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ABSTRACT

Over the past three years, major reforms have been approved in Spain in order to restructure the banking sector. The purpose of these reforms has been to reinforce the solvency of credit institutions through recapitalization and integration into larger organizations. The credit cooperatives have not presented any solvency problems which would justify these measures being applied to them. The problem that the financial authorities see in their case is their limited size. As a result, the credit cooperatives are immersed in an integration process which is not revolving around the Banco Cooperativo Español (BCE) or the Spanish Association of Rural Savings Banks, as might be expected, but is taking place through mergers between individual institutions and the setting up of various cooperative groups. While the credit cooperatives have not been channelled into bankization (conversion into banks) like the savings banks, ways to become banks have been opened up to them.

KEY WORDS: Cooperative credit, legislation, financial crisis, restructuring process, Spain.

ECONLIT DESCRIPTORS: K290, G010, G210, G280.

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La viabilidad de las cooperativas de crédito españolas tras la reciente regulación sobre capitalización y reestructuración bancaria

RESUMEN: En los últimos tres años se han aprobado en España importantes reformas que han implicado la reestructuración del sector bancario. Esas reformas han tenido por objeto reforzar la solvencia de las entidades de crédito, a través del incremento de sus recursos propios y su integración en estructuras de mayor dimensión. En el caso de las cooperativas de crédito, no han tenido problemas de solvencia que justificasen la aplicación de esas medidas. El problema que para las autoridades financieras presentan las cooperativas de crédito es su reducido tamaño. Las cooperativas de crédito están inmersas por esa causa en un proceso de integración que no se está realizando en torno al Banco Cooperativo Español (BCE) o a la Asociación Española de Cajas Rurales, como cabría esperar, sino a través de la fusión entre entidades individuales y mediante la constitución de diversos grupos cooperativos. Las cooperativas de crédito no se han visto abocadas a un proceso de “bancarización” o transformación en bancos, como las cajas de ahorro, pero sí se han abierto vías para ello.

PALABRAS CLAVE: Cooperativas de crédito, legislación, crisis financiera, reestructuración, España.

Dans quelle mesure les coopératives de crédit en Espagne sont-elles viables après la récente réglementation sur la capitalisation et la restructuration bancaire ?

RESUME : Au cours des trois dernières années, des réformes majeures ont été adoptées en Espagne afin de restructurer le secteur bancaire. L'objectif de ces réformes était de renforcer la solvabilité des établissements de crédit par le biais de la restructuration de leur capital et de leur intégration dans de plus grandes organisations. Les coopératives de crédit n'ont présenté aucun problème de solvabilité qui justifierait que ces mesures leur soient appliquées. Le seul problème que les autorités financières distinguent dans leur cas, c'est leur taille limitée. Par conséquent, les coopératives de crédit sont plongées dans un processus d'intégration qui ne gravite pas autour du Banco Cooperativo Español (BCE) ou de l'Association espagnole des caisses d'épargne rurales, comme l'on pourrait s'y attendre, mais qui se déroule par le biais de fusions entre des institutions individuelles et la création de différents groupes coopératifs. Bien que les coopératives de crédit n'aient pas été prises dans la « bancarisation » (la transformation en banques) comme les caisses d'épargne, des voies vers la transformation leur ont été ouvertes.

MOTS CLÉ : Coopérative de crédit, législation, crise financière, processus de restructuration, Espagne.

1.- Introduction¹

This presentation attempts to explain the situation in which Spanish credit cooperatives find themselves following the recent reform of the financial sector. After referring to the main features that distinguish credit cooperatives in Spain and reviewing the main laws relating to the banking sector that have been passed since 2009, we will look at the effect this reform has had on credit cooperatives. Lastly, we will end with some personal opinions on this process and how it may affect the future of the cooperative credit sector in Spain.

2.- Credit cooperatives in Spain. Main characteristics²

2.1. Recognition in the Constitution

The Spanish Constitution in force since 1978 establishes in article 129.2 that the public authorities shall foster cooperative societies through suitable legislation. The scope of this mandate embraces all cooperatives, including credit cooperatives³. It is the duty of the authorities (Parliament and national, regional and local government) to foster credit cooperatives and to do so through legislation that is appropriate for this purpose.

2.2. Credit cooperatives as credit institutions

Royal Legislative Decree 1298/1986 on 28 of June states that together with banks and saving banks, credit cooperatives are credit institutions.

