CUATRECASAS

Spain – Banking Regulation 2019

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INTRODUCTION

From late 2008, the Spanish banking sector underwent a deep restructuring process ultimately driven by regulatory responses to the severe crisis which the sector and the country faced post-2007. After reshaping the sector completely, the worst of the crisis is over and we now face a more stable, more transparent and sounder financial sector. However, the relative stability we have enjoyed these last couple of years was disrupted in June 2017 by Banco Popular's failure and its acquisition by Santander for one euro, bringing a battle of claims by shareholders. We still believe that restructuring will continue, via further concentration and repositioning. As an example, recent relevant transactions include: the sale of EVO Banco by Apollo to Bankinter; the sale of 49% of Wizink by Santander (previously owned by Popular) to Varde Partners; and Abanca acquiring the Spanish business of Caixa Geral. The next in the pipeline could be Bankia, a large, listed bank in which the State still holds a significant controlling stake, but which it has announced plans to divest.

Until 2009, it was probably accurate to describe the Spanish banking sector as unique among its European counterparts. While the country was, and is, home to two of the world's largest banking corporations (Santander and BBVA) – present in other European jurisdictions and outside the EU, most significantly in Latin America – such large corporations did not account for more than 30% of the domestic deposit market share; the rest was in the hands of many other institutions, including a wide array of mid- and small-sized companies. Bank of Spain's census as

of early 2009 comprised some 80 private banks (of which roughly 10 had a material market share), 80 credit cooperatives (accounting, altogether, for 5% of the share, approximately) and 45 savings banks (cajas de ahorros), representing, roughly, 50% of the market. Branches of foreign institutions (almost exclusively EU-incorporated) were and are present, but hold a negligible share of the retail market.1

The relevant presence of savings banks was doubtlessly the most salient feature of the Spanish banking system. Cajas were a genuinely Spanish type of institution, with no full equivalent in any other Western jurisdiction. The Supreme and Constitutional Courts described them in several judgments as 'foundation-like'. Strictly speaking, savings banks were foundations not subject to the governance rules in the Foundations Act. As foundations, they lacked capital or any equivalent fund composed of legal instruments bearing voting rights. Their corporate governance depended on a complex set of mechanisms ultimately enacted by regional laws which placed them under the control of regional powers. For this reason, it has been argued that savings banks were similar to German Landesbanken.

The deep crisis changed this landscape dramatically.

The banking sector was severely hit by the real estate crisis. Excessive exposures to developers and builders accounted for a very significant proportion of the banks'2 assets. That, in addition to the effects of the general economic crisis, led many institutions into serious trouble if not actual insolvency. All institutions were affected, but savings banks were particularly in trouble, since their exposure was almost purely domestic and highly concentrated in real estate.

The regulatory response to the crisis came, both at the National and European levels, in the form of a wide array of measures (see the section entitled, 'Recent regulatory themes and key regulatory developments in Spain' below) that, ultimately, have changed (and still keep on changing) the banking sector and the regulatory architecture itself. The legislative measures have addressed virtually all aspects relating to the financial sector, encompassing: (i) measures to provide liquidity and solvency support to banks; (ii) measures to promote concentration among institutions and to set up restructuring alternatives, including resolution mechanisms; (iii) changes in the legal regime of savings banks; (iv) provisioning requirements; (v) strengthening corporate governance; (vi) new and significantly higher capital requirements; and (vii) changes in the supervisory and regulatory architecture. But the measure that will probably prove to be most far-reaching over time is the introduction of the EU (Eurozone) Single Supervisory System (the "SSM"), with the ECB taking over most of the supervisory duties of the former Member States' domestic supervisors (a measure that took full effect on 4 November 2014) and the implementation of the Banking Recovery and Resolution Directive ("BRRD")3 and, again for the Eurozone, the Single Resolution System (the "SRM").

During the crisis, the State had to take over some banks and provide support to others. The banking sector recapitalisation needs, evidenced through successive stress tests conducted both at the EU and domestic levels, led to Spain's request for financial assistance from the EU in the form of a €100 billion credit facility (of which the amount actually used was €40 billion). In order to obtain the line, in July 2012 Spain entered into a MoU with the EU on financial sector policy conditionality ("MoU") which led to further regulatory measures, including the creation of an

asset management company named SAREB4 (commonly known as "bad bank") in operation from December 31, 2012. To a good extent thanks to the creation of SAREB – followed by the banking sector in general – the country now enjoys an active secondary market for loans and REOs and a developed servicing industry. All this has provided the banks with efficient tools to implement their NPL management strategies.

As a result of this all, the landscape of the banking sector has changed very significantly. Savings banks have de facto disappeared (with two tiny exceptions), their banking business having been taken over by banks, and the savings banks themselves have become foundations, some of them still holding significant stakes in banks, while others do not. Concentration has also happened, to a lesser extent, within the subsectors of cooperatives and banks. The State took over several financial institutions, all of which were subsequently auctioned and acquired by other privately held entities except Bankia (where the State remains the controlling shareholder, but it is likely that such stake will be finally sold by the State at the right time) and Banco Mare Nostrum, a mid-sized, unlisted bank, which a few months ago merged into Bankia to facilitate the State's divestment when all its stake in Bankia is finally sold. The Fund for Orderly Bank Restructuring (Fondo de Reestructuración Ordenada Bancaria – FROB)5 has played a crucial role in the restructuring process of our banking system. The FROB has ultimately become the Spanish executive resolution authority, and is thus integrated within the SRM.

In addition to the traditional credit institutions supervised by Bank of Spain, due to the weakness of most local banks, there are also new players in the banking sector providing credit and marketing other financial products without any supervision, since they take advantage of the fact that collecting funds from the public is the only typical banking activity strictly reserved to credit entities.6 This trend of non-bank channels which supplement the regular banking sector will continue progressively in Spain. Therefore, the "shadow-banking" phenomenon, the new cryptocurrencies and the need to supervise these incoming entities or not, constitutes a major debate not only in Spain but also at EU level for harmonisation purposes. Due to the low ROE in the banking sector, Spanish financial institutions are very focused on increasing efficiency and yields to compensate the low level of interest rates, and are concentrated on new strategies such as "going digital" and investing in "fintechs" to develop new tools and applications. The crowdfunding initiatives and non-financial return models (outside the scope of Law 5/2015, of April 27, when dealing exclusively with donations, sale of assets and services, and free-interest loans) are growing, particularly through online platforms, but the overall amounts and transactions remain low. In addition, some of the Spanish financial institutions are also expanding into nearby markets such as Portugal and the UK, taking advantage of certain credit institutions on sale after being rescued by the local authorities. On the other hand, there are increased rumours of banks' integration in Spain to face the challenges resulting from low capital returns and in order to gain efficiency. There are even rumours about the first integration of a large Spanish credit institution with another EU large financial entity.

