

# 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)

## National Securities Market Commission (CNMV) Circular on requirements for internal organisation and control functions in entities providing investment services (Circular 1/2014, published in the BOE on April 3<sup>rd</sup>, 2014)

The Circular primarily includes measures affecting the compliance function in credit institutions providing investment services. In broad terms, the main features of this regulation are:

- Its **scope** includes Spanish investment firms and EU investment firms operating in Spain, credit institutions, branches of credit institutions and investment firms from Member States of the European Union, and agents established in Spain acting for entities incorporated in other EU countries.
- The **administrative or management body** of entities providing investment services will be responsible for establishing and maintaining an appropriate organisational structure and implementing the internal organisation requirements, which include the requirement that a unit performing the regulatory compliance function be set up and maintained.
- The **tasks** that units performing regulatory compliance, risk management, and internal audit functions **are to carry out**, and their obligations regarding reporting to senior management and the CNMV are set out.

- The requirements applicable to the **delegation of control** functions are addressed, and entities are required to have internal manuals setting out the policies and procedures established. These manuals must be made available to the CNMV.

CNMV Circular 3/2013 of June 12<sup>th</sup>, 2013, on the implementation of certain obligations to provide information to investment services clients, in relation to the assessment of the suitability of financial instruments, has also been amended. In particular its scope has been narrowed such that it is **no longer applicable to certain professional clients**. Entities do not need to obtain a handwritten statement when conducting transactions with clients of this type.

The Circular is applicable to **credit institutions** in so far as they provide investment services or auxiliary services, and solely with regard to the scope of these services, while bearing in mind their nature, scale and complexity. Specifically, the Circular's provisions on **internal organisation requirements** are applicable to credit institutions operating in Spain. Consequently, the sixth (risk management function), seventh (internal audit function), eighth (delegation of control functions and other obligations) and ninth (limits to scope of application) rules are not applicable.

Therefore, credit institutions providing investment services are mainly affected by the **measures concerning the compliance function**.

The regulation establishes that entities providing investment services must **adapt their structure**

to the Circular's requirements by **December 31<sup>st</sup>, 2014**.

Finally, CNMV **Circular 1/1998**, of June 10<sup>th</sup> 1998, on internal systems for the ongoing risk control, monitoring and assessment, is repealed.

### **Royal Decree-Law adopting urgent measures on the refinancing and restructuring of corporate debt (Royal Decree-Law 4/2014, published in the BOE on March 8<sup>th</sup>, 2014)**

This Royal Decree-Law aims to help companies clean up their balance sheets and return to financial health, such that their remaining debt is sustainable, so as to allow companies to meet their commitments in the course of trade. It also introduces mechanisms whereby debt can be converted into capital. As a consequence, the Royal Decree-Law makes improvements to the legal framework for pre-bankruptcy refinancing agreements, amending Law 22/2003 of July 9<sup>th</sup>, 2003, on Bankruptcy (referred to here as the Bankruptcy Law).

#### **1. Amendments to the Bankruptcy Law**

- Submission of a **notice of commencement of negotiations** towards a refinancing agreement is sufficient to suspend the court's awarding of assets necessary for the continuation of the debtor's professional or business activity as settlement of debts during the envisaged duration of the negotiations.

**Individual claim proceedings** by creditors holding financial liabilities may not be commenced or shall be suspended, provided that holders of not less than 51% of the financial liabilities are accredited to expressly support the negotiations towards the signing of the refinancing agreement, with the undertaking not to begin or continue individual claims against the debtor while negotiations are under way.

- Proceedings to recover shares or holdings in companies solely engaged in the holding of an asset or liability necessary for its financing are excluded from the **suspension of claims against collateral backed assets**, such that this suspension is limited to those assets that are necessary for the continuation of the debtor's professional or business activity.
- The **requirement for an independent expert report is eliminated**, it being replaced by a certificate accrediting that the majority required for adoption has been obtained. However, both the debtor and the creditors may request the **appointment of an independent expert** to report on the feasibility plan, the proportionality of the guarantees, or any other circumstances.
- A new category of **refinancing agreements that are deemed irrevocable**, subject to certain conditions, has been introduced. Court-approved financing agreements are also deemed irrevocable.
- **Legitimacy** for proceedings to challenge an agreement remains limited to the receiver in bankruptcy and may only apply in the absence of the conditions stipulated in the regulations. Other legal challenges are also limited to the receiver in bankruptcy.
- As a means of creating incentives for new financing, **all new cash inflows** are given the status of **credit with a claim against the estate**, including those from a refinancing agreement and cash flows from the debtor or closely related parties, excluding capital increases. This measure has been adopted on a **temporary and extraordinary basis** for all new cash inflows taking place in the two years following the entry into force of the Royal Decree-Law.