1.- *This paper is part of a research project funded by the Spanish Ministry of Science and Research, The Social Economy in Public Policy. An economic policy perspective (DER2009-14462-C02-02). It was presented at the ICA Global Research Conference New Opportunities for Cooperatives. Mikkeli, 2011. It has been translated into English by Mary Georgina Hardinge.*

2.- *General studies on credit cooperatives in Spain may be found in SANCHIS J.R. (1997) El crédito cooperativo en España: un enfoque estratégico sobre las cooperativas de crédito, CIRIEC-España; PALOMO, R.J. (2000) Pasado, presente y futuro de la banca cooperativa en España, CIRIEC-España; or PALOMO, R.J. and VALOR, C. (2001) Banca cooperativa: entorno financiero y proyección social, Unión Nacional de Cooperativas de Crédito.*

3.- *FONT DE MORA, P. and CONDE, C. (2003) "Las cooperativas de crédito y la Constitución Española" in CIRIEC- España. Revista de economía pública, social y cooperativa, no. 47, p. 105- 117.*

Being credit institutions, credit cooperatives are subject to the banking regulations, mainly Law 26/1988 on the Discipline and Intervention of Credit Institutions, Law 13/1985 on Investment Ratios, Own Funds and Reporting Requirements of Financial Intermediaries and Royal Decree 2606/1996 on Deposit Guarantee Funds.

Credit cooperatives are the smallest and most numerous of Spain's financial institutions.

2011	Banks	Savings Banks	Credit Coops.
No. of institutions	71	35	80
Assets	€ 1,718,940 M	€ 1,252,424 M	€ 125,259 M

SOURCE: Bank of Spain. Register of Institutions (April 2011) and Statistical Bulletin (2011), <http://www.bde.es>.

2.3. Special legislation: substantive and fiscal, national and regional

Credit cooperatives are not only financial institutions but also cooperatives, however, and as such, they are subject to the laws on cooperatives.

In Spain, the nation (the State) and the regions (Autonomous Communities) share the power to legislate on cooperatives, but the basic rules on banking and credit matters are the responsibility of the State.

Credit cooperatives are governed by national Law 13/1989 on Credit Cooperatives and their pursuant Regulations (Royal Decree 84/1993). Secondly, they are also governed by the applicable Cooperatives Act (national Law 27/1999 of 16 July 1999 or the regional cooperative law). Some regions have also developed the legislation on credit cooperatives further (Law 5/2001 in Extremadura and Decree 83/2005 in the Valencia region).

Lastly, Law 20/1990 of 19 December 1990 on the Tax System for Cooperatives also applies to credit cooperatives, particularly articles 39 and 40⁴.

2.4. Peculiarities of their legal status

Credit cooperatives can also be called rural savings banks (*cajas rurales*) when they provide their financial services in country areas. Setting up a credit cooperative requires authorization from the Economy and Treasury Ministry, following a report from the Bank of Spain, and registration in the Cooperatives Register, the Company Register and the Bank of Spain's Register of Institutions.

4.- For more information on credit cooperatives in the Spanish legal system see VICENT (1994) "El nuevo estatuto jurídico de las cooperativas de crédito" in *Revista de Derecho Bancario y Bursátil*, no. 53, p. 9-52 and no. 54, p. 305-337; and VALENZUELA and VALENZUELA (2007) "Las cooperativas de crédito en el vigente ordenamiento jurídico español (una visión sintética)" in *Estudios de derecho de sociedades y derecho concursal: libro homenaje al profesor Rafael García Villaverde Vol. 3*, p. 1609-1632.

Credit cooperatives can engage in the same transactions as other financial institutions. They have to give priority to attending to their members' needs and their transactions with non-members must remain below 50% of their total funds. The Government sets the required level of capital for founding and running a credit cooperative according to the area in which it will operate and the population of that area.

Credit cooperative members can be individual or legal persons. Every member must hold at least one certificate of contribution to the cooperative's capital with a value of no less than € 60. The total contributions of each member may not exceed 20% of the capital in the case of a legal person or 2.5% for an individual. Under no circumstances may legal persons that are not cooperatives hold more than 50% of the cooperative's share capital.

The shareholders' return on paid-up capital may not be greater than 6 points above the legal rate of interest and after covering the losses of previous years and subtracting taxes and compensation on capital, a minimum of 20% of the profit has to be allocated to the indivisible Obligatory Reserve Fund and between 10% and 30% to the cooperative's Education and Promotion Fund. The remainder can be allocated to dividends or voluntary reserves.

