

Recent reforms in Spain's business climate: Assessment and pending issues

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The Spanish government has actively pursued a structural reform agenda since 2012. While notable progress has been made in some areas, such as improving the insolvency regime, reforms in other key areas have yet to be adopted, or in some cases, seem insufficient to address existing challenges.

The Spanish government has adopted a number of structural reforms aimed to improve the business climate since 2012. The most significant progress has been made with the reform of the insolvency regime, which has improved the risk sharing balance between creditors and debtors and includes new provisions for personal insolvency. In contrast, not enough has been done to reform professional services – despite commitments from the past two administrations. In the remaining policy areas, progress has been mixed. Reform of the competition and regulatory authorities offers some prospects of improved decision-making. However, the changes raise concerns over the independence and accountability of the new regime. In the area of entrepreneurship, the Government has focused efforts on reducing start-up costs, but still lacks a comprehensive strategy. Finally, there have been some market specific reforms in the electricity sector and reforms to increase openness and competition in the management of railways and airports, but it is not yet clear that these reforms will be sufficient to address pending issues.

Introduction

Optimal business climate regulation is an essential condition for companies and countries to prosper. In the EU/Euro Area context, where countries have transferred monetary sovereignty to the European Central Bank and domestic fiscal policy is increasingly under greater EU supervision, structural reforms remain one of few major areas of economic policy under domestic discretionary power. For this reason, it is important to examine

whether there has been adequate progress on this front.

In November 2011, following Spain's general elections, there was a change in the central government, which many viewed as an opportunity to introduce bold, pro-competitive changes in the main lines of business climate regulation. Now, just a few months before the end of the four-year term, it seems appropriate to look at the progress achieved since the beginning of 2012, as well as at the main pending reforms.

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In this context, this paper focuses on regulatory (*i.e.* legal modifications) in the following five policy areas: entrepreneurship, competition enforcement, regulation of product and service markets, the insolvency regime and professional services.

Monitoring progress on reforming Spain's business climate

Scope of policy reform

The scope for policy reform is very large and therefore one needs to work with a certain conceptual structure to single out which policy issues are included in the analysis. In an effort to

do so, this paper follows the methodology of the *Spanish Reforms* project.² This project classifies economic policy into six broad areas, which in turn are divided into 18 policy subareas (see Table 1).

This classification was designed to be compatible with those that appear in the Spanish National Reform Programs (NRP) and in the main economic policy documents prepared by major international economic institutions (the European Commission, the IMF and the OECD).

On the basis of this classification, it is possible to select five policy areas that are more closely related to business climate policy reforms. These are presented in Table 2 and they will be covered in detail in the following section:

Table 1

Classification of economic policy areas (*Spanish Reforms* nomenclature for policy areas and subareas)

Area	Subarea
1. GROWTH AND COMPETITIVENESS	1.1. R&D and the knowledge society 1.2. Internationalization 1.3. Entrepreneurship 1.4. Education
2. COMPETITION AND REGULATION	2.1. Competition enforcement 2.2. Regulation of product and service markets 2.3. Red tape and business climate regulation, including the insolvency law 2.4. Professional services
3. LABOUR MARKET	3.1. Labour market regulations 3.2. Active labour market policies
4. FINANCIAL SYSTEM	4.1. Recapitalization and Restructuring 4.2. Other financial measures
5. FISCAL POLICY AND PUBLIC ADMINISTRATION	5.1. Economic governance 5.2. Fiscal consolidation and fiscal reform 5.3. Reform of the public administration
6. WELFARE STATE	6.1. Social Security and pensions 6.2. Health system 6.3. Other welfare state reforms

Source: *SpanishReforms project*.

² *Spanish Reforms* is an academic, non-governmental project that aims to be a useful reference for those interested in independent, rigorous and up-to-date information about the Spanish economy and its economic policy reforms. The main element of the project is a webpage (<http://www.spanishreforms.com>) that regularly monitors progress on the economic reforms adopted by the Spanish government, as well as provides analysis of the Spanish economy undertaken by the major international institutions. *Spanish Reforms* is an initiative of the Public-Private Sector Research Center (PPSRC) at IESE Business School and it has as partners FUNCAS, Evers and ESCI-UPF.