- It is envisaged that parties becoming shareholders as a result of the conversion of debt into capital through a refinancing operation

should not be considered **closely related parties** for the purposes of classifying the financing granted as a result of this operation as subordinated.

Similarly, creditors who have signed the refinancing agreement for obligations assumed by the debtor in relation to the feasibility plan **shall not be considered de facto directors**.

- In order to encourage the **transformation of debt into capital**, a new case is added in which **fraud or gross negligence** is presumed when the debtor refuses, without good cause, to capitalise credits, securities issues, or convertible instruments, thereby hampering the achievement of a refinancing agreement.
- A **revision of the system of court approval of refinancing agreements** has been undertaken, whereby the scope of application is expanded to include all types of financial liabilities, excluding creditors for commercial operations and creditors for public liabilities.

The extension to **dissenting creditors** (those who have not signed the refinancing agreement or have stated their disagreement with it) of **moratoriums** is enabled, and, with a greater percentage of liabilities, of other measures agreed within the refinancing agreement, as is the case of **haircuts, debt-equity swaps, and transfers of assets** in/for payment of debt.

The possibility of extending the effects of the agreement to certain creditors with collateral is envisaged and the **approval procedure has been simplified** such that the court hears the application directly. In order not to undermine the value of the guarantee in the event of default by the debtor, special rules have been established allocating the remainder to the creditor.

In addition, a measure has been established to avoid the overweighting of certain minority shareholdings in **syndicated financing**

**agreements**, defining a limit on the percentage of votes in favour in the syndicate in the case of an overall refinancing agreement for the debtor.

## 2. Other provisions

- The Bank of Spain is authorised to establish and publish uniform criteria for the **classification of restructured operations** resulting from refinancing agreements **as normal risk**, within a period of one month.
- **Transitional arrangements:** in the case of refinancing agreements that are being negotiated at the time this Royal Decree-Law comes into force, the previous rules shall be applicable if the debtor has already applied to the mercantile registrar for the appointment of an **independent expert**, unless the parties opt for the same in the refinancing agreement.
- Other rules, such as the Code of Civil Procedure or various tax rules, have also been modified.

## Draft Bill of a law to promote corporate finance

On March 5<sup>th</sup>, the Government published the draft bill for a law to promote corporate finance, containing a series of measures to enhance access and flexibility of bank finance for SMEs and stimulate a recovery of bank credit. It also incorporates measures to promote the development of alternative means of financing.

Broadly, the text regulates the following points:

- **Credit institutions are required to give** at least three months **advance notice** and specific information on the credit status of those SMEs whose financing is due to be cancelled or substantially reduced.
- **The functioning of mutual guarantee societies is to be enhanced** through the capitalisation

vis-à-vis the creditor of the reguarantee of the Compañía Española de Reafianzamiento, in the case of default by the mutual guarantee society on first demand. Additionally, to bolster these companies' management, professionalism and good governance, the requirements of good repute, knowledge and experience applicable to directors of credit institutions will extend to them.

- The bill adapts the **legal framework applicable to finance companies** as a result of their loss of the status of credit institutions under CRR and CRD IV. The aim is to provide these entities with a more effective legal framework so as to maintain and promote their activity, which is geared towards corporate and consumer finance through alternative channels to the banks.

- Three-pronged **improvement to securitisation regulations**: firstly, unifying the regulatory dispersion on the subject to ensure consistency; secondly, bringing Spain's legal framework closer to that of neighbouring countries; and, finally, offering maximum legal security and legal support to customary operations in the securitisation area, strengthening requirements in terms of transparency and investor protection.

- **Promoting the operation of the alternative stock market** (MAB), by facilitating the transition of companies listed on the stock exchange to this alternative trading platform. To do so, the requirement to submit an offer for the delisting of the company will be replaced by a less burdensome procedure, guaranteeing adequate protection of minority shareholders.

- The **bond issue system** will be improved, with the introduction of a variety of company regulation measures to facilitate Spanish companies' direct access to debt markets by lifting issue limits.

- Participatory financing platforms known as "**crowdfunding**" are being regulated in Spain for the first time. The aim is to regulate this

phenomenon, already present in neighbouring countries, whereby investors and projects seeking funding are put in direct contact with one another via electronic platforms. The objective is to promote this new tool for direct financing of business projects in their early stages of development, while protecting investors. To this end, these platforms are required to be transparent and to provide investors with adequate information. Limits are also set on individual investors' investments per project of 3,000 euros and per platform of 6,000 euros a year.

This bill is currently being debated in parliament, so may undergo amendments.