The latest Financial Stability Report issued by Bank of Spain dated November 2018 provides an updated description of the Spanish banking sector.7 In a nutshell, some key references are as follows: (i) consolidated P&L of the financial sector has increased by 12.5% due to the high

reduction in losses derived from asset depreciation; (ii) total consolidated assets decreased by 0.5%; (iii) loans and credits to the private sector have decreased by 2.9%; (iv) the NPL rate (tasa de morosidad) has gone down to 3.6% (meaning a decrease from 4.5% compared to 2017), although the impaired assets level is still high (increase default signs in consumption), despite the important reduction in the past years (-60% since 2013); (v) recourse of Spanish banks to the Eurosystem continued at a high level (€168b) but has at least not increased in the last three years (average allocation to Spanish entities was 22%); (vi) private deposits at banks and their patrimony on a consolidated basis increased by 0.6% but in total decreased by 1.3%; (vii) the level of provisions due to asset deterioration has also decreased due to better performance, and impaired assets ("dudosos") have been reduced by 26.7% in the last year; and (viii) common equity tier 1 capital ratio ("CET1") has been reduced slightly to 11.9% and has only increased by 0.3% since 2014. The report also cites evidence that the credit to SMEs in Spain went down 7.2% and that the Spanish banking system is more efficient than comparable systems in the main European jurisdictions and the European average.

Brexit has set up a new economic and financial scenario for Spain (as for most continental countries). It is extremely difficult to anticipate the effects of Brexit, since it would directly depend on the final scenario of the UK's exit from the EU (due on March 29, 2019) and the negotiations for the subsequent UK-EU relationship. In any case, there are high risks of a "hard Brexit", meaning a big challenge for all sectors, but no doubt that financial services would be affected, particularly those activities that are more dependent on the 'EU passport'. At this stage, we have seen some relevant relocations of business related to financial activities into other jurisdictions by large financial institutions, and Dublin, Frankfurt and Luxembourg will take some operations. A "hard Brexit" will accelerate banks' contingency plans and movements in their balance sheets from the UK to their affiliates in EU jurisdictions. On the other hand, the Spanish banks' activities abroad are increasing very significantly. Activities in the US and in the UK already represent more than half of the international exposure of Spanish financial institutions.

Regulatory architecture: overview of banking regulators and key regulations

Spanish regulatory architecture is traditionally based on a sectoral approach (with a different regulator for banks, investment companies and insurance companies). Banking supervision, traditionally attributed to Banco de España (the country's central bank) underwent a very significant change after the implementation of the SSM and SRM Regulations.[8]

The most relevant public authority for banks is now the ECB[9] which: (i) is responsible for licensing; (ii) controls transfers of significant holdings; (iii) is responsible for prudential supervision, including on- and off-site direct inspection of most relevant institutions[10] and receives reporting; and (iv) may trigger the exercise of disciplinary powers. However, stating that the ECB has become "the" banking supervisor is an oversimplification, since Bank of Spain, further to cooperating with the ECB in its supervisory tasks, still holds regulatory powers, may, within a larger or lesser scope depending on topics, issue regulations on solvency, conduct, accounting and

other matters relating to banks11 and is the sole supervisor for certain other financial intermediaries.

Although it is the most important, Bank of Spain is not the only national public authority of relevance to banks. Apart from the Ministry of Finance:

- The National Securities Market Commission (Comisión Nacional del Mercado de Valores – CNMV) holds authority over banks, whether listed or not,12 as providers of investment services.13
- The SEPBLAC14 is the Spanish financial intelligence unit and controls the application of anti-money laundering and terrorist financing prevention rules in accordance with FATF standards (to which banks are subject). It holds supervisory capacity of its own and may exercise disciplinary powers in its field.
- The Deposit Guarantee Fund (Fondo de Garantía de Depósitos en Entidades de Crédito – FGD) is privately ex ante funded by banks via compulsory periodical contributions, and is governed by a committee which is split on a 50/50 basis between representatives of the banks themselves and Bank of Spain. The Spanish FGD is like the US FDIC and has wide capacity to adopt preventive measures rather than acting like a mere deposit box, though its role is nowadays much less salient than it used to be.
- The Fund for Orderly Bank Restructuring (Fondo de Reestructuración Ordenada Bancaria – FROB)15 is a public institution, created in 2009 to cover the FGD's lack of financial capacity to deal with a systemic crisis. Its function was to provide support to (and eventually take over) banks in need of restructuring. In 2012 its legal status was re-shaped to turn it into a resolution authority and in 2015 adapted to the BRRD and integrated with the rest of Eurozone resolution authorities as part of the SRM.

Spain is a member of the EU and the Eurozone and, therefore, most banking legislation and regulations – when not directly in the form of EU regulations – are based on directives or adapted to them. Thus, in many areas, Spanish banking law is highly similar or even identical to other EU jurisdictions. The primary EU statutes applicable, as amended from time to time, are:

- The Capital Requirements Directive. The text now in force is EU Parliament and the Council 2013/36/EC of 26 June 2006 ("CRD IV"), coupled with Regulation (EU) 575/2013 of the EU Parliament and the Council, of the same date ("CRR").
- The Banking Recovery and Resolution Directive. Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014.
- The MiFID II-MiFIR package.
- The Third and Fourth Anti-Money Laundering Directive. EU Parliament and Council Directive 2005/60/EC of 26 October 2005 and superseded by Directive 2015/849 of 20 May 2015 and to be implemented before 31 December 2017.
- The minimum reserves regulation. Council Regulation (EC) nº 2531/98 of 23 November

1998.

- The SSM Regulations: Council Regulation (EU) nº 1024/2013 of 15 October 2013 and ECB Regulation (EU) nº 468/2014 of 16 April 2014.

- The SRM Regulation: Regulation (EU) nº 806/2014 of the European Parliament and of the Council of 15 July.

EU legislation, in turn, is mostly framed on international standards issued by relevant committees and organisations, among which is the Basel Committee on Banking Supervision. CRD IV and CRR implement Basel III.

In 2011, the EU upgraded its supervisory framework by turning the pre-existing "level III" committees16 into as many EU supervisory authorities. For the banking sector, the relevant authority is the EBA, which has taken over the role of the CEBS. The EBA performs an array of tasks, including the issuance of guidance on supervisory policy matters. During its three first years of operation, EBA, further to maintaining CEBS's standards, has produced many significant documents that have either regulatory content on their own or are applied as interpretation criteria, not only for EU but also for national law.