Each member has one vote at the General Meetings, although the articles of association can decide that the vote will be weighted in proportion to the capital or work contributed, or to the membership of the cooperative members. The majority of the board of directors must be members and their liability is equivalent to that of the directors of a *sociedad anónima* (approximately equivalent to a public limited company) if the post is remunerated.

From the tax point of view, credit cooperatives are fiscally protected: their profits attract 26% company tax compared to 35% for banks.

2.5. The organization of cooperative credit in Spain

The Spanish Association of Credit Cooperatives was founded in 1989 and changed its name to Spanish Association of Rural Savings Banks (*Asociación Española de Cajas Rurales*) in 1995. Practically all the rural savings banks belong to it. This association is the core of the Grupo Caja Rural, which also includes a bank (*Banco Cooperativo Español S.A. BCE*) and other organizations set up in the 1980s to provide services to the group, such as Rural Servicios Informáticos (IT services) o Rural Grupo Asegurador (insurance).

All the credit cooperatives also belong to the National Union of Credit Cooperatives (*Unión Nacional de Cooperativas de Crédito*), which represents them and defends their interests.

It should be pointed out that the credit cooperatives usually remain aloof from the cooperative federations and that of the social economy (CEPES).

Among the 80 credit cooperatives in existence in 2011, 76 are rural savings banks and the rest are credit cooperatives set up by professional groups (engineers, lawyers, architects) or as part of a cooperative group (Grupo Mondragón's Caja Laboral Popular).

2.6. Credit cooperatives as social economy institutions

The Spanish Parliament recently passed Law 5/2011 of 29 March 2011 on the Social Economy. Its purpose is to establish a shared legal framework for all the organizations that make up the social economy, with full regard for the specific rules that apply to each of them, and to determine measures to foster them, in recognition of their characteristic aims and principles (article 1).

This law defines the social economy as the body of activities carried out by organizations that pursue the collective interest of their members and/or the general interest, whether economic or social or both, and operate according to certain guiding principles. In article 5 it identifies cooperatives as social economy organizations and its preamble justifies this insofar as the different types of cooperative, including credit cooperatives, share the guiding principles of the social economy.

In accordance with the ultimate purpose of this law, article 8 considers the promotion, encouragement and growth of social economy organizations and their federations to be in the general interest. This should be materialized in actions such as removing the obstacles that prevent social economy organizations from starting and expanding an economic activity, or promoting the principles and values of the social economy.

3.- Recent changes in the law with an impact on credit cooperatives

3.1. Changes to the system for conversion of credit cooperatives

Law 3/2009, passed on 3 April 2009, regulates structural changes in commercial companies (conversion, merger, split or general assignment of assets and liabilities). It does not affect cooperatives directly, as in law they are not considered commercial companies, but some of the provisions are applicable to them. One of these is the Fourth Final Provision, which modifies the Credit Cooperatives Law by establishing, among other matters, that when a credit cooperative is converted into a different type of credit institution, its Obligatory Reserve Fund becomes part of the share capital of the resulting company.

This rule has subsequently been confirmed by Law 2/2011 of 4 March 2011 on the Sustainable Economy, which specifies that the balance of the Obligatory Reserve Fund of a converted credit cooperative may become part of the share capital of the resulting company in the 2011 financial year (Ninth Transitory Disposition).

3.2. Banking sector reorganization and recapitalization of credit institutions involved in integration processes

Royal Decree Law 9/2009 on bank restructuring and credit institution equity reinforcement was passed on 26 June 2009. This instrument aims, on the one hand, to increase the solvency and strengthen the management of credit institutions that find themselves in difficulties by means of an orderly reorganization of the banking system and, on the other hand, to support integration processes among credit institutions that are not in difficulties but wish to improve their medium-term efficiency. According to this law, such integration processes can include, among others, what are known as Institutional Protection Systems, which have aims that can be considered similar to those which are generated in a merger as regards the way they operate, the adoption and execution of policies and strategies by the organizations in question and the institution and exercise of their internal and risk management controls.

To carry out both processes (restructuring and recapitalization), this law set up the Fund for Orderly Bank Restructuring (Fondo de Reestructuración Ordenada Bancaria FROB). This fund has an initial endowment of € 9,000 million and can seek external funding of up to 10 times this initial sum on the equity markets. It will provide assistance by buying convertible preference shares with a five-year conversion date⁵.