Table 2

Main business climate reforms passed and in force since 2012, by policy area
(Spanish Reforms nomenclature for policy subareas)

Policy subarea	Policy reform
Entrepreneurship	<ul style="list-style-type: none"> ■ Royal Decree Law 4/2013 on entrepreneurship and job creation. February 22nd, 2013. ■ Law 14/2013 on entrepreneurship and internationalization. September 28th, 2013. ■ Royal Decree Law 3/2014 on employment and permanent hiring. March 1st, 2014.
Competition enforcement	<ul style="list-style-type: none"> ■ Law 3/2013 on the Creation of the National Markets and Competition Commission (CNMC), June 4th, 2013.
Regulation of product and service markets	<ul style="list-style-type: none"> ■ Law 20/2013 on the Spanish single market. December 9th, 2013. ■ Law 24/2013 on the Electric Sector. December 27th, 2013. ■ Reforms in Passenger Railway Sector and the Airport Operator. June 13th, 2014.
Insolvency law	<ul style="list-style-type: none"> ■ Royal Decree Law 4/2014 refinancing and restructuring of corporate debt, March 7th, 2014. ■ Royal Decree Law 11/2014 on urgent insolvency measures. September 5th, 2014. ■ Law 17/2014 on refinancing and restructuring of corporate debt (modifies RDL 4/2014). September 30th, 2014. ■ Royal Decree Law 1/2015 on fresh start mechanism. February 28th, 2015.
Professional services	None. ^(*)

Note (): Recent reforms prompted by the transposition of the EU services directive to Spanish law have improved how professional services operate in Spain. However, further action is needed to remove existing guidelines, as well as improve the functioning of professional associations themselves, in order to increase the efficacy of the reforms (Spanish Economic and Financial Outlook 2014).*

Source: SpanishReforms project.

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| <ol style="list-style-type: none"> 1. Entrepreneurship 2. Competition enforcement 3. Regulation of product and service markets 4. The insolvency law 5. Professional services | <p>here. Some of the most important ones are listed below and, for each one, there is a brief mention of the main developments since 2012.</p> <ul style="list-style-type: none"> ■ Labour market reform. The Spanish government introduced major changes to labour market regulation in three dimensions: i) collective bargaining, making it easier for firms to opt-out from higher-level agreements; ii) internal flexibility, removing obstacles to, or protection from, functional changes within the company; and, iii) contract design, reducing the severance pay for existing contracts and introducing new types of contracts for entrepreneurs that allow |
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This selection is obviously subjective in nature and it is fair to mention that there are other important policy dimensions that might be relevant for the business climate and that are not covered in detail

for firing without severance payment for the first year. It is still too soon to make a comprehensive assessment of the reform. The OECD (OECD, 2013), in a preliminary assessment, finds that the reform has contributed to wage moderation and fostered hiring on permanent contracts. The main concern, however, is the macroeconomic impact the reform may have on the disposable income of low-skilled workers and the extension of poverty in Spain.

- *Financial sector reform.* There has been an intense reform agenda since 2009 along the lines of clean-up and recapitalization. The 2014 ECB Comprehensive Assessment has examined 15 Spanish banks, accounting for 90% of the assets of the Spanish financial system and only one of those has been found to have a significant capital shortfall.
- *Suppliers' payment system.* The Spanish government set up in 2012, in conjunction with the new Budget Sustainability Law, a new scheme to provide liquidity to suppliers of local and regional governments (FFPP). The funding of this programme between 2012 and 2014 (when it was closed) has amounted to more than 42 billion euros.

Adopted reforms

Table 2 reports the main legal reforms in the five policy areas mentioned above that the Spanish government has approved and that are already in force. The main changes in the Spanish business climate as a result of these reforms are explained below.