In 2013–2015, Spain carried out a significant effort towards the systematisation of its banking law. For many years the country lacked a comprehensive source of banking legislation that could mirror the Italian or French Banking Codes. In addition, between 2008 and 2012 the regulatory management of the crisis resulted in a very high number of pieces of legislation (mostly executive), amended multiple times within a short timeframe, which also needed to be re-cast. While banking law is still a vast domain, the most relevant statutes further to those directly applicable EU laws, are:17

- Royal Legislative Decree 4/2015, of October 23, approving the restated text of the Securities Markets Act (regulates, among other matters, investment services and implements MiFID18).

- Bank of Spain's Autonomy Act 13/1994 of June 1.

- The Money Laundering and Terrorist Financing Prevention Act 10/2010 of April 28 (implementing the III AML Directive).

- Royal Decree-law 16/2011, of October 14, on the Credit Institutions Deposit Guarantee Fund (merged the previous schemes into a single FGD).

- Credit Institutions and Investment Firms Recovery and Resolution Act 11/2015 of June 18 (gives the FROB its present legal status and institutes a comprehensive restructuring and resolution framework, implementing the BRRD).19

- Savings Banks and Banking Foundations Act 26/2013 of December 27.

- Credit Institutions Ordination, Supervision and Solvency Act 10/2014 of June 26, developed by Royal Decree 84/2015 of February 13.

As stated, these acts and other relevant legal provisions are developed by a high number of specific regulations. Due to the technical nature of the matters, it is not unusual that the development is not completed in a single step but requires a multiple-tier set of regulations from different authorities. Highly complex parts of the rulebook or matters that require a very detailed degree of specification are frequently left for Bank of Spain's regulations (Circulares) which, while forming the lowest tier in the cascade of regulations, become the most directly applicable and are thus perceived by the banks as essential.20

Finally, mirroring EBA guidance, in recent times there is yet another tier of (albeit "soft") regulation being developed, named "Bank of Spain Guidelines" and other "good practices" codes. These may be direct adoptions of EBA Guidelines (most frequently) or developed ad hoc by the Bank.

Recent regulatory themes and key regulatory developments in Spain21

After the December 2015 elections, it took over 10 months and another call to the polls, and the whole of 2016, for Spain to have a fully empowered government – which, however, was a minority one and lasted only until mid-2018. In June 2018, after a no-confidence vote, the centre-right government was replaced by a new cabinet whose parliamentary support has proven unstable. This means that, since 2015/16, the country has entered a certain impasse when it comes to regulatory developments, with very significant delays in the implementation of relevant EU directives. This is in stark contrast with recent past experience since, as stated above, the years since the outbreak of the crisis had seen unprecedented regulatory activity in Spain in many fields: after the adoption of the CRD IV/CRR package, the country has been lagging behind on important pieces of financial legislation, namely: the MiFID II-MiFIR package; the IDD (insurance distribution directive); PSD 2 (second payment services directive); and the MDC (mortgage credit directive) – note that these are 2014/15 directives, all of which should have been implemented by early 2018. Some of the latter have been finally implemented; however late, by recourse to executive legislation (in the form of Royal Decree-laws). This has been the case with MiFID II (finally implemented by means of Royal Decree-law 14/2018 of September 28 after a partial, and very limited, implementation in late 2017 by means of another Royal Decree-law) and PSD 2, implemented by means of Royal Decree-law 19/2018, of November 23. The fourth AML directive was also implemented in 2018 by means of executive legislation. The IDD and the MCD should come next, in early 2019.

On a domestic level, the establecimientos fiancieros de crédito – a type of non-deposit-gathering credit institution which plays a minor but not irrelevant role in the Spanish market – await the development of their regulations, after a project posted for consultation in 2015 – a proposed development of Act 5/2015 – which has not translated into an actual piece of law.

A very relevant and long-lasting set of measures have been implemented, related to the **legal status of savings banks.** As mentioned above, these institutions are a particular type of

foundation, thus unable to issue shares or any other vote-bearing securities (a fact that, among other implications, made it impossible for them to merge but with another savings bank). Reform was implemented in successive stages, ultimately leading to the de facto disappearance of savings banks. Current regulation is contained in the Savings Banks and Banking Foundations Act 26/2013 of December 27.

Savings banks may (and do) still exist under their traditional status, as slightly amended. However, keeping such traditional status now carries significant limitations: the geographical scope of activities is limited and the balance sheet may not exceed €10 billion. If those conditions are not met, the savings bank must transfer its business to a bank and become either an ordinary foundation (if its participation in a bank falls below 10%) or a "banking foundation". Banking foundations are under Bank of Spain's supervision and the higher their stake in a bank, the more stringent their obligations. Banking foundations holding 50% or more of the capital of a bank must create a reserve fund in their own books to meet possible capital needs at the level of the bank.

As mentioned, only two institutions keep their original savings bank form. All others have either disappeared entirely or become foundations. All banking business is now carried out by banks.

Regarding **solvency and resilience**, Spain got through the crisis by implementing successive ad hoc measures anticipating, or going beyond, Basel III rules. All such measures are now abrogated and the country operates within the general CRD IV-CRR framework, mostly under ECB direct supervision.

The **regulatory, supervisory and crisis management architecture** of the country was upgraded by the creation of the FROB. The FROB was created by Royal Decree-law 9/2009 of June 26, and initially conceived as a financial tool. The Credit Institutions Restructuring and Resolution Act 9/2012 turned it into a fully-fledged resolution authority, widely empowered, capable of issuing administrative decisions binding on third parties. From its creation, the FROB has gained remarkable experience in crisis management, resolving, nationalising and re-privatising a relevant number of institutions. Ultimately, as the Spanish branch of the SRB, the FROB has taken part in the resolution process of Banco Popular and its subsequent sale to Banco Santander. Act 9/2012 is now superseded by the BRRD-SRM Regulation and the Spanish Act 11/2015, which are in line with the BRRD.

On its side, the Bank of Spain has made consistent progress in the field of accounting. In late 2016, it published an updating of its provisioning and credit impairment rules and, more recently, in order to keep Spanish rules up to IFRS9 and IFRS15, it adopted a brand new set of accounting standards by means of Circular 4/2017 of November 27, effective on 1 January 2018, superseding the 2004 standards that, after many amendments (the last in late 2016) have been the basis of the system since the transition to IAS/IFRS. Both IFRS9 and the new Spanish standards carry out a major change in loan loss allowance calculation policies, shifting from an "incurred loss" model to an "expected loss" (through the entire remaining life of the loan) model.

The relative lack of activity of Spanish lawmakers and standard setters has contrasted deeply with regulatory activity at the EU level. Both the EU Commission and the EBA have issued numerous

rulings, secondary regulations (mostly in development of the CRR and other major legislative pieces) and guidelines on various topics, from solvency to remuneration practices.