3.3. Recapitalization of the credit institutions

Royal Decree Law 2/2011 for the reinforcement of the financial system was passed on 18 February 2011. This law takes measures that aim to reinforce the capital of the credit institutions. Its preamble justifies these measures on the grounds that doubts have been expressed about the soundness of Spain's financial system and in order to dispel any uncertainty, it must be ensured that all the institutions in the Spanish banking system possess top-quality capitalization levels.

5.- This assistance is subject to the limitations and conditions set out by the European Commission in several Communications since 13 October 2008. It was approved by the Commission and its closing date was subsequently extended. On the compatibility between this assistance and Competition Law see URIA, F (2010) "Crisis financiera, mecanismos de apoyo a las entidades de crédito en dificultades y Derecho de la competencia" in Estabilidad Financiera, Banco de España, no. 18, p. 85-108.

The measures set out in this Royal Decree Law are:

- a) Reinforcement of capital through early application of the new international capital requirements (Basle III).
- b) Adaptation of the FROB as a public policy instrument to facilitate the required capitalization levels.

4.- Credit cooperatives and the bank recapitalization process

The law on reinforcement of the financial system (RDL 2/2011) requires financial institutions that may take deposits of repayable funds from the public to possess a core capital of at least 8% of their total risk-weighted assets, rising to 10% when these institutions meet the following two conditions:

- a) They have a wholesale funding ratio of over 20%
- b) They have not placed certificates of equity ownership or voting rights representing a percentage of 20% or more of their capital with their members or shareholders (article 1).

Core capital is defined as including, among others, contributions to the capital of the credit cooperatives and their joining fees and reserves, whether statutory or required by their articles of association (article 2).

The new core capital level was required by 10 March 2011 and if an institution was unable to meet the requirement, it was required to submit a strategy to the Bank of Spain within 15 days with a calendar for completion by 30 September 2011. The strategy could include attracting funds from third parties, stock market listing or resorting to funding from the FROB (First Transitory Provision).

The 10% core capital requirement is aimed at the **savings banks** that have a wholesale funding ratio in excess of 20% because their legal form is a foundation, they have no members and although it is possible for them to issue participation shares, such issues have been neither frequent nor sufficient. The reason the preamble to this law gives for this discriminatory treatment is that these institutions find it less easy to raise capital if they need to do so.

The higher capital requirement that has to be achieved within 6 months is giving rise to mergers between savings banks and their conversion into banks in order to be able to offer shares to third parties, including the FROB. Whichever option is taken, whether seeking private capital investors (institutional or otherwise), stock market listing or acquiring a public shareholder, the savings banks have

to be converted into public limited companies (become banks) or set up banks and transfer their business to them.

The only savings banks that will be allowed to retain their present form are ones of limited size that have not had recourse to a high percentage of wholesale funding. The savings banks of Ontinyent (Valencia) and Pollença (Mallorca) are in this situation.

Turning now to the **credit cooperatives**, since they are cooperatives all their capital is shared between their members and they have barely used any wholesale funding to meet their needs. Consequently, the core capital ratio required of them is 8%.

On 10 February 2011 the Bank of Spain revealed the solvency ratios of Spanish banks, noting that all the credit cooperatives were above the required 8% level. Also, even if they needed to increase their capital they could seek funding from their members and third parties, including the FROB, without needing to become banks.

5.- Credit cooperatives and reorganization of the banking sector to rescue institutions in difficulties

The purposes of the above-mentioned Royal Decree Law 9/2009 include strengthening the solvency and management of credit institutions that find themselves in difficulties through an orderly reorganization of these institutions.

The preamble to this law recognizes that the viability of some medium or small credit institutions could be jeopardized as a result of the current recession, which is characterized by a hardening of conditions for obtaining funding on the market, deterioration of property-based asset values, an increase in bad debts and a shrinking business.

Under normal circumstances this situation would be remedied by the measures provided in law (Royal Decree 2606/1996 on the legal regime of Credit Institution Deposit Guarantee Funds). However, the present situation is not considered normal, as it affects numerous institutions and could potentially generate a systemic risk, so additional instruments and public resources need to be provided in case they need to be used.

This was the reason for setting up the FROB, with the mission of managing credit institution reorganization processes and helping to reinforce their equity.

