

corporate

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UPDATES CORPORATE 5/2013
ROYAL DECREE 256/2013, OF APRIL 12, 2013, INCORPORATING THE
CRITERIA OF THE EUROPEAN BANKING AUTHORITY OR NOVEMBER
22, 2012 ON THE ASSESSMENT OF THE SUITABILITY OF MEMBERS OF
THE MANAGEMENT BODY AND KEY FUNCTION HOLDERS INTO THE
LEGISLATION ON CREDIT INSTITUTIONS

1. INTRODUCTION

Royal Decree 256/2013, of April 12, 2013, incorporating the guidelines of the European Banking Authority dated November 22, 2012 on the assessment of the suitability of members of the management body and key function holders into the legislation on credit institutions and other financial institutions, was published in the Official State Gazette on April 13, 2013 and came into force the day after.

Although the European Banking Authority's nonbinding guidelines refer only to credit institutions, it was decided, for the sake of consistency with the rules on reputation and experience hitherto in force, to make the new legislation applicable to a broader spectrum of financial institutions which, in addition to credit institutions, takes in electronic money institutions, payment institutions, appraisal companies, counter-guarantee companies, foreign currency exchange establishments and mixed financial holding companies.

This has been done by amending the following pieces of legislation (i) Royal Decree 1245/1995, of July 14, 1995, on the creation of banks, cross-border activity and other matters relating to the legal regime for credit institutions; (ii) Royal Decree 84/1993, of January 22, 1993, implementing Law 13/1989, of May 26, 1989, on Credit Cooperatives; (iii) Royal Decree 692/1996, of April 26, 1996, on the legal regime for credit financial institutions; (iv) Royal Decree 775/1997, of May 30, 1997 on the legal regime for the approval of appraisal services and companies; (v) Royal Decree 2660/1998, of December 14, 1998, on foreign currency exchange; (vi) Royal Decree 1332/2005, of November 11, 2005, implementing Law 5/2005, of April 22, 2005, on the supervision of financial conglomerates; and (vii) Royal Decree 712/2010, of May 28, 2010 on the legal regime for payment services and payment institutions.

Because the Bank of Spain is the only organization with the power to authorize the financial institutions subject to this legislation (following the amendment made by Law 9/2012 of November 14, 2012, on the restructuring and resolution of credit institutions) – not the Ministry of the Economy, as was previously the case–, it will be the Bank of Spain that is responsible for assessing the suitability requirements in terms of reputation, experience and good governance.

As we shall see below in greater detail, Royal Decree 256/2013 makes material amendments in three basic areas:

- The commercial and professional reputation of the officials subject to this legislation.
- Experience requirements, which also takes in theoretical training and the assessment of suitability in the management body as a whole.
- Broader, more demanding, good governance rules, particularly, in relation to conflicts of interest.

The new legislation has broadened, generally, the current suitability levels required to carry on the functions of director and general manager and equivalent officials. They have been extended to apply, for the first time, to those responsible for internal control functions and other key positions at the institution and at its parent company, according to what the Bank of Spain may determine.

It also contains a transitional regime for the authorization procedures that have already started and for adaptation of existing institutions to the new legislation.

The Bank of Spain has also been conferred the power to authorize amendments to credit institutions' bylaws, in keeping with the earlier transfer made by Law 9/2012, to the supervisor of the power to authorize credit institutions.

2. REPUTATION CRITERIA

The law provides generally that commercial professional reputation will be found to exist where a person's personal, commercial and professional conduct leaves no doubt as to their ability to carry out sound and prudent management of the institution. The following elements will be taken into consideration in particular:

2.1 Professional history

The legislation gives further details of the evaluation criteria for the professional history of an official. Their relationship with the regulation and supervisory authorities must be looked at; the reasons why they may have been dismissed or removed from previous positions; their personal creditworthiness history; their professional conduct, whether they had held positions of responsibility at credit institutions that have undergone a restructuring or resolution process; or whether they have been disqualified under insolvency legislation.

2.2 Convictions for crimes or misdemeanors and administrative penalties

The assessment of this factor is much more detailed, and the following elements must be taken into account:

- Whether there was willful misconduct or negligence in the crime, misdemeanor or infringement.
- Whether the conviction or penalty is nonappealable.

- The seriousness of the imposed conviction or penalty.
- The defined criminal acts that gave rise to the conviction or penalty, in particular, whether it was a financial crime, money-laundering crime, crime against the social and economic order or a tax and social security crime.
- Whether the acts that gave rise to the conviction or penalty were carried out for the person's own gain or to the detriment of the interests of others where they had been conferred responsibility for administering or managing their business.
- The statute of limitations for the unlawful criminal or administrative acts.
- The existence of mitigating circumstances and the person's conduct after the crime or infringement was committed.

