

Recent key developments in the area of Spanish financial regulation

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Royal Decree-Law on urgent measures for the transposition of EU Directives into Spanish Law (Royal Decree-Law 3/2020, published in the official state journal on February 5th, 2020)

Royal Decree-Law 3/2020 transposes several European directives into Spanish law, some of which affect the financial sector. Specifically, Directive (EU) 2016/97 of the European Parliament and of the Council of January 20th, 2016, on insurance distribution; Directive (EU) 2016/2341 of the European Parliament and of the Council of December 14th, 2016, on the activities and supervision of institutions for occupational retirement provision (IORPs); and Directive (EU) 2017/828 of the European Parliament and of the Council of May 17th, 2017, amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement. The Royal Decree-Law took effect the day after its publication.

Firstly, the transposition of Directive (EU) 2016/97 on insurance distribution is designed to set rules for entering the insurance and reinsurance distribution business, the conditions on which that business must be carried out and the applicable governance, supervisory and penalty regimes, all with the overriding aim of guaranteeing protection of the rights of policyholders and beneficiaries under insurance contracts.

The following aspects stand out:

- It defines an ‘ancillary insurance intermediary’ as any natural or legal person, other than a credit institution or an investment firm, who, for remuneration, takes up or pursues the activity of insurance distribution on an ancillary basis.
- It stipulates that insurance and ancillary insurance intermediaries, insurance brokers and reinsurance brokers, must be registered in the official public register of insurance and reinsurance distributors.
- It allocates competences between the state and the regional governments.
- It regulates the activities of insurance and reinsurance distributors resident or domiciled in Spain and in other European Union member states.
- Insurance and reinsurance undertakings must keep an internal register itemising the employees directly involved in distribution activities and the person in charge thereof. They must also identify a function to ensure correct execution of the endorsed internal policies and procedures in order to monitor that the persons directly involved in insurance distribution activities, the person in charge of the distribution activities and, if warranted, the persons sitting on the management body responsible for the distribution activity are of good repute and possess the appropriate level of knowledge and competence.
- It stipulates the general regime applicable to the activities of insurance agents.
- It establishes conflict resolution mechanisms.
- It introduces insurance product information requirements for customers. Insurance undertakings and intermediaries are required to offer customers of insurance-based investment products guidance on and warnings of the risks associated with

insurance-based investment products or in respect of particular investment strategies proposed; information about all associated costs and charges; and a suitability assessment, if appropriate.

- It regulates packaged or bundled product sales.
- With respect to remuneration, insurance distributors must inform their customers about the type of remuneration they will receive at the pre-contractual stage.
- It introduces product design, approval, oversight and governance requirements for insurance distributors which design products for sale, including the requirement that they specify the identified target market.
- It establishes implementing and supervisory powers, professional secrecy requirements, the requirement to cooperate and exchange information with other competent authorities, responsibilities vis-à-vis the administration and the sanction regime.
- It specifies the requirements for bancassurance operators, notably among which:
 - They must be a credit institution or a specialised lending institution (SLI or EFC for its acronym in Spanish). They may also be a corporate enterprise controlled or invested in by credit institutions or SLIs or their groups.
 - They must present a report indicating the insurance undertaking for which they are distributing insurance, the geographical coverage and the procedures in place for resolving conflicts deriving from customer complaints and claims.
 - They must certify that the person in charge of the distribution activity or, as warranted, the persons sitting on the management body responsible for the distribution activity and all of the persons directly involved in the distribution of the insurance are of

good repute and possess the appropriate level of knowledge and competence.

Secondly, in order to partially transpose Directive (EU) 2016/2341 on the activities and supervision of institutions for occupational retirement provision (IORPs), the consolidated text of the pension plan and pension fund act (enacted via Royal Legislative Decree 1/2002) is amended in order to introduce into Spanish law new matters not regulated until now to ensure the good governance and prudential supervision of IORPs, the provision of adequate information to members and beneficiaries and IORP transparency and legal certainty.

The main areas transposed:

- It establishes the principles which must be held with respect to the information to be provided to prospective members, members and beneficiaries about pension plans and funds to enable them to make informed decisions about their retirement and understand the contents of and trends in their plan rights. The information terms, contents and means of provision are to be established in implementing regulations.
- New duties are vested in the pension fund control committee.
- Rules have been established regarding the prudential supervision to which pension plans and funds and their management firms shall be bound. They include rules regarding technical provisions and how they are financed, own funds requirements, solvency margin, investment rules and investment management. The new regulations itemise the powers vested in the national competent authority, the DGSFP for its acronym in Spanish, in order to enable it to perform its pension system oversight duties and its powers with respect to outsourced functions.
- They introduce the broad guidelines for the IORP governance system and any control bodies, notable among which the following aspects:

- Entities must have an effective governance system equipped to guarantee appropriate and prudent management of their activities and the funds they manage. The system must include written corporate governance policies related with the management of risks and the internal audit function and, if warranted, the actuarial activities performed by the entity and the functions outsourced, as well as an effective internal control system and contingency plans. The governance system must require IORPs to factor environmental, social and governance considerations into their investment decision-making.
- The persons who effectively run the management firms, perform key functions and any persons or entities to which key functions have been outsourced must be of good repute and integrity and possess adequate qualifications, knowledge and experience.
- Entities must establish and apply a remuneration policy in keeping with their internal organisational, size and the nature, scale and complexity of their activities, all of which framed by the principles enshrined in the Directive.
- IORPs must have the following key functions: a risk-management function, an internal audit function, and, where applicable, an actuarial function.
- Every IORP must carry out and document an own-risk assessment at least every three years.
- IORPs may outsource functions, including the key functions, subject to the legally-stipulated exceptions and conditions.
- Lastly, it regulates the exchange of information between the competent authorities of the host and home Member States and permits the transfer of an IORP to an IORP authorised in another Member State.