The restructuring process comprises three successive stages (articles 6 and 7):

- 1) Private solutions must be sought to reinforce the solvency of the institution at risk.
- 2) If it has not proved possible to solve the situation privately, an action plan for one of the following must be submitted to the Bank of Spain: reinforcement of the institution's assets and solvency; its merger or takeover; or total or partial transfer of its business or of business units. These measures will have the support of the sector's Deposit Guarantee Fund.
- 3) If the weakness persists despite the above measures, the FROB will intervene.

In this last stage, the institution's management will be replaced by administrators appointed by the FROB, who will draw up a Plan to restructure the institution through merging it with another or other institutions of recognized solvency or by transferring part or all of its business to other institutions through general or partial assignment of its assets and liabilities. This Plan must set out the form that the FROB's support will take in terms of both financial support measures and management measures.

The financial support measures can consist in providing guarantees, loans under favourable terms or subsidiary funding, or acquiring any type of asset shown on the institution's financial statements or subscribing or acquiring securities representing its equity ownership.

The investments made by the FROB in executing a restructuring plan will not be subject to certain legal limitations or obligations, such as restrictions on attending general meetings, voting rights, etc.

Should a credit cooperative undergo a banking reorganization process, the FROB could contribute to its funds by subscribing or acquiring contributions to its capital (article 7.3 a). In this case, the legal limitations on the acquisition of contributions to credit cooperative share capital by legal persons shall not apply and the right to vote in the assembly shall be in proportion to the share capital represented by the contributions acquired or subscribed (articles 7.6 c and 7.9).

The credit cooperatives have also suffered the consequences of the recession⁶ but unlike the savings banks, they have had higher levels of equity, have not had recourse to international funding, have been conservative about opening new branches outside their native areas and have taken a smaller part in funding the property sector, the cause of the crisis in Spain. As a result, to date they have not created any solvency problems that would make it advisable to subject them to the reorganization process we are examining⁷.

6.- According to data supplied by the Bank of Spain, credit cooperative profits fell from € 774 million in 2007 to € 256 million in 2010.

7.- Some recent writings on the financial crisis and the credit cooperatives may be cited here: CALVO and PAUL (2010) "Las cajas de ahorros y las cooperativas de crédito ante la crisis: evolución en su presencia territorial y en su operativa" in REVESCO. *Revista de estudios cooperativos*, no. 100, p. 68-100; SEGUÍ and SERVER (2010) "Las cooperativas de crédito y su entorno en el contexto de la crisis bancaria: análisis de su capital relacional como base desde la que explotar oportunidades" in CIRIEC-España. *Revista de economía pública, social y cooperativa*, no. 68, no. 35-59; or ENCINAS and ESCRIBANO (2011) "Evolución comparada del modelo de negocio de las cooperativas de crédito en el contexto de la crisis financiera" in *Boletín económico de ICE, Información Comercial Española*, no. 3006, p. 43-61.

6.- Credit cooperatives and integration. The institutional protection system (SIP)

6.1. Integration to resize credit institutions

One of the most salient features of the Spanish banking system has been the small size of its institutions. The financial authorities consider this a weakness and have tried to combat it by encouraging mergers and takeovers.

The first bank mergers took place in the 1980s. Currently only two Spanish banks, Santander and BBVA, are of a size that can be considered internationally competitive⁸.

Integration between savings banks and between credit cooperatives mainly occurred in the 1990s. The credit institutions were integrated with different legal forms. Law 12/1989 on Credit Cooperatives and its pursuant regulations (Royal Decree 84/1993) made it possible for credit cooperatives to integrate with banks and savings banks, mainly through global assignment of assets and liabilities⁹.

Despite these integration processes, at the end of 2008 there were 66 banks, 46 savings banks and 83 credit cooperatives registered in Spain¹⁰.

Royal Decree Law 9/2009 was passed in 2009, as we have already mentioned. As well as regulating the reorganization of banking institutions in difficulty, it also provided for measures to support integration between credit institutions that are not encountering difficulties but wish to improve their efficiency in the medium term.

The preamble to this law considers that in the present climate, integration is necessary in order to obtain equity on the wholesale markets. The experts emphasize that when wholesale capital markets are called upon to provide funds, the cost of these liabilities varies according to each institution's credit rating, and the rating agencies' calculations are based not only on solvency but also on size. The international markets are said to distrust small financial intermediaries more than large ones. Solvency alone does not suffice to achieve a good rating, it needs to be accompanied by volume, and it is the credit institutions with the best ratings that find it easiest to obtain international loans¹¹.