Bank governance and internal controls

External controls

As in many other jurisdictions, Spanish credit institutions' conduct and activities are specifically regulated and supervised by public administration authorities. This special regime for credit entities is mainly developed in Act 10/2014 of June 26, on Ordination, Supervision and Solvency of Credit Institutions and Act 9/2012 of November 14, on Restructuring and Resolution of Credit Institutions, which has been partially superseded by Act 11/2015 of 18 June, on Recovery and Resolution of Credit Entities and Investment Services Companies, which implements Spain Directive 2014/59/EU. Similarly to other EU jurisdictions, the aim is to set up mechanisms to allow the supervisor access to critical information about the situation and evolution of financial entities, restrict or prohibit practices or operations which increase insolvency risks or reduce liquidity, and reinforce the capital structure and protect their customers. Such regulation is applicable both to Spanish entities and other foreign institutions operating in Spain (with limitations regarding those acting through an EU passport, under the home country control principle). Breaches of regulation are subject to sanctions (among others, penalties, disqualification, temporary intervention, revocation of licence).

Day-to-day credit institution surveillance is now shaped by the responsibility shift from the Bank of Spain to the ECB. Within the cooperation framework provided by ECB Regulation (EU) nº 468/2014 of 16 April 2014, banks are now being supervised by teams composed of both Bank of Spain and ECB officials.

Although the ECB now concentrates most functions on filing, control, monitoring, surveillance and inspection of all credit institutions in order to foster the solvency, stability and efficient operation of the financial sector and assure full compliance of the banking regulation, enforcement needs the cooperation of national authorities. Under Act 10/2014 (further developed by Royal Decree 84/2015, of February 13), credit institutions and their directors, senior managers or any other individual holding a management position, which breach the regime ruling conduct and discipline, will be subject to administrative liability. Breaches are classified as very serious, serious and minor offences. Under Act 11/2015 (further developed by Royal Decree 1012/2015, of November 6), the supervision and the resolution activities are now clearly separated in order to act at early stages and to avoid conflicts of interest during the decision-making process. Depending on the stage, bodies of Bank of Spain, CNMV or FROB shall intervene in accordance with their functions.

Credit entities, if listed in capital markets, would also be subject, as issuers, to Royal Legislative Decree 4/2015, of October 23, approving the restated text of the Securities Markets Act, which imposes obligations on disclosure of information in connection with the publication of the annual report on corporate governance and the annual report of directors' remuneration. This is, of

course, without prejudice to their duties, also under the same act, as investment services providers.

Internal controls22

Act 31/2014, of December 3, amended the Spanish Companies Act (Royal Legislative Decree 1/2010 of July 2) on corporate governance matters and came into force in December 2014, strengthening the legal requirements that companies have to comply with in regard to the structure and dynamics of their governing bodies: the board of directors and the general shareholders' meeting. In addition, more specifically for credit institutions, Act 10/201423 has introduced substantial developments in corporate governance matters in order to promote efficient practices, establish internal control mechanisms and develop remuneration policies aligned with the risks taken by credit institutions in the medium term.24 Finally, more recently, Royal Decree 84/2015, of 13 February, develops Act 10/2014, and a new Spanish Code of Good Practices in Corporate Governance for listed companies was released by the Spanish supervisor CNMV in February 2015.25
The most relevant credit institutions in Spain are set up as special public companies (sociedades anónimas) subject to general corporate rules but also to particular requirements.26 The day-to-day management of banks, as in any other company, corresponds to their boards of directors. Pursuant to EU directives, however, the board and its members must meet certain adequacy requisites in order to assure prudent management and prevent conflict of interests. Under this regime, the board of directors is directly liable for the risks assumed by the credit entity.
The current main areas of concern from a corporate governance perspective are the composition, structure and dynamics of the board of directors, the remuneration of its members, and operations related to issuances of capital or debt which may impact on shareholders' rights. In the case of financial entities, special attention is placed on the last two aspects, as well as in the risk and control areas and in the independence of the external auditor.
The board of directors of a bank shall be composed by a minimum of five members (in practice, the number of directors in a bank tends to be significantly higher). According to Royal Decree 84/2015, which further develops Act 10/2014, all directors (members of the board), senior management of banks and those individuals responsible for the internal control should have broad expertise and a good professional track-record (meaning sufficient experience in banking and financial services from previous positions to be evaluated depending on the level of responsibility required) and with an outstanding reputation and honourability in order to adequately perform their duties (meaning having no criminal records, not being declared bankrupt and not having been disqualified to conduct public or private activities due to judicial resolutions or convictions). The chairman of the board of directors cannot be the CEO except if the size and complexity of the financial entity so justifies it and the Bank of Spain authorises it. Members of the board, general managers, senior directors and the like are subject to the regime on discipline of Act 10/2014, so they can be sanctioned in case of breach of their duties (the administrative regime does not waive the general liability principle set forth in the Companies

Act, but applies in addition to the latter). These individuals are also subject to the incompatibilities regime by which they cannot hold similar positions in other banks and have certain restrictions to be members of the board at other companies. Finally, members of the board and senior management should be identified and filed at the Official Register of Senior Banking Officers (Registro Oficial de Altos Cargos de la Banca) which is managed by Bank of Spain. The internal requirements imposed on banks aim to guarantee that the directors of credit institutions are properly informed of all significant facts related to the banks so they can comply properly with all their obligations and assume their liabilities. Banks shall have a good administrative organisation and accounting services, as well as internal control procedures to assure sound and prudent management. In addition, Royal Decree 84/2015 of February 13 also establishes that banks shall set up adequate bodies and proceedings for internal control purposes in order to prevent and avoid any transaction which may trigger anti-money laundering provisions.

Particular attention is paid to risk management and control, and the remuneration policies. Financial entities shall set up procedures to identify, manage, control and communicate existing or potential risks. Articles 32 to 34 of Act 10/2014 regulate the remuneration policies, its main general principles and the variable elements of salaries, which shall reflect a steady performance and be duly adjusted to the risks involved. The remuneration of directors and top management of financial entities is scrutinised with special emphasis (approval requirements and disclosure of data), but also the executive director's remuneration schemes. As a result of the above, together with the board of directors, the bank's organisation must also comprise certain separated and delegated commissions and committees to periodically inform the board and take care of key aspects such as internal audit and control, remuneration and risk management.27 Best practices in corporate governance also imply improving the level of independence of the board of directors, the adequate composition of its key Committees (Executive, Audit and Control, Remuneration, Nominations, Investment and Risk),28 an efficient evaluation process, and the existence of a solid succession plan.

