	CAIXA RURAL ALTEA
3056	CAJA R. DE ALBACETE
3057	CAJA RURAL ALICANTE
3059	CAJA R. DE ASTURIAS
3060	CAJA R. DE BURGOS
3061	CAJA R. CREDICOOP
3062	CAJA R. DE CIUDAD REAL
3063	CAJA R. DE CORDOBA
3064	CAJA R. DE CUENCA
3067	CAJA R. DE JAEN, COOP.CREDITO
3070	CAIXA RURAL DE LUGO
3076	CAJA R. DE TENERIFE,COOP.CTO.
3078	CAJA RURAL DE SEGOVIA
3080	CAJA R. DE TERUEL, S.C.C.

3081	CAJA R. DE TOLEDO, COOP.CTO.
3082	CAJA R. VALENCIA, S.C.C.
3083	CAJA R. DEL DUERO
3085	CAJA R. DE ZAMORA, COOP.CTO.
3089	BAENA
3093	CAJA R. DEL CAMPO CARIÑENA
3094	CAJA R. VALENCIA CASTELLANA
3095	CAJA R. S. ROQUE DE ALMENARA
3096	CAIXA R. DE L'ALCUDIA
3098	CAJA R. NTRA. SRA. DEL ROSARIO
3102	CAJA R. S. V. FERRER VALL UXO
3104	CAJA R. NTRA. SRA. DEL CAMPO
3105	CAJA DE CREDITO DE CALLOSA
3110	VILLARREAL
3111	CAIXA RURAL LA VALL SAN ISIDRO
3112	CAJA R. S. JOSE DE BURRIANA
3113	CAJA R. S. JOSE DE ALCORA
3114	CAJA R. CASTELLON - SAN ISIDRO
3115	CAJA R. NTRA. MADRE DEL SOL
3116	CAJA R. COMARCAL MOTA DEL CUERVO
3117	CAIXA RURAL D'ALGEMESI
3118	CAJA R. DE TORRENT
3119	CAJA R. S. JAIME ALQUERIAS N.P.
3121	CAJA R. DE CHESTE
3123	CAIXA R. DE TURIS
3127	CAJA R. DE CASAS IBAÑEZ
3128	CAJA R. DE LA RODA
3130	CAJA R. S. JOSE DE ALMAZORA
3134	CAJA R. NTRA. SRA. LA ESPE.ONDA
3135	CAJA R. S. JOSE DE NULES
3137	CAJA R. DE CASINOS
3138	CAJA R. DE BETXI
3140	CAJA R. DE GUISSONA
3144	CAJA R. DE VILLAMALEA
3146	CAJA ESCOLAR DE FOMENTO
3147	CAIXA R. DE BALEARS
3150	CAJA R. DE ALBAL
3152	CAJA R. DE VILLAR ARZOBISPO
3157	CAJA R. LA JUNQUERA DE CHILCHES
3160	CAJA R. S. JOSE DE VILLAVIEJA
3161	CAJA R. S. FORTUNATO CASTELLDANS
3162	CAIXA RURAL BENICARLO
3165	CAJA R. S. ISIDRO DE VILAFAMES
3166	CAJA R. S. ISIDRO DE COV.VINROMA
3169	COBANEXPO-PASAJES
3174	CAIXA RURAL VINAROS, S.COOP.CTO.
3177	CAJA R. DE CANARIAS
3179	CAJA R. DE ALGINET
3181	CAJA DE ELCHE CTO.VAL.
3186	CAJA RR LOS SANTOS DE ALBALAT
3187	CAJA RURAL DEL SUR
3188	CREDIT VALENCIA CAJA RURAL
3189	C.R.ARAGONESA Y DE LOS PIRINEOS
4706	CATERPILLAR FINANCIAL
4709	ING LEASE (ESPAÑA)
4761	IBM FINANCIACION
4789	H. SANTOS
4799	MERCEDES-BENZ LEASING
8219	PRAGA HIPOTECAS Y CREDITOS
8233	AHORROGESTION HIPOTECARIO
8234	A.I.G. FINANZAS

8235	BILBAO HIPOTECARIA
8240	CREDITER
8307	VOLKSWAGEN FINANCE, SA
8308	FINANCIERA CARRION
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8778	XEROX DE FINANCIACION
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8805	FINANCIERA EL CORTE INGLES
8806	VFS FINANCIAL SERVICES SPAIN
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