Recent key developments in the area of Spanish financial regulation

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Royal Decree implementing the Law on regulation, supervision and solvency (Royal Decree 84/2015, published in the official gazette on February 14th, 2015)

Royal Decree 84/2015, of February 13th, 2015, implementing Law 10/2014 of June 26th, 2014, on the regulation, supervision and solvency of credit institutions (hereinafter, RD 84/2015), completes the implementation of Law 10/2014 and consolidates the rules on the regulation and discipline of credit institutions in a single text. The Royal Decree also forms part of the transposition of Directive 2013/36/EU (CRD IV).

The **main features** of RD 84/2015 are:

1. Measures concerning authorisation, registration and activity

- The authorisation arrangements are limited to **banks**, while savings banks and credit unions will be governed by their own specific regulations.

- The RD establishes the **requirements** to be met in order to **conduct banking business.** These include: (i) incorporation as a joint-stock company; (ii) having a share capital of at least 18 million euros, fully paid-up in cash and in the form of registered shares; (iii) that shareholders with significant stakes meet suitability criteria; and (iv) having a board of directors comprising at least five members who must meet the suitability requirements (recognised good repute and professional standing, with the necessary knowledge and experience to perform their duties, and able to exercise good governance).

- It sets out the requirements for the **application for authorisation** to create a bank and the reasons for **refusal**, and the rules for amendments to the articles of association and structural changes.

- It sets out the regulations for **cross-border activity** concerning the opening of branches and the freedom to provide services in other EU Member States and in non-EU States, and for the provision of services in Spain by credit institutions from other EU Member States and non-EU States. It also establishes the rules applicable to the opening of **representative offices** of Spanish institutions abroad, of which the Bank of Spain must be notified in advance, and the rules applicable to credit institutions authorised in other EU Member States wishing to open a representative office in Spain, authorisation of which corresponds to the Bank of Spain.

- It regulates the relationship between credit institutions and their **agents and the delegation of the provision of services.**

2. Significant shareholdings

- It maintains the treatment of significant shareholdings laid down in **Royal Decree 1245/1995**, July 14th, 1995, on the creation of banks, cross-border activity and other points regarding the legal framework governing credit institutions, repealing the latter Royal Decree.

- **The Bank of Spain will evaluate proposed acquisitions** of significant shareholdings to ensure certain criteria are met (including the good repute and professional standing of the potential acquirer or compliance with the suitability requirements applicable to members of the board of directors and general managers and similar who will be running the entity's business).

3. Corporate governance measures and remuneration

- RD 84/2015 incorporates the **suitability requirements** envisaged in Royal Decree 256/2013, of April 12th, 2013, including the criteria of the European Banking Authority of November 22nd, 2012, on the assessment of the suitability of members of the governing body and holders of key positions. It also adds the following:

  ✓ In addition to the **assessment of the suitability requirements,** conducted by the Bank of Spain (or, by the ECB, where applicable), an evaluation will also be conducted by the acquirer of a significant shareholding when fresh appointments derive from this acquisition.

  ✓ The **deadlines for the suitability assessment** by the Bank of Spain will depend on the reason for the assessment.

  ✓ In the case of the **requirement for good repute and professional standing**, the holding of posts of responsibility in credit institutions that have been subjected to a process of early intervention or resolution will be taken into account.

- In the following cases, authorisation by the Bank of Spain is not required in order to **obtain credits, sureties and guarantees to senior officials of the institution**:

  ✓ Those covered under collective labour agreements between the entity and its employees.

  ✓ By virtue of contracts with standard conditions, applied en masse and on a habitual basis to a large number of customers and which do not exceed 200,000 euros.

- Certain aspects of **variable remuneration components** are clarified.

- The following provisions are laid down regarding the constitution of **appointments and remunerations committees**:

  ✓ This obligation will be deemed to have been fulfilled: (i) in the case of subsidiary credit institutions that have been exempted from application of prudential requirements on an individual basis; and (ii) provided that the parent institution constitutes these committees and exercises their functions for its subsidiaries.

  ✓ The **functions** of the appointments committee and the remuneration committee are specified.

  ✓ The Bank of Spain is authorised to make comparisons of **practices to promote diversity** and trends and practices regarding remuneration.

- The board of directors is given responsibility for ensuring that the **corporate governance and remuneration policy information on the entity's website** is kept up to date. The Bank of Spain is authorised to specify the terms of website configuration and the information to be included.

- Implements the provisions of Law 20/2014 regarding the **risk function and the risk committee**.