There is also a special regulation on corporate governance applicable to investment services companies, which was introduced by Royal Decree 358/2015, partially amending Royal Decree 217/2008. As a result, the rules and requirements applicable to managers and their remuneration regime in credit institutions are now extended to investment services companies in order to improve efficiency and prudence.

Needless to say, "know your client" (KYC) and "anti-money laundering" (AML) internal procedures, and data protection controls, have been given a lot of attention in the Spanish financial sector in recent years. Royal Decree-Law 5/2018, of July 27, has implemented EU regulation on data protection in Spain.

Bank capital requirements

As stated before, since Spain is a member of the EU, capital requirements (and limits to large

exposures) are governed by the CRD IV and the CRR. The Bank of Spain, by mid-2014, dictated a supplementary regulation to cover the few matters the CRR leaves to national discretion. It is to be remarked, however, that the CRR sets the absolute minimum all banks must comply with (the so-called Pillar I). Banks may face tighter capital requirements from the application of institution-specific ratios under national legislation implementing the CRD IV (Act 10/2014), if decided by the ECB/Bank of Spain. The implementation of the CRD IV framework was completed by means of Bank of Spain's Circular 2/2016, of February 2, which fills certain technical gaps, mostly in the form of national discretions contained in the CRR.

The CRD IV-pack replaced a complex and short-lived set of national rules, designed to restore confidence in the banking sector, introduced during the crisis. By means of such rules, Basel III was somehow anticipated in Spain. Now the country is entirely back in line with the rest of the EU.

Unlike other EU jurisdictions and following a model which is closer to the US, Spain has quite a quite prescriptive framework of provisioning standards.29 General provisions and rules to account for asset impairment have been until recently set in Bank of Spain's Circular 4/2004 of December 22. Regulations set minimum amounts for provisions depending on the type of loan, guarantee and time of arrears. In addition, banks are obliged to account for supplementary, generic provisions which are forward-looking in essence and operate counter-cyclically (i.e. the buffer of provisions may decrease as assets get impaired – and thus specific provisions are allocated – and the other way around). The rules were substantially amended in 2016, by means of Bank of Spain's Circular 4/2016 of April 27, introducing a new text of Annex IX to Circular 4/2004. Circular 4/2004 was subsequently superseded by Circular 4/2017, in force from 1 January 2018. Circular 4/2017 is in line with IFRS 9 (also in force from 1 January 2018).

Rules governing banks' relationships with their customers and other third parties

Spanish law provides, in general, a protective regime to consumers.30 When consumers are dealing with credit institutions, there is also a special regime to protect the banking customer, both as debtor in loan or credit operations and as a creditor for its deposits (Ministerial Order EHA/2899/2011 of October 28, on Banking Services Transparency and Customer Protection; Bank of Spain's Circular 5/2012 of June 27, on Transparency of Operations and Customer Protection, as amended by Circular 5/2017, of December 22; and Act 10/2014 of June 26, on Regulation, Supervision and Solvency of Credit Institutions).31 The rationale is that improving the information provided to customers and increasing banking transparency will increase competition among credit entities. As a result, the set of rules applicable only to individuals mainly (i) requires a written formalisation of the contracts, their delivery to the customer and bookkeeping duties; and (ii) assures transparency of the terms and conditions applied to financial products (i.e., fees, interest rates, etc.) by disclosing such information to Bank of Spain and to the general public.32 Such description of characteristics shall be complete, accurate, comprehensive and clear.33 In addition, following Ruling EU 1286/2014, Order ECC/2316/2015, on information obligations and

classification of financial products, is already applicable in Spain and primarily protects non-professional and non-institutional investors when commercialising certain financial products (mainly, deposit accounts, insurance policies and pension plans), but excluding those specifically covered under Ruling EU 1286/2014.

The mortgage market is getting a lot of attention from the legislator, due to certain abusive practices by financial entities, as determined by Spanish courts. As a result, there is a project to reform the Mortgage Credit Act, which has not been approved by the Parliament yet. Its main principles and goals are: (i) to increase the protection level to debtors; (ii) to promote more transparency and legal certainty to credit transactions; (iii) to regulate the expenses attributable to each party; (iv) to limit the fees, default interests (up to 9%) and other connected commercial sales by lenders; (v) to provide flexibility so that variable-interest rate loans can be easily transformed to fixed-interest rate loans; and (vi) to reduce the volume of judicial claims raised by customers against financial entities.

Spanish banks as investment services providers are also subject to the Second Markets in Financial Instruments Directive ("MiFID II"). MiFID II covers nearly all transactions on financial products and, among other matters, deals with customer protection. According to MiFID II, customers are classified according to their knowledge and experience (investor categorisation) in order to assess their suitability for each financial product.34 In recent years, Spanish financial entities have made significant efforts to deliver appropriate information on their offered products to customers and to get a better understanding of their clients' profiles in order to classify them according to their characteristics, background and investment goals.

The effects of anti-money laundering and anti-terrorism financing provisions in the relationships between banks (both Spanish and EU entities rendering services in Spain) and their customers are also worth mentioning. The third AML Directive was implemented by Act 10/2010 of April 28 and the fourth AML Directive was implemented by Royal Decree-Law 11/2018. The obligation to identify the ultimate beneficial owner ("titularidad real") of an entity acting in Spain has become particularly relevant, as has the creation of the Spanish public registry ("Registro de Titularidades Reales"), but there is also a relevant series of provisions imposing multiple reporting obligations on various grounds, in particular, relating to transactions with foreign counterparties.35 Bank secrecy and bank information have also become major issues under discussion. There is a traditional duty on credit entities and their senior management personnel to safeguard and preserve customers' financial information (i.e. balances, products, movements and operations, transactions), keeping it strictly confidential, so it shall not be disclosed to third parties, which applies in addition to general personal data protection regulations. However, Spain does not have a strong "bank secrecy" regime, since the customers' privacy rights may be overcome by various prevailing public interest duties to report to the tax authorities, AML authorities and the supervisor (and, of course, the courts).