Entrepreneurship

The main approach of the Spanish government in supporting entrepreneurship has been basically seeking cost reductions for start-ups. For instance, one of the main measures in RDL 4/2013 was a drastic reduction in the amount of social contributions a young entrepreneur

needs to pay, down from the previous amount of 256 euros per month to 50 euros per month. In the same vein, Law 14/2013 introduced mild reforms in the regulations of entrepreneurship, with several ad-hoc measures, like the creation of a special VAT regime, R&D tax subsidies and a new legal status for entrepreneurs with limited liability aimed at facilitating fresh-start. Along the same line of cost-saving, RDL 3/2014 reduces the social security contribution that companies pay when hiring new workers on permanent contracts. In particular, if a company hires a worker with a permanent contract and this increases both the total employment and the number of workers with permanent contracts in the company, the social security contributions payable by the firm are limited to 100 euros per month.

However, this sort of “low cost” model for stimulating entrepreneurship contrasts with the international mainstream approach, which tends to be more ambitious, structural and comprehensive. International policy best practices in favour of entrepreneurs and young SMEs tend to be linked to internationalization and innovation. They pay particular attention to facilitate companies' high-growth and they try to make sure that the overall business climate is competition-friendly (see OECD 2014 for a review of the situation in Spain in relative terms to other OECD countries).

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Competition enforcement

The reform of the Competition Authority and the Sector Regulatory Bodies has been a long-standing issue in Spain since 2011. The current and the previous Spanish governments included in

the corresponding National Reform Programmes successive commitments to reform the institutional framework of regulatory and competition systems in Spain. Finally, Law 3/2013, creating the CNMC, entered into force in June 2013. The new Commission integrates the function of the former Competition Commission (CNC), together with those of all the regulatory authorities in Spain, except the Financial Sector Regulator. The new authority became fully operational in October 2013 and in November, new Director Generals were appointed.

One of the main concerns with the reform is that it might have been taken by the Government as an opportunity to devolve some regulatory and competition competences back to the Ministries in detriment to the independent bodies (the CNC and the sector regulators). There have even been formal calls from the European Commission to the Spanish government to preserve the independence of the new macro regulatory and competition authority. At present, the degree of independence and accountability of the CNMC

The new Commission (CNMC) integrates the function of the former Competition Commission (CNC), together with those of all the regulatory authorities in Spain, except the Financial Sector Regulator. At present, the degree of independence and accountability of the CNMC remains yet to be established.

remains yet to be established. Finally, in terms of staffing, it appears that the reform has not changed the common practice of relying mainly on civil servants to fill key positions. As a result, prominent lawyers and business executives, as well as distinguished academics, have to date not had access to the board of the new CNMC (see Xifré 2014 for a more detailed account of the CNMC reform).

Regulation of product and service markets

Single market law

The Spanish Constitution establishes that no Spanish public administration is allowed to adopt measures that, directly or indirectly, impede the free movement of people and goods in Spain or that represent an obstacle to setting up a new business. The country, as the Constitution establishes, is administratively organized as a relatively decentralized state with some regulatory competences being attributed to regional governments or local authorities. As a result, the possibility of formally regulating market unity in Spain (*i.e.* explicitly removing barriers to the operation and the setting-up of business) has been a highly politically-loaded issue for a long time.

Law 20/2013 on the Spanish Single Market seeks to reduce the alleged market segmentation in Spain and to allow Spanish companies to profit from economies of scale. To do so, the core of the Law establishes the principle that any business entity (or good) operating (or being distributed) in one part of Spain shall be entitled to move to another part without further restrictions. The Law also includes requirements on how authorization permits shall work all over Spain, independently of the level of the administration (central, regional, local) in charge of granting the permit.

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competencies and legislative powers attributed by the Spanish Constitution to sub central (regional and local) governments and the need to protect the Spanish single market. Should this “loyalty between administrations” principle be violated, the law would be exposed to a high risk of being overturned. In this respect, the Catalan government has challenged the law before Spain’s Constitutional Court on the ground that it invades regional legal competences granted by the Constitution.

Product and service markets

Since 2012, there have been major changes in two markets: the electric sector and passenger transportation (railways and airports).