8.- According to a financial report the Spanish Banking Association (AEB) published in March 2011, as of December 2010 the Santander group had consolidated assets worth over € 1217 billion (US thousand billion) and those of the Banco Bilbao Vizcaya Argentaria (BBVA) group exceeded € 552 billion. See <http://www.aebanca.es/internet/groups/public/documents/publicaciones/18-201101144.pdf>.

9.- On these processes, see VAÑÓ, M.J. (2001) *Fusión heterogénea y cesión global en el sector bancario*, Tirant lo Blanch, Valencia.

10.- All the data on the number of registered credit institutions cited in this paper have been published on the Bank of Spain website. See <http://www.bde.es/webbde/es/secciones/servicio/regis/regent.html>.

11.- The Bank of Spain report of December 2010 on the situation and prospects of the Spanish banking sector (*Situación y perspectiva del Sector Bancario Español*) analyzes the legislation to support integration among the credit institutions and emphasizes that their aim is to achieve larger institutions which, among other things, will enjoy lower funding costs, as greater size makes it easier to obtain funding on the markets. <http://www.bde.es/webbde/es/secciones/prensa/situacion/actualizacionsectorbancarioesp122010.pdf> (see p. 21).

Integration, which will receive support from FROB funds, can take the form of a merger or can be carried out through an Institutional Protection System (SIP), which has similar aims to those generated in a merger.

The measures to support the integration of credit institutions are aimed at all the types: banks, savings banks and credit cooperatives. According to the Governor of the Bank of Spain, it makes no sense to have credit institutions with assets of under € 70,000 million¹².

From December 2009 to December 2010, integration processes between savings banks reduced their number from 46 to 35. These processes took the form of mergers and takeovers. Savings banks are also integrating through Institutional Protection Systems (SIP), whereby they preserve their legal personality but set up banks and transfer their business to them¹³. These processes will continue if the Banks of Spain's objective, as is being said, is no more than 17 savings banks in no more than 6 groups with assets of around € 80,000 million each.

Some smaller banks will probably also use the SIP system to merge with each other and with other credit institutions in the coming months.

Credit cooperatives are the smallest and most numerous of the credit institutions. Over the past 10 years their number has fallen from 94 to 80, but the Bank of Spain still considers that there are too many and they are too small. In total, the 80 credit cooperatives have assets worth € 125,259 million, of which over € 30,000 million belong to the Cajamar group and € 21,210 million to the Caja Laboral Popular, the two largest.

The credit cooperatives are also involved in integration processes, mainly mergers and SIPs.

6.2. Credit cooperative integration

Credit cooperatives are also being called upon to integrate. Indeed, given their limited size, they are the institutions that most need to do so, according not only to the authorities but also to the sector itself¹⁴.

They can employ various methods: merger, general assignment of assets and liabilities, cooperative groups or institutional protection systems¹⁵.

12.- Remarks published on 28 February 2011 in the Spanish business newsletter *Intelligence & Capital News Report*, no. 692.

13.- Banco Financiero y de Ahorros (Bankia), Banco Base, Banca Cívica or Banco Mare Nostrum.

14.- According to the secretary general of the National Union of Credit Cooperatives (UNACC), "The credit cooperatives do not have a solvency or bad debt problem but a size problem, and they are already laying the foundations for a more solid future, which will allow them to gain competitive strength" (<http://www.finanzas.com/noticias/bolsas/2011-02-18>).

15.- On credit cooperative concentration see BELMONTE and CORTÉS (2010) "La concentración del sector de cooperativas de crédito en España" in CIRIEC-España. *Revista de economía pública, social y cooperativa*, no. 68, p. 223-246; and on cooperative integration instruments, VICENT CHULIÁ, F. (2010) "Sistemas institucionales de protección (SIP) y reestructuración bancaria, como derecho paraconcursal" in *Revista Derecho Concursal y paraconcursal*, no. 13, p. 47.