In this area, Bank of Spain provides two additional independent public services: (i) Central Information Risk (Central de Información de Riesgos del Banco de España), in short, "CIRBE", which is a database managed by Bank of Spain containing all financial transactions involving banks and individuals. As a result, any individual person may check with Bank of Spain the information

they have about themselves. All bank members of CIRBE may check the database in order to analyse the solvency of a specific customer and its suitability for a product; and (ii) Bank of Spain new Department of Market Conduct and Claims (Departamento de Conducta de Mercado y Reclamaciones del Banco de España or "DCMR") which takes responsibility for the work of the previous Claims Service and adds special expertise on matters related to market conduct, transparency of information, good practices, information to consumers and conflict resolution.36 Therefore, it now deals with all queries and claims from customers in their relationships with credit entities derived from eventual breaches of transparency or customer protection regulation or of good banking practices and financial usages.37 However, before claiming at DCMR, customers must file their claims within the credit entity through its customer service or internal ombudsman in order to have the opportunity to solve the conflict at an earlier stage. For these purposes, consumers may claim before credit entities for facts or events occurring within two years, and credit entities must respond to such claims within two months. Credit entities must file their internal rulings regulating their customer service or internal ombudsman before the Bank of Spain in order to assure they comply with applicable law.

During the financial crisis, the banking sector was also hit by massive litigation involving customers. On one hand, due to the increase of default rates by individuals in residential mortgage loans, foreclosure of mortgages has rocketed in Spanish courts. These judicial proceedings order the eviction of tenants and the immediate sale of the property under an auction process. Evictions are unfortunately widespread and have created social concern, forcing the Government to enact a new framework to protect mortgagee debtors.38 As a result, mortgage enforcement may be suspended or avoided for two years, provided that certain requirements are met by the debtor and their family.

Additional protective measures are foreseen in the future mortgage credit act (implementing the MCD and past-due) under debate at the Spanish Parliament. Restructuring arrangements between debtor and creditor through extensions and write-offs are promoted in order to avoid insolvency situations, and Spanish banks have increasingly adhered to the Good Banking Practices Code for reputational reasons, offering some flexibility in these dramatic social situations. More recently, pursuant to Royal Decree-law 5/2017 of March 17, the moratorium on evicting families in particularly vulnerable circumstances from their primary residence laid down in Act 1/2013 has been extended until 15 May 2020. Moreover, local regulation enacted in certain Spanish regions should also be taken into account when transferring or assigning mortgage loans to third parties. In certain situations, pre-emptive rights vested in the regional government would apply.

The intense litigation continues against financial institutions by investors, bank customers and consumers' associations, claiming unfair practices in the sale of complex financial instruments. It mainly started dealing with participaciones preferentes (preferred quotas),39 quickly extended to other products such as multicurrency loans, Bankia's shares in its IPO,40 etc. and later moved into massive litigation in connection with interest rate floor levels in loan agreements and dealing with costs and expenses attributable to the debtor when entering into a mortgage loan or credit. Some judgments have also declared these provisions abusive, awarding compensation to the debtor. A landmark resolution by our Supreme Court in November 2018 reconciled contradictory

judgements and finally determined that stamp duty costs derived from the granting of a mortgage shall be paid by the debtor/client. Finally, more recently shareholders of Banco Popular are claiming compensation in connection with the Santander acquisition of Popular for one euro. Spanish courts have collapsed under the weight of these massive claims, and Law 7/2017 of November 2, implementing Directive 2013/11/UE, has been enacted in order to promote alternative dispute resolution mechanisms for consumer disputes, through arbitration within the EU.

Also worth mentioning is that Royal Decree-Law 19/2017 of November 24 on payment accounts has incorporated into Spanish law Directive 2014/92/EU of the Parliament and of Council of 23 July 2014, on the comparability of fees related to payment accounts and payment accounts switching.

Finally, as elsewhere in the EU, holders of cash deposits at Spanish credit entities are protected for up to €100,000 per individual by the Deposit Guarantee Fund (Fondo de Garantía de Depósitos de Entidades de Crédito – FGD) according to Royal Decree-law 16/2011 of October 14.

The "shadow banking" system in Spain41

"Shadow banking" or "market based-financing" is an increasing phenomenon in Spain and we can confirm it is already a true alternative source of financing which competes with the traditional banking system. Although direct lending and secondary debt trades were common in other jurisdictions in previous decades, there is no doubt these are quite recent financial activities involving new players in Spain. The spreads offered by private debt funds in Spain have been reduced due to competition and specialisation. As a result, direct lending and traditional financing face competition, particularly in real estate finance and in restructurings when new money is required.

While in other Western jurisdictions non-bank channels could comprise more than 50% of the financial system, in Spain they represent less than 20%, but this has been growing significantly in recent years, particularly in the lending business to SMEs. This rate is further reduced by Bank of Spain to 5% of total assets held by financial institutions, since other financial intermediaries and those entities which do not involve a financial risk are excluded. It is important to note that lending is not a reserved banking activity in Spain. As a result, neither a licence nor an authorisation is required to grant loans and credits (and consequently to become a beneficiary of any related security or guarantee42) in Spain.43

The severe crisis of the traditional Spanish banks and savings entities in need of recapitalisation has led to an extraordinary process of integration in the financial sector, which ended with few active financial players and will further continue its concentration process. In addition, Spanish debt capital markets are complex and not developed enough to fill this gap and the financial needs of the majority of Spanish companies, particularly SMEs. This situation proved to be the perfect combination for debt funds, hedge funds and other special situations and distressed investors to emerge as a credible alternative by providing tailor-made funding structures and flexibility at reasonable financial cost.

In this way, shadow banking has been supplementing Spain's traditional banking system and has positively impacted the recovery process of the Spanish economy by providing liquidity to the financial system, and by participating where traditional local banks could no longer be exposed. Therefore, we see more and more situations in Spain in which debt funds perform bank-like functions and compete directly with traditional lenders.

There is increased speculation about the future introduction in Europe of similar limitations or guidelines to leveraged lending, as now apply in the US since the latest 2013 guidelines (in particular, major concern by the US federal agencies are those transactions where leverage levels would be in excess of 6× Total Debt/EBITDA after planned assets sales). It is quite paradoxical that the EU will be implementing similar measures in the near future now that President Trump plans to introduce more flexibility for financial activities in the US by derogating the 2010 Dodd Frank Act. These restrictions would eventually open a window of opportunity for more debt structuring and non-bank lending. It is a fact that during the period 2015–2018, Spanish banks have been increasing their lending activities and, thereby, reducing the market niche and commercial space available for unregulated debt funds.

In Spain we primarily see these new, highly specialised players and institutional investors in the acquisition of secured and unsecured loan portfolios (either performing or non-performing loans) sold by the Spanish "bad bank" (SAREB) or other sound financial institutions. In addition, they have a special interest in lending to SMEs and short-term financing due to the gap left by the Spanish savings banks. It is also now common to see international alternative and unregulated credit providers and traditional local banks being part of sophisticated restructurings of Spanish large companies. Finally, they are also involved in corporate debt trading and securitisation structures (i.e. sale or refinancing the acquisition of large NPL portfolios through the issue of bonds to be acquired by other investors). In summary, they act as traditional banks except for the collections of funds and deposits from the public, and small and mid-market transactions may benefit from this.