4. Solvency of credit institutions

- As regards requirements for organisation, risk management and internal control, RD 84/2015 lays down that entities must (i) have an organisational structure suited to the nature of their business; (ii) have an **internal audit function;** and (iii) have a **regulatory compliance function** independent from other areas, units or functions.

- The board of directors must have unimpeded access to information on the entity's risk status.

- Entities are to have **policies and procedures to control credit, counterparty, residual, and concentration risk, risks deriving from securitisation transactions, market risk, interest risks arising out of activities separate from the trading book, operational risk, liquidity risk, and risk of excessive leverage.**

- For the purpose of calculating risk-weighted exposures for credit risk, exposures to the Spanish autonomous regions and local government bodies shall be treated in the same way as **exposures to the central government.** It also lists the **public sector bodies** that will be treated in the same way as **exposures to the level of government to which they belong.**

- The following points stand out regarding **capital buffers**:

  ✓ **Bank of Spain authorisation** to (i) set the percentages of countercyclical buffers; (ii) identify global systemically important institutions (G-SII); (iii) identify other systemically important institutions (O-SII); and (iv) define the rules for joint implementation on G-SIIs buffer, O-SIIs buffer and systemic risk buffer.

  ✓ Establishment of the rules for calculating the **maximum distributable amount.**

  ✓ Content of the **capital conservation plan** that institutions not complying with the combined buffer requirement are to submit to the Bank of Spain.

5. Supervisory measures

- The Bank of Spain will **review the systems, strategies, procedures and mechanisms** institutions apply to comply with the solvency standards, and **assess**:

  ✓ The risks to which institutions are or might be exposed.

  ✓ The risks an institution poses for the financial system.

  ✓ The risks that have been revealed in the stress tests.

- **Internal methods.** The Bank of Spain will apply controls to ensure that institutions do not depend solely on external credit ratings when assessing the solvency of an entity or financial instrument. To this end, it may publish technical guidelines. Additionally:

  ✓ Institutions authorised to apply internal models will **notify the Bank of Spain of the results of applying these internal models to their exposures** included on **reference portfolios** drawn up by the EBA, and where applicable, on the **specific portfolios** prepared by the Bank of Spain, in order to **identify possible divergences** in the risk-weighted exposures or the capital requirements so as to **take corrective measures**.

  ✓ The **Bank of Spain will regularly review** (at least once every three years) institutions' **compliance** with the requirements of models whose use to calculate capital requirements is subject to prior authorisation.

- **Consolidated basis supervision** includes financial holding companies and mixed financial holding companies and institutional protection systems.

- It establishes the criteria for **collaboration between supervisory authorities** and sets out the criteria upon which the Bank of Spain **will establish and preside over colleges of supervisors**.

6. Other points

- The **calculation of credit institutions' Additional Tier 1 and Tier 2 instruments** will be subject to prior approval by the Bank of Spain under CRR.

- **Integration of the Bank of Spain in the Single Supervisory Mechanism (SSM)**: The Bank of Spain's powers of authorisation and supervision envisaged in this RD will be applied in the framework of those assigned to the ECB and the SSM. In particular, the ECB will be responsible for issuing and revoking the authorisation of credit institutions, and possible opposition to the acquisition of a significant shareholding; without prejudice to the functions assigned to the Bank of Spain as the competent national authority for these matters. Additionally, the powers assigned to the Bank of Spain over corporate governance and remunerations, solvency and supervision will be exercised by the ECB in those cases where the latter is considered the competent authority.

- **It establishes the number of people** on the board of trustees of **banking foundations** that must have specific knowledge and experience of financial matters.

- It defines the **representatives of the member institutions of the Deposit Guarantee Fund.**

- **Entry into force.** On the **day following that of its publication** in the official gazette (BOE), with the exception of the obligation to provide information on corporate governance and remuneration policy on institutions' websites. For this it will have a period of **three months** starting on **the date when the Bank of Spain publishes the envisaged developments**.

Royal Decree amending the Regulation implementing the Law on collective investment institutions (Royal Decree 83/2015, published in the official gazette on February 14th, 2015)

Royal Decree 83/2015, of February 13th, 2015, amending Royal Decree 1082/2012, of July 13th, 2012, enacting the Regulation implementing Law 35/2003, of November 4th, 2003, on collective investment institutions, transposes the Alternative Investment Fund Managers Directive (AIFMD) and takes the opportunity to introduce new improvements to the existing legal rules applicable to collective investments, particularly as regards depositaries.