To assess these elements, the Bank of Spain may set up a committee of independent experts to report on the assessment cases in which there have been convictions for crimes or misdemeanors. This committee will not therefore evaluate administrative penalties.

2.3 Material investigations

The existence of material and founded investigations, in both criminal and administrative law will also be looked at, although a supervening lack of reputation cannot not be found to exist simply because those types of investigations are carried out on an assessed person while they are in office.

If, however, while the assessed person is in office, the institution considered that there were any material circumstances requiring assessment of the reputation, it would have to notify the Bank of Spain within 15 business days. Similarly, the assessed persons themselves must notify of any circumstances relating to their reputation.

3. EXPERIENCE

Royal Decree 256/2013 sets out in much greater detail the parameters to be used to judge the suitable experience and know-how that the assessed persons must have. Furthermore, it is now all the board members (not the majority as required before) that must have the suitable experience and know-how.

In this respect, the assessed person must have the suitable level of training and profile to carry out his functions and have had practical experience for sufficient lengths of time (before a period of not less than five years was required). As a new requirement, theoretical know-how must also be looked at, alongside professional experience.

The test for professional experience will take into account the nature, size and complexity of each institution and the specific functions of the assessed person.

Moreover, the board members must have sufficient professional experience between them in the governance of credit institutions to ensure the effective ability of the board of directors to take decisions independently and autonomously to the benefit of the institution.

4. GOOD GOVERNANCE

A new requirement has been placed on directors, who must now be in a position to practice good governance of the institution, which basically translates as broader conflict of interest rules.

For these purposes, (i) the existence of potential conflicts of interest will be looked at in connection with present or past positions held at the institution or at other organizations; and (ii) their personal, professional or economic relationships with other directors at the institution, at its parent or subsidiaries, and with its controlling shareholders.

Another new requirement is to look into whether the person will have sufficient time to spend on their duties.

5. MONITORING COMPLIANCE

5.1 Units and internal procedures

Institutions must now have, in proportion to the nature, scale and complexity of their activities, suitable units and internal procedures to carry out the selection and ongoing assessment of people in assessable positions.

They must identify the key positions in the performance of their business (which now must be assessed also) and that list of people, together with the suitability assessment made by the institution, must be made available to the Bank of Spain.

5.2 Assessment and communication procedure

The suitability assessment will be performed (i) by the institution itself when an application for authorization to carry on banking business is filed with the Bank of Spain, where new appointments are made and in all cases where circumstances arise that make it advisable to reassess suitability; and (ii) by the Bank of Spain itself in connection with the authorization to set up an institution, following receipt of the notification of new appointments, and where the existence of founded evidence makes it necessary to look into whether the serving members continue to be suitable.

Institutions must notify the Bank of Spain of the appointment of new assessable persons within 15 business day from when they are appointed.

5.3 Penalty rules

If these requirements are not met, the Bank of Spain may request the temporary or permanent removal of the director or general manager or similar official, or that the identified shortfalls be remedied. Moreover, the penalty rules in the Credit Institutions (Discipline and Control) Law (Law 26/1988) will be applied, as the case may be.

6. REGISTER OF SENIOR OFFICIALS AT PARENT INSTITUTIONS

Besides keeping the Register of Senior Officials, the Bank of Spain has been given responsibility for creating and managing a register of directors and general managers of parent companies, other than Spanish credit institutions, investment services firms or insurers or reinsurers, on which the directors, general managers and similar officials must obligatorily be entered.

7. TRANSITIONAL RULES

Any administrative authorization processes that have already started before the entry into force of Royal Decree 256/2013 will be authorized under the procedure in force when they were started. The applicants for these processes will have 3 months in which to adapt their applications, where necessary, to the new reputation, experience and good governance requirements.

Existing institutions will have a three month period from the entry into force of Royal Decree 256/2013 (i.e., until July 14, 2013) to put in place the units and internal procedures mentioned above and carry out the selection and ongoing assessment of assessable persons. In the same three month period, they must also notify the Bank of Spain of the existence and material components of their structure.

Institutions also have a six month period following the entry into force of Royal Decree 256/2013 (i.e., until October 14, 2013) to replace their directors, general managers or similar officials and other employees who fail to meet the suitability requirements.

8. IMPLEMENTATION

The Bank of Spain has been given the power to issue the provisions needed to implement Real Decree 256/2013 and, in particular, to specify the information that must be sent to it by the institutions subject to the royal decree, the weighting of the various evaluation criteria for the existence of commercial and professional reputation and good governance, and the adaptation of the know-how and experience criteria to the area in which each type of institution carries on its business.

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