Thirdly, Royal Decree-Law 3/2020 partially transposes Directive (EU) 2017/828 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement, specifically in relation to the matters that affect the insurance sector, with the aim of preventing pressure on undertakings to perform in the short-term. To that end, amendments have been made to Law 20/2015 of July 14th, 2015, on the structuring, supervision and capital adequacy of insurance and reinsurance undertakings.

Bank of Spain Circular amending the Risk Information Register Circular (Circular 1/2020, published in the official state journal on February 5th, 2020)

The purpose of the Circular is to adapt Circular 1/2013 for the provisions of Law 5/2019 (of March 15th, 2019) regulating mortgage credit agreements. In addition, it introduces certain amendments in order to: (i) enhance the consistency of the information collected via the Risk Information Register vis-à-vis the requirements set down in the AnaCredit Regulation (Regulation (EU) 2016/867); (ii) clarify which information needs to be submitted with respect to certain transactions; and, (iii) reorganise the form in which the information is presented in some modules and introduce the odd additional dimension. It also introduces certain clarifications with respect to the presentation of claims to the Register.

In broad terms, it introduces the following changes:

- It introduces two new types of reporting entities: credit institutions operating under the freedom of provision of services regime and real estate lenders. It specifies the information they will have to submit and sets the technical requirements for reporting to the Risk Information Register.
- It gives mortgage credit intermediaries access to the credit risk reports on the natural and legal persons registered in the Risk Information Register on the same terms and conditions as the other reporting entities.

- It contemplates the possibility of temporarily restricting access to the Register's data if an entity breaches its reporting requirements in respect of the quality or accuracy required.
- It introduces changes to the data modules which the reporting entities are obliged to submit to the Bank of Spain and exemptions from reporting certain modules.
- The information requirements demanded of the branches of credit institutions from other reporting countries have been eased.
- For the entities that were already reporting prior to effectiveness of Law 5/2019, the first submission of data to the Risk Information Register in keeping with the terms of this Circular will be that corresponding to their April 2020 data, except for the modules related with guarantees, for which the first compliant submission will be that reporting the October 2020 figures.

Royal Decree on the legal regime governing specialised lending institutions, amending the Companies Register Regulation, Royal Decree 84/2015, of February 13th, 2015, implementing the Law on the structuring, supervision and capital adequacy of credit institutions (Royal Decree 309/2020, published in the official state journal on February 25th, 2020)

The purpose of the Royal Decree is to establish the legal regime governing the so-called specialised lending institutions (SLIs or EFCs for their acronym in Spanish), with respect to incorporation, solvency and supervisory regime requirements, duly implementing the provisions of Law 5/2015, of April 27th, 2015, on the stimulation of corporate financing. The new legislation takes effect on July 1st, 2020, with the exception of the provisions regarding the liquidity buffer and sources of financing and maturity profiles, which will take effect three months after publication of the implementing Bank of Spain Circular and amendment of Royal Decree 84/2015, which will take effect the day after its publication in the official state journal.

In broad terms, the new legislation regulates the following:

- It defines specialised lending institutions as undertakings that, without being credit institutions, but subject to authorisation from the Ministry of Economic Affairs and Digital Transformation, are professionally devoted to carrying out one or more of the activities contemplated in article 6 of Law 5/2015.
- It permits the creation of hybrid legal forms: specialised lending institutions-payment institutions; and specialised lending institutions-electronic money institutions.
- Given that the SLIs are not allowed to take repayable funds from the public in the form of deposits, loans, repurchase agreements, *etc.* no matter the use of proceeds, they are not subject to the deposit guarantee legislation.
- The legislation establishes the requirements for obtaining and maintaining authorisation to operate as an SLI, the grounds for denying such authorisation and the procedure for opening branches abroad.
- The terms of Law 10/2014 shall apply to SLIs with respect to the following areas:
 - Opening of branches, designation of agents and delegation of functions by SLIs.
 - Significant shareholdings, assessment of suitability, conflicts, registration of senior executives, corporate governance and remuneration. However, SLIs with total assets of less than one billion euros are exempt from the requirements to have: appointments and remuneration committees and independent directors.
 - Capital adequacy obligations. The Bank of Spain is entitled to exempt the SLIs that are part of a consolidable group of credit institutions from the individual capital requirements stipulated in the CRR using the same criteria as are used to exempt subsidiaries that are credit institutions.

- SLIs must at all times hold a high quality liquidity buffer deemed sufficient to cover their net cash outflows during a period of grave financial instability and to maintain an appropriate mix of sources of financing and maturity profiles, in order to avoid potential liquidity mismatches that could harm or jeopardise the entity's financial situation.
- SLIs are required to submit the information required for supervisory reporting purposes detailed in Commission Implementing Regulation (EU) 680/2014. However, the Bank of Spain will be broadly empowered to regulate the associated frequency, thresholds and requirements.
- It is up to the Bank of Spain to supervise, at the consolidated level, consolidable groups of SLIs.
- SLIs must have their annual financial statements audited.
- Any procedure applying for authorisation to transform from a bank to an SLI authorised prior to effectiveness of Law 5/2015 that was initiated prior to December 31st, 2019, will be governed in keeping with the simplified procedure contemplated in the said Law.
- It regulates SLIs deriving from credit institutions with limited operating scope and share capital of less than 5 million euros.

Lastly, Royal Decree 309/2020 implies:

- The repeal of Royal Decree 692/1996 (of April 26th, 1996) on the legal regime governing specialised lending institutions.
- The amendment of the Companies Register Regulation to clarify the fact that it also applies to SLIs.
- The amendment of Royal Decree 84/2015 in order to regulate inscription of expiry in the Companies Register.