a) Merger

Traditionally, cooperatives have been allowed to merge, but only with other cooperatives¹⁶. Law 13/1989 of 26 May 1989 on credit cooperatives appeared to allow mixed mergers, but without expressly saying so¹⁷. This possibility was confirmed when the regulations pursuant to this law (Royal Decree 84/1993 of 22 January 1993) were approved, as article 30 regulated the authorization requirement for mergers involving credit cooperatives and allowed various types of merger. As well as mergers between credit cooperatives and with cooperatives in general, it provides for mergers with other deposit-takers when a merger proposal has not been taken up by other cooperative sector companies within a stated period of time. Later, the Cooperatives Act currently in force (Law 27/1999 of 16 July) expressly allowed cooperatives to merge with partnerships or commercial companies of all kinds, provided that no legal rule prohibits it¹⁸. According to this law, the legislation that applies to these processes is that of the company that absorbs the other or others or that is founded as a result of the merger, but as regards the adoption of the agreement and the guarantees for the members and creditors of the cooperatives taking part, the provisions of cooperative law apply. Lastly, if the company formed by the merger is not a cooperative, the obligatory legal reserves, which are indivisible, do not become assets of that company (article 67).

b) General assignment

Mergers are allowed between institutions with members or shareholders (banks and credit cooperatives), but not between credit cooperatives and savings banks, as the latter are foundations. As a result, the mechanism used in these cases is a general assignment of assets and liabilities. The credit cooperatives regulations envisaged this possibility, but it has not been regulated in the cooperative laws¹⁹. For commercial companies, general assignment of assets and liabilities is regulated by Law 3/2009 of 3 April 2009 on structural modifications (articles 81 to 91). While law 3/2009 does not apply directly to cooperatives, in the event of legal omission such as this it can be applied by analogy.

c) Second-tier cooperatives and cooperative groups

Another way that cooperatives can integrate is to set up second-tier cooperatives and cooperative groups.

16.- Article 94 of Spain's Cooperative Law 3/1987 of 2 April 1987, provided for cooperatives' merging to form a new cooperative, or one or more being taken over by an existing cooperative.

17.- Article 10 states that "in the event of the institution resulting from the merger ... being a credit cooperative ...", implying that the result of the merger could be a different type of organization.

18.- For more detail on cooperative mergers, particularly in credit cooperatives, see FAJARDO (2006) "La fusión de cooperativas en la legislación española" in CIRIEC-España. *Revista jurídica de economía social y cooperativa*, no. 17, p. 35-84.

19.- An exception was the Valencia region's Cooperative Law 3/1995 of 2 March 1995, which regulated the general assignment of assets and liabilities. It required the agreement to be taken with the same majorities required for changes in the articles of association and to set out the conditions of assignment, taking into account an independent expert's valuation of the assets and liabilities assigned. This agreement had to be made public and had to recognize the right of the assigner's and assignee's creditors to oppose it, under the same conditions and with the same effects as in the case of mergers (article 67).

Second-tier cooperatives have to be set up by at least two cooperatives, but they can also have members that are other types of legal person, public or private, up to a maximum of 45% of their total membership. Their purpose can be to promote, coordinate and carry out the shared economic aims of their members, but they can also reinforce and even integrate the economic activities of the latter. No member of a second-tier cooperative may hold more than 30% of its share capital (Cooperatives Law 27/1999, article 77).

Cooperative groups were first mentioned in Spanish law when the arrangements for taxing the consolidated profits of groups of companies were adapted to cover groups of cooperatives (Royal Decree 1345/1992 of 6 November 1992).

Shortly afterwards, cooperative groups were regulated by Cooperatives Law 27/1999 (article 78), which defined them as groups formed of several cooperatives, whatever their class and whatever the organization heading the group that exercises powers or issues instructions that the cooperatives in the groups are obliged to carry out, such that unity of decision occurs within the scope of these powers. The issuing of instructions can involve the spheres of management, administration or governance of the cooperatives and the agreements in this regard can consist, among others, in establishing common rules through the articles of association or through internal regulations, in relationships of association between the primary tier cooperative members or in undertakings to supply resources.

d) Institutional Protection Systems

An Institutional Protection System or Institutional System of Protection (*Sistema Institucional de Protección – SIP*) is a contractual mutual assistance mechanism. It was introduced into the Spanish financial system by Royal Decree 216/2008 of 15 February 2008 on the shareholders' equity of credit institutions and the Bank of Spain's Circular 3/2008 of 22 May 2008 on determining and controlling the minimum equity of credit institutions. These effect the incorporation into Spanish law of article 80.8 of European Parliament and Council Directive 2006/48/CE of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions, which, in turn, gives concrete form to the Basle Agreement on Banking Supervision (Basle II).