Shadow banking is a global phenomenon which cannot be dealt with or regulated on an isolated basis in each jurisdiction. There is no specific regulation in Spain dealing with these new financiers that are acting without specific regulatory controls, but Bank of Spain has already started monitoring their activities and for now, it does not consider it relevant to require further regulation due to the absence of significant risks. However, since they are not supervised as traditional banks are, they could eventually constitute a systemic risk and unfair competition compared to the status of other supervised financial institutions; in particular, because there are no limitations on leverage and liquidity transformation. Indeed, shadow banking is quite strongly connected with the regular banking system. This is why any approach to regulate shadow banking in order to prevent any potential risk for the financial system, must be discussed broadly at EU level,44 or even globally following recommendations from the G-20,45 the International Monetary Fund (IMF)46 and the Financial Stability Board (FSB).47 The future framework should be accommodated for each category of participant and adjusted to the features and specific activities of these debt investors. Furthermore, any prudential regulatory approach should be harmonised for implementation in each jurisdiction.

Having said this, any individual or entity entering into financial transactions or providing financial services in Spain may be required by the Ministry of Economy to periodically disclose any information in connection with its activities, or be subject to inspections48 by Bank of Spain to confirm whether the activity performed is subject to supervision. Moreover, when the financial activities deal with consumers and granting mortgage loans, the lender (or its servicer in Spain) will be required to be registered at the Spanish Consumption Agency by filing the applicable form (Act 2/2009 of March 31).

No doubt we will have to closely follow how all of these international principles and recommendations affecting these debt providers will be implemented in Spain within the following years. The transformation of the Spanish financial sector will continue and should be adequately monitored to detect business opportunities for international debt providers and investors.

Finally, it is worth mentioning about "cryptocurrencies" (still unregulated in Spain) and other financing alternatives such as "crowdfunding" which is now regulated in Spain under Act 5/1015. As a result, these platforms must comply with certain requirements in order to be incorporated, be previously authorised and registered at the special registers of the CNMV, and not conduct activities limited to investment services providers or credit institutions. In addition, the projects to be funded must be subject to scrutiny rules, and any risk involved disclosed to participants.

ENDNOTES

1. This statement does not hold true if wholesale or investment banking activities are taken into account. Foreign banks play a very significant role in these sectors.

2. Please consider that, unless otherwise stated, we use the term "bank" as meaning the three existing types of banking institution.

3. Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) nº 1093/2010 and (EU) nº 648/2012, of the European Parliament and of the Council.

4. SAREB stands for "Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria".

5. For more information see: http://www.frob.es/en/Paginas/Home.aspx.

6. Section 3.1 of the Credit Institutions Ordination, Supervision and Solvency Act 10/2014 of June 26.

7. For more information, see the latest full report at: https://www.bde.es/f/webbde/INF/MenuHorizontal/Publicaciones/Boletines%20y%20revistas/InformedeEstabilidadFinanciera/IEF_Noviembre2018.pdf.

8. Council Regulation (EU) nº 1024/2013 of 15 October 2013 (SSM) and Regulation (EU) nº 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) nº 1093/2010 (SRM).

9. For more information, check ECB and Bank of Spain's websites: https://www.ecb.europa.eu/home/html/index.en.html and http://www.bde.es/bde/en/, respectively.

10. Since one of the relevant criteria is size, virtually all Spanish banking groups of any material significance are under direct ECB control, since they exceed the €30 billion total asset threshold.

11. Bank of Spain rulings are in the form of Circulares, which develop laws under its regulatory scope.

12. If listed, or in case they issue listed securities of any kind, banks are subject to Securities Markets' discipline and regulations on an equal footing with other issuers.

13. Pursuant to the EU directives, banks are, on the basis of their licence, enabled to provide investment services.

14. SEPBLAC stands for "Servicio Ejecutivo de la Comisión de Prevención del Blanqueo de Capitales e Infracciones Monetarias". For more information: http://www.sepblac.es/ingles/acerca_sepblac/acercade.htm.

15. For more information: http://www.frob.es/en/Paginas/Home.aspx.

16. The Committee of European Banking Supervisors (CEBS), the Committee of European Securities Regulators (CESR) and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS).

17. Please note that, save what will come next about savings banks, we omit references to acts governing structural matters relating to each type of banking institution (for banks, as companies, it would be the Companies Act ("Ley de Sociedades de Capital") and Structural Amendments Act ("Ley de Modificaciones Estructurales").

18. It also implements the CAD for investment services companies other than banks.

19. Act 9/2012 has been developed by Royal Decree 1559/2012 of November 15 on the Regime of Asset Management Companies. Act 9/2012 is now superseded by the BRRD-SRM Regulation and the Spanish Act 11/2015.

20. The most relevant of these are the Accounting Regulation (4/2004) and the Credit Register Regulation (1/2013), but there are many others.

21. For further study we recommend reviewing the summary prepared by F. Vicent Chuliá in his Mercantile Law Manual Book Introducción al Derecho Mercantil, Volume II, 23rd Edition, Tirant lo Blanch, Valencia 2012 pp 1711–1713.

22. Until recently, saving banks (Cajas) and banks were the predominant players in the Spanish banking and credit market. However, as a result of the banking sector restructuring, all saving banks have been transformed either to banks or special foundations. Therefore, we will focus generally on management and corporate governance of banks.

23. Its Chapter IV introduces the corporate governance principles contained in Directive 2013/36/EU of 26 June.

24. In addition, it also applies to credit entities the general regime applicable under Spanish Companies Law (Royal Decree-law 1/2010 of July 2) and Act 31/2014 of December 3, amending RDL 1/2010 on corporate governance.

25. http://www.cnmv.es/DocPortal/Publicaciones/CodigoGov/Good_Governanceen.pdf.

26. As mentioned, since savings banks have virtually ceased to exist, the only other significant form of incorporation of credit institutions is as credit co-operatives. As the name indicates, these are co-operatives and thus subject to the corporate governance structures of a co-operative. Notwithstanding, at least for the large ones, credit institutions governance rules supplement general co-operative rules (setting apart the fact that some of them are also issuers of listed fixed income securities and thus subject to Securities Markets' discipline) so, in practice, corporate governance requirements are very similar to banks'.

27. Vid. Minguez Prieto, R.: Las nuevas tendencias reguladoras sobre el gobierno corporativo de las entidades de crédito (Chapter 31), Corporate Governance, Thomson Reuters Aranzadi, Spain, 2015.