The transposition of the AIFMD began with Law 22/2014, November 12th, 2014, regulating venture capital firms, other closed-ended collective investment undertakings, and amending Law 35/2003, of November 4th, 2003, on collective investment institutions (CII). This Directive affects **unharmonised CII management companies**, that is to say, those not authorised under the rules envisaged in Directive 2009/65/EC, of the European Parliament and of the Council, of July 13th, 2009, on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS). New requirements are introduced for the authorisation of the aforementioned management companies and the commercialisation of the CIIs they manage. The RD also establishes in more detail the rules of conduct to which they are subject, and the operational, organisational and transparency requirements they are to meet, with particular attention being paid to risk management, liquidity and conflicts of interest.

It also covers other issues that **complete the transposition of the AIFMD**, including:

- Additional information to be included in the prospectus of non-harmonised CIIs.
- The periodic information that CII management companies are to submit to the National Securities and Exchange Commission on the main markets and instruments in which they trade on behalf of the alternative CIIs they manage.
- The limits to the investments in securitisations and clarification of the concept of investment management as established in the AIFMD, which includes portfolio management and risk control.
- The requirements for the delegation of functions by management companies, the adjustments to own resources required of management companies with respect to the minimum required by European law, and appropriate and consistent procedures allowing correct and independent evaluation of the CII's assets.
- The strengthening of the **risk management function**, which must be functionally and hierarchically separate from the operational units.
- A **liquidity management** system is included.
- The aspects concerning the **remuneration policy**, applicable to management companies, **and the depositary regime**, stand out, applying to depositaries for all types of CII, bearing in mind that the treatment given to these issues in the European Directives (including UCITS) as regards the functions of the depositary, the remuneration policy and penalties, is practically identical. The regime for depositaries defines and regulates depositaries' functions and responsibilities. Some of these features of the regime for depositaries were already regulated in Spanish legislation by **Order EHA/596/2008**, of March 5th, 2008, which regulates certain aspects of the legal framework for CII depositaries (now repealed). Nevertheless, Royal Decree 83/2015 has opted to **integrate in a single title the regulatory provisions concerning depositaries** to enhance their regulation by making it more consistent and systematic.

The key new features of the **regime applicable to depositaries** include:

- ✓ The Regulation incorporates the updated content of Order EHA/596/2008, thereby raising the rank of their obligations. Nevertheless, the incorporation is partial, as certain points have been left for subsequent implementation. The specificities and exceptions applicable to depositaries of venture capital firms, closed-ended collective investment undertakings, and free investment collective investment institutions are also pending implementation.
- ✓ The rules for the delegation of the deposit function and strict liability rules are established.
- ✓ The minimum content of the depositary's written agreement with the CII's management company, for each CII it manages or with the investment firm.

A second block of **new features** concerns the **permanent development of the Spanish collective investment market**. The emergence of new marketing instruments and mechanisms makes it advisable to adjust the regulations to ensure an appropriate balance between their development and investor protection. In particular, these new features include **the following**:

- The **active marketing of free investment CIIs to qualified retail customers** is allowed provided they make a minimum disbursement of 100,000 euros and state in writing that they are aware of the risks inherent in the investment. Accordingly, the minimum disbursement whereby a retail customer may buy or subscribe shares in a free investment CII has been set at 100,000 euros.

- **Various types of free investment CII are regulated** to enable investments in invoices, loans, commercial bills in habitual use in commercial matters and other similar assets, in financial assets linked to investment strategies with a time horizon of more than a year and derivative financial instruments, irrespective of the type of underlying asset.

- Certain provisions of the regulation have been adapted to allow the use of **omnibus accounts**, the assets in which harmonised CII may invest have been adapted to include those considered suitable by the ESMA, and the range of instruments and derivatives in which non-harmonised open-ended collective investment schemes and non-harmonised financial investment funds can invest has been widened. Moreover, the rules governing agents and representatives of investment services companies have been harmonised.

Finally, the Royal Decree contains an amendment to **Royal Decree 1310/2005**, of November 4th, 2005, partially implementing the Securities Market Act, as regards the listing of securities on official secondary markets, public offers of sale or subscription and the prospectus required for these purposes, with a **dual objective**:

- To correctly transpose Directive 2003/71/EC of the European Parliament and of the Council of November 4th, 2003, on the **prospectus** to be published when securities are offered to the public or admitted to trading. To this end, it is stated that when the final offered price and the number of securities that are going to be offered to the public cannot be included in the prospectus, the prospectus is to state the criteria or conditions for determining these points, or in the case of the price, the maximum price.

- To make an **adjustment** to adapt the aforementioned Royal Decree to the content of Directive 2014/51/EU regarding the powers of the ESMA.