

Recent key developments in the area of Spanish financial regulation

Prepared by the Regulation and Research Department of the Spanish Confederation of Savings Banks (CECA)

Bank of Spain Circular amending the Accounting circular (Circular 1/2014, published in the State Official Gazette (BOE) on February 5th, 2014)

This Circular aims to fulfil the provisions of Law 8/2012, October 30th, 2012, on the writing down and sale of the financial sector's property assets, as regards the adoption of measures for the allocation, to those assets the Bank of Spain so determines, of the **outstanding balance of the coverage set aside for lending relating to the real estate promotion and construction business in Spain, classified as normal risk on December 31st, 2011, which had not subsequently been applied as a result of a later reclassification (doubtful or substandard assets) or due to foreclosure or receipt of assets in settlement of debts.**

The main features of the Circular are:

- Institutions are to submit a report to the Bank of Spain with a breakdown of the amount set aside to cover normal risks and the amounts used as of December 31st, 2013, along with an analysis of the reasons for which the remaining balance corresponds to risks classified as normal at year-end 2013.

- The remaining balance will be credited as a recovery of unused provisions made and simultaneously an identical amount will be debited to cover or write-down the following assets: (i) financial assets classified as doubtful and real estate assets for which the minimum coverage is insufficient, and (ii) financial assets relating to investments in equity instruments not traded on organised markets in companies whose business is linked to the property sector.
- Certain statements have been eliminated from the Accounting circular (Bank of Spain Circular 4/2004, December 22nd, 2004, on public and confidential financial reporting rules, and standard formats for financial statements).

Bank of Spain Circular on the exercise of various regulatory options contained in the Capital Requirements Regulation (Circular 2/2014, published in the BOE on February 5th, 2014)

Royal Decree-Law 14/2013, November 19th, 2013, on urgent measures to adapt Spanish law to European Union standards on the supervision and solvency of financial institutions, adapted Spanish legislation to the essential regulatory changes for the European standards on capital requirements known as CRR/CRD IV¹ to be operational as

¹ Regulation 575/2013 of the European Parliament and the Council, June 26th, 2013, on prudential requirements for credit institutions and investment firms, amending Regulation (EU) No 648/2012 (CRR) and Directive 2013/36/EU of the European Parliament and of the Council of June 26th, 2013, on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD IV).

soon as they came into effect on January 1st, 2014. It also authorised the Bank of Spain, as the competent authority, to use the options assigned to it in the CRR.

To this end, Circular 2/2014 was published, **which determined what option and with what scope, with national discretionary powers, consolidated groups of credit institutions and Spanish credit institutions, whether forming part of a consolidated group or not, will be required to comply with.** Specifically, it referred to the national discretionary powers over capital requirements, leaving those concerning the capital ratio denominator (risk-weighted exposures) for subsequent implementation.

■ The following **general points** stand out:

- In the case of holdings of equity instruments in a financial sector entity, the Bank of Spain may authorise entities to not deduct them from their equity in exchange for their being subject to the applicable credit risk weighting (IRB or standard method). In the case of qualified holdings in non-financial entities, the weighting is 1,250%.
- Under the CRR, entities may apply **exemptions to compliance with the limits on their large exposures** until the relevant legislation comes into effect or until December 31st, 2028. Nevertheless, making use of national discretion, the exemption will be for the full amount except in the case of certain exposures for which it will be 50%.

■ As regards the **transitional arrangements**:

- The Bank of Spain has not used its national discretionary powers to apply shorter intervals for the capital ratios, as between January 1st,

2014, and December 31st, 2014, entities will be required to maintain a common equity Tier 1 (CET1) ratio of 4.5% and a Tier 1 capital ratio of 6%.

- The percentages established by the Bank of Spain for the application of prudential filters regarding losses and gains valued at fair value during the transitional period (from January 1st, 2014 to December 31st, 2017) are less demanding than those provided in the CRR.
 - ✓ For losses, 20% in the first year, and gradual increases up to December 31st, 2017, and for gains, 100% the first year, with gradual decrements until December 31st, 2017.
 - ✓ Moreover, during this period, entities will exclude from their equity 100% of the gains or losses measured at fair value arising from derivative liabilities and the results of changes in the entity's own credit standing.
- The transitional treatment of CET1 deductions (between January 1st, 2014 and December 31st, 2017) will not be applicable to certain items, which will be deducted in full.² For all other elements, the percentages applicable to the CET1 item deductions during the transitional period are less demanding than those provided under CRR.
 - ✓ 20% the first year, with gradual increments up to December 31st, 2017.
 - ✓ In the case of tax assets depending on future earnings, and which existed prior to January 1st, 2014, it will be 0% the first year, with increments of 10% a year up until December 31st, 2017.
- The Bank of Spain may authorise (between

² (i) Losses from the current year, (ii) certain intangible assets, (iii) own instruments of the CET1 held by an entity that has real or contingent obligations to acquire these instruments under a contractual commitment in force, and (iv) CET1 instruments of financial sector entities when an entity has a cross holding that, in the opinion of the competent authority, is destined to artificially inflate the entity's own funds.

January 1st, 2014, and December 31st, 2022) entities that, following an application stating their reasons, accredit that certain conditions have been met, to not deduce holdings in the capital of insurance companies, reinsurance companies and insurance portfolio companies. In such cases, a risk weight of 370% will be assigned.

- It also envisages provisions for the items eligible, prior to the CRR, as consolidable reserves or similar that do not meet the new conditions to be eligible as CET1.

- The circular repeals Bank of Spain Circular 7/2012 of November 30th, 2012, on minimum core capital requirements.

Order adopting exemptions from certain technical and business requirements for transfers and direct debits in euros applicable until February 1st, 2016 (Order ECC 243/2014, published in the BOE on February 22nd, 2014)

Regulation (EU) No 260/2012 of the European Parliament and of the Council of March 14th, 2012, establishing technical and business requirements for credit transfers and direct debits in euro, forms part of the European legislation on payment services to promote the **SEPA** (Single Euro Payments Area) project, which aims to create a single internal market for euro payment services, in which cross-border payments within the European Union are to be treated in the same way as domestic payments. This is expected to save money and yield advantages for the wider European economy. This Regulation sets February 1st, 2014, as the deadline for migration of transfers and direct debits to SEPA, and introduces a series of mandatory common rules and technical requirements for payments made after that date. At the same time, it gives Member States the option to adopt some or all of

the exemptions allowing application of the rules concerning certain technical requirements or products to be deferred.

In the case of **Spain**, the adoption of the community options will facilitate adaptation to the technical requirements required to achieve effective migration to SEPA within the deadlines set, and the most appropriate and prudent treatment of those products of greatest interest and operational complexity.

Up until February 1st, 2016, payment service providers will have the following commitments:

- They may offer retail customers free BBAN to IBAN conversion services for domestic operations only, and must provide customers with the IBAN code prior to the transaction.
- They must guarantee interoperability by converting payer and payee BBANs to IBANs using secure technical means.
- They may not charge retail payment service users any fees or commissions directly or indirectly related to these conversion services.
- They must inform users of the characteristics of the new service, and the consequences of the conversion.

Similarly, up until February 1st, 2016, compliance with certain requirements of transfers and direct debits will not be required in the case of transactions conducted with credit advances referred to in Notebook 58 of the series of banking procedures and rules and with bills included in Notebook 32 of the series of banking procedures and rules.

In relation to the formats of messages used in their communications with payment service suppliers, payment service users are not required to use standard ISO 20022 until February 1st, 2016.