Electricity

The Government approved in December 2013, Law 24/2013 on the Electric Sector, which introduced a “flexible” model in the remuneration of, mainly, renewable energies subject to revision every six years with the final goal of cutting payments to this market segment. The Law mandates that the electricity system revenues will be sufficient to cover all the costs; therefore, an increase of costs in the system or a reduction in revenues (due to decreased demand from companies and households) shall entail a reduction in payments to operators. In addition, the Law introduces a compulsory toll on self-consumption (*i.e.*, users of the system that generate part of the electricity they consume) and creates a voluntary price regime for small consumers that could replace the old last-resort tariff (TUR).

The prevailing view is that the Law on the Electric Sector can probably already be viewed as insufficient to tackle the problems of the electricity tariff system. Indeed, the same week that the Law was finally approved by the Spanish parliament, the Government announced that it would modify

the current electricity price setting mechanism, which the new Law endorsed.

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Transportation

The Spanish government announced in June 2014 the initiation of two separate processes that should improve the functioning of the transport market and open it to private sector participation.

In the railway system, the Government will allow a private operator to provide passenger railway services, in competition with the public one (Renfe). The new operator shall set freely travel times, prices and it will have the right to rent the rolling stock from a Renfe subsidiary. There will be an initial term of seven years for this license; following this term, the corridor will be fully opened up to free competition. With respect to the airport operator (AENA), the Government allowed private capital to enter the company. In February 2015, the company went public with the Government retaining 51% of the capital.

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of passenger transport affects only one relatively small segment of the network. Furthermore, the real bottleneck for railway transport in Spain,

freight transportation, appears not to be on the Government's reform agenda. Regarding the privatization of AENA, some experts consider that the real possibility for the Spanish airport system to grow and generate added value depends not so much on the nature of ownership (private or public) but on the mode of management (centrally organized vs. competition-driven). The reform proposed by the Government makes no progress on this second dimension.

The insolvency law

In this area, there have been a large number of changes since 2012. Back in 2009, the reforms began by extending the scope for the simplified insolvency procedures, reducing their costs and simplifying the pre-insolvency procedures. This has been one of the reform avenues post 2012, in particular by means of RDL 4/2014, RDL 11/2014 and Law 17/2014. RDL 4/2014 extended the available options for restructuring in pre-insolvency procedures. RDL 11/2014 (modified later on by Law 17/2014) revised in-court debt restructuring procedures and offered options to promote liquidation as an integrated solution rather than piecemeal liquidation. Finally, a recent reform, RDL 1/2015 introduced the possibility of a

The need to establish legal provisions for a fresh start for individuals was one of the strongest recommendations by international organizations. While assessment of the new insolvency reforms is difficult, there appears to be a consensus that they incentivize creditors to absorb more risk in business operations.

fresh start for individuals under certain limitations and when certain circumstances apply. The need to establish legal provisions for a fresh start for individuals was one of the strongest recommendations that international organizations made to the Spanish government (see IMF, 2014).

Assessment of these insolvency reforms is difficult. The original insolvency Law, passed in 2003, has been amended by 12 reforms since then and interpretations are probably not yet final. However, there appears to be a consensus that, in essence, the reforms allow –and provide appropriate incentives– for creditors to absorb more risk in business operations. Given that the Spanish insolvency law is strongly biased in favour of creditors, the reforms appear to set the rules for a more even playing field (see Celentani and Gómez, 2014 for an extended analysis).

Professional services

There have been multiple calls from international institutions to reform the professional services regulations in Spain, for instance, one of the last ones by the IMF (2014) and the European Commission (2014b). These recommendations in general agree on the direction of the change: the number of professions that require compulsory registration requirements should be reduced and the transparency and accountability of professional bodies should improve with the overarching goal of opening up unjustifiably reserved activities in Spain. According to the Spanish government, this sector of activity concentrates 30% of graduate employment in Spain.