28. On 27 June 2012, Bank of Spain upheld the EBA Guidelines on Internal Governance (GL44) of 27 September 2011. Note that the EBA is working on a revised Guidelines on Internal Governance pursuing further harmonising institutions' internal governance arrangements, processes and mechanisms across the EU. More information is available at: https://www.eba.europa.eu/regulation-and-policy/internal-governance/guidelines-on-internal-governance-revised-/-/regulatory-activity/consultation-paper;jsessionid=86D6D188E67EAA.

29. But for the recommendations of the Basel Committee, provisioning issues are treated in most jurisdictions as a purely accounting matter and thus left to accounting standards. In Spain, given that the Bank of Spain is also an accounting standards-setter for banks, the matter is de facto part of the supervisory/regulatory policy.

30. Mainly: Royal Legislative Decree 1/2007 of November 16 on Protection of Consumers and Users; Act 34/2002 of July 11 on Electronic Commerce (implementing Directive 2000/31/CE of June 8); Act 28/1998 of July 13 on Sale on Instalments; Act 7/1996 on Retail Commerce (as amended by Act 47/2002 of December 19); and Act 7/1998 on General Contractual Conditions (as amended, among others, by Act 44/2006 of December 29, on Improvement of the Protection of Consumers and Users, and Act 3/2014, of 27 March).

31. In addition, other special protective provisions are included in Act 16/2011 of June 24, on Consumer Credit Contracts; and Act 16/2009 of November 13, on Payment Services.

32. Order EHA/1718/2010 of June 11, on Regulation and Control of Marketing of Financial Products and Services; and Order EHA/1608/2010 of June 19, on Transparency of Fees and Information Requirements Applicable to Payment Services.

33. Section 29 of Act 2/2011 of March 4, on Sustainable Economy, has reinforced the protection to customers of financial services by requiring financial entities to provide them with all necessary pre-contractual information and adequate explanations to duly assess if the offered products match their requirements and the eventual effects in case of non-payment. This regime will be reinforced by the implementation of the Mortgage Credit Directive 2014/17/EU on credit agreements for consumers relating to residential immovable property. The Spanish legislator is currently working on a draft of a new act to implement this Directive in Spain.

34. Act 2/2011 on Sustainable Economy regulates the bank's liability as lender to consumers and imposes the duty to conduct adequate assessment on customers' solvency following the criteria established by the Ministry of Finance (Order EHA/2899/2011 of October 28 on Banking Services Transparency and Customer Protection) in order to guarantee the protection to consumers and users of financial services provided by credit institutions. Bank of Spain's Circular 5/2012 of June 27 (as amended by Circular 5/2017 of December 22) deals with the same principles.

35. On anti-money laundering and anti-terrorism financing see also Royal Decree 304/2014 of May

5, Bank of Spain's Circular 4/2012 and the Resolution dated August 10, 2012 of the Secretary General of the Treasury and Financial Policy.

36. For more information, please review the Annual Report available at: http://www.bde.es/bde/es/secciones/informes/Publicaciones_an/Memoria_del_Serv/.

37. According to Bank of Spain's latest information report, in 2016 there were 14,462 claims filed (nearly -28% compared to 2015 which already had a 32% decrease), 1,935 written queries (-40%) and 31,661567 phone queries (-11%).

38. Mainly: Royal Decree-law 6/2012 of March 9; Royal Decree-law 27/2012 of November 15; Law 1/2013 of May 14; and Law 14/2013 of September 27 (Royal Decree-law 6/2012 and Law 1/2013 have been amended by Royal Decree-law 5/2017 of March 17). This regime would also be amended to implement the Mortgage Credit Directive 2014/17/EU on credit agreements for consumers relating to residential real estate property. In addition, please see Act 25/2015 and Royal Decree-law 1/2015.

39. Participaciones preferentes or preferred quotas are a sort of perpetual (subordinated) debt which was issued by many Spanish credit entities in order to obtain funding and improve their capital ratios. Retail banking intensely commercialised this product. Many investors were not aware of the risks involved and as a result of the financial crisis and collapse of some of the financial entities, the value of this product has plummeted.

40. Several judgments from our Supreme Court (SSTS 27 January 2016 nº 23/2016 and 24/2016) declared null and void the subscription of shares of Bankia by minority investors under the IPO transaction. The nullity is based on the lack of due consent since the Supreme Court established the existence of error on the minority investors due to fraud of Bankia because the disclosure of information was not accurate.

41. Minguez Prieto, R.; Buil Aldana, I.: Sistema financiero en la sombra y mercado distressed: una aproximación a sus principales aspectos legales y prácticos, Revista de Derecho del Mercado de Valores, nº 14/2014 (January–June), Spain. Also see the EBA Guidelines' limits on exposures to shadow banking: https://www.eba.europa.eu/regulation-and-policy/large-exposures/guidelines-on-limits-on-exposures-to-shadow-banking.

42. However, note than non-credit entities could be subject to certain limitations when benefiting from certain types of security such as floating mortgages (article 153bis of Spanish Mortgage Law).

43. According to Law 10/2014, there is a narrow concept of credit entity which even sets aside the Financial Establishment of Credit (Establecimientos Financieros de Crédito or EFC). In addition to Law 10/2014 and Royal Decree 84/2015, new regulation over EFCs will be implemented following Law 5/2015 on Promoting Business Finance.

44. COM/2013/0614, Shadow Banking – Addressing New Sources of Risk in the Financial Sector, September 30, 2013. More recently in September 2018, the European Systemic Risk Board published the EU Shadow Banking Monitor (No 3), which is available at:

https://www.esrb.europa.eu/pub/pdf/reports/esrb.report180910_shadow_banking.en.pdf.

45. Vid., Updated G20 Roadmap towards Strengthened Oversight and Regulation of Shadow Banking in 2015 and the Implementation and Effects of the G20 Financial Regulatory Reforms (Fourth Annual Report, November 2018). More information available at: http://www.fsb.org/wp-content/uploads/P281118-1.pdf

46. IMF, "Global Financial Stability report", October 2018. More information available at: https://www.imfconnect.org/content/dam/imf/Spring-Annual%20Meetings/AM18/Public%20Documents/V3%20GFSR%202018.pdf.

47. FSB, Strengthening Oversight and Regulation of Shadow Banking, an Overview of Policy Recommendation, 2013. More information is available at: http://www.fsb.org/wp-content/uploads/r_130829a.pdf; Global Shadow Banking Monitoring Report, 2016. More information available at: http://www.fsb.org/wp-content/uploads/global-shadow-banking-monitoring-report-2016.pdf. Assessment of shadow banking activities, risks and the adequacy of post-crisis policy tools to address financial stability concerns, July 2017. More information available at: http://www.fsb.org/wp-content/uploads/P300617-1.pdf.

48. Additional Disposition 4 of Law 10/2014.

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