On the actual policy front, the Spanish government released a draft reform of the professional services law in August 2013, but since then there has been no progress and therefore the regulation of professional services remains without changes and it is most likely to remain this way until the end of the current administration. The delay is in part due to the pressures and lobbying efforts that various interest groups potentially affected by the new regulations (engineers of various fields –in some case with conflicts between fields–, architects, lawyers, pharmacists, etc.) have exerted against the reform. It is only fair to say, however, that the previous Spanish government also made an attempt to liberalize this sector of

activity but it was also unable to do so in the end. The Spanish competition authority (CNMC) issued an assessment of the draft reform and it produced an exhaustive and comprehensive analysis of the situation (CNMC, 2013).

Reforms in the pipeline

In addition to the above reforms, the Government has approved a few more which are still in the legislative pipeline and that, in principle, should be in force by the end of the legislature. Table 3 outlines these reforms, which are focused on further improving the framework for entrepreneurship in Spain.

The text of the new laws is not yet finished as amendments can be introduced during the legislative procedure and therefore it is not possible to assess them. However, the main orientation of the two reforms pending approval is to improve business financing and to streamline the functioning of the one-stop service points for entrepreneurs.

Regarding the new law to improve business financing, there is a publicly available draft which

was approved by the Congress in January 2015. On the basis of this tentative text, the law will advance on two fronts: on the one hand, making banking financing more flexible and feasible for companies and on the other hand, establishing the regulatory fundamentals to further develop non-banking (or direct) business finance by means of alternative markets.

The new law to improve business finance will advance on two fronts: on the one hand, making banking financing more flexible and feasible for companies and on the other hand, establishing the regulatory fundamentals to further develop non-banking business finance by means of alternative markets.

With respect to the plans for streamlining the one-stop service points for start-ups, the draft text of the RDL has not yet been submitted to the Congress. In its current form, it is basically a development of Law 14/2013 and it establishes that the network to support early business developers will be a single

Table 3

Main business climate reforms initiated since 2012 by policy area, approved but not yet in force (Spanish Reforms nomenclature for policy subareas)

Policy subarea	Policy reform	Last milestone accomplished	Next step
Entrepreneurship	■ Draft Law for the promotion of the Business Financing.	Approved by the Congress. January, 2015.	Approval by the Senate pending.
	■ Draft Royal Decree Law for streamlining one-stop service points for entrepreneurs.	Draft presented by Government. February 2015.	Discussion in the Parliament.
Competition enforcement	None.		
Regulation of product and service markets	None.		
Insolvency Law	None.		
Professional services	None.		

Source: SpanishReforms project.

one in Spain, with the same name, corporate image, and portfolio of services in the territory.

Assessment and conclusion

The Spanish government has been active in reforming the business climate with part of the motivation for doing so resulting from the recommendations by international organizations like the European Commission and the IMF. These reforms, usually referred to as structural reforms, have been stronger in certain policy areas than others (see European Commission, 2014a).

The reform agenda of the Spanish government has been particularly ambitious regarding the insolvency regime. On this issue, the Government has adopted a large number of the main recommendations proposed by the international institutions. The resulting insolvency law, which has been frequently amended since its inception in 2003, is likely to strike a better balance between the risks that creditors and debtors take, which represents much-needed progress in Spain.

On the contrary, the Government has not done enough regarding the modernization of the professional service sector, where international recommendations are equally clear and coherent. In this dimension, there has been little progress in the last four years. To aggravate the issue, the performance of the previous Spanish government, of a different political orientation, was similar in that it tried but did not succeed in approval of legislation due to its politically sensitive nature.

Between these two extremes, the reform outcome in the other main elements of business climate is mixed. The reform of the competition and regulatory authorities is imperfect, as it is not clear that the new mega-regulator (CNMC) represents an improvement on the previous architecture, as regards independence and technical ability. The efforts to enhance entrepreneurship appear to be headed towards cost reduction rather than pursuing a comprehensive, ambitious and truly

structural reform. On the regulation of product and service markets, there have been some important positive steps ahead to open certain sectors to the entry of private capital, but the airport model still remains too centrally organized.

Overall, the reforms of Spain's business climate appear not to have the caliber that the country's difficult situation demands. A worrisome conclusion, given that structural reforms are likely to be one of the last policy areas for governments to exert their national economic sovereignty.

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