The initial objective of the SIP is not integration but protection in crisis situations. As Martín de Vidales²⁰ says, it does not emerge from a reading of the SIP rules that this system is any kind of integration mechanism, but rather one to reinforce solvency and liquidity whereby some institutions take responsibility for others and common rules on risks and risk control are demanded of them. The SIP rules require united decisions on certain matters but do not require any sharing of human or material resources.

20. - MARTÍN DE VIDALES (2010) "El SIP como fórmula de integración de entidades financieras" in *Revista de derecho del mercado de valores*, no. 6, p. 242.

However, while the SIP is not necessarily an integration mechanism it can become one, essentially because its scant regulation makes it possible to reach agreements for greater involvement between the participants. This gradation makes it possible to differentiate between:

- Soft or regulation SIPs that only aim to strengthen their solvency and liquidity through a mutual guarantee mechanism and centralization of their risk management, without mutualising profits.
- Strong or reinforced SIPs where as well as the above undertakings, at least 40% of the equity and profits of each of the institutions taking part are mutualised and an institution is set up to head the group.
- Highly reinforced SIPs, with mutualisation of 100% of the participants' profits.

A SIP can constitute a consolidatable group, bearing in mind that control over another company can be achieved not only by holding the majority voting rights or the right to appoint the majority of the directors in the controlled companies, but also through integration and shared control agreements such as those setting up a SIP. In fact, as Mínguez points out²¹, the formulae the credit institutions are being offered do not answer to the idea of a SIP but to the better-known concept of the contractual group.

For instance, Law 13/1985 of 25 May 1985 on investment ratios, own funds and reporting requirements of financial intermediaries states that a group of credit institutions can be considered a consolidatable group if it forms a SIP through a contractual agreement and meets certain requirements: a central institution that takes binding decisions on the group's business policies and strategies as well as its internal and risk management control levels and measures; the contractual agreement setting up the SIP contains a mutual solvency and liquidity undertaking between the participant institutions that covers at least 40% of the equity of each; a significant proportion (at least 40%) of their results are pooled and distributed in proportion to the share of each; the agreement establishes a minimum 10 year continuance in the SIP; etc. (article 8).

However, the law that most clearly sees the SIP as an integration formula is probably Royal Decree Law 9/2009, which we referred to earlier. This set up the FROB, with aims that include supporting processes to integrate credit institutions. As its preamble states, these processes can comprise (among others) SIPs that have similar objectives to those generated during a merger as regards their operating methods, the definition and execution of the participant institutions' policies and strategies and the introduction and implementation of their internal and risk management controls.

21.- MÍNGUEZ (2010) "Estructuras de integración contractuales entre entidades de crédito: los denominados Sistemas Institucionales de Protección. Situación tras los Reales Decretos-Leyes 6/2010, de 9 de abril y 11/2010, de 9 de julio" in *Revista de derecho del mercado de valores*, no. 7, p. 9.

The similarity mentioned by this Royal Decree Law has led to these processes being described as 'cold fusion' (*fusión* is also the Spanish for 'merger'). However, unlike a merger, a SIP does not dissolve and extinguish the legal persons that comprise it, nor do these lose their legal personality. Also, mergers unite the entirety of the assets of all the companies involved, whereas the institutions participating in a SIP are under no obligation to hold their assets in common; even in an integration SIP they only share the assets they have agreed to, not their entire equity.

This institutional integration system can be applied by any group of credit institutions and therefore also by **credit cooperatives**²².

In 2005 the Bank of Spain tried to persuade all the credit cooperatives to consolidate their balance sheets with the Banco Cooperativo Español, but the proposal did not succeed²³.

Later, in 2008, following the approval of its Solvency Circular (3/2008), the Bank of Spain urged the credit cooperatives to set up an Institutional Protection System (SIP).

Up to that point, the cooperatives in the Caja Rural group had not only the statutory Deposit Guarantee Fund but also an internal solidarity fund to tackle situations of insolvency among its members. However, this mechanism could only be activated if there was sufficient consensus within the association. A SIP makes it possible to act more swiftly, as it does not need a decision by the meeting of the Spanish Association of Rural Savings Banks to start operating. Also, the SIP controls non-compliance by its members and conducts its own risk assessments.

On 8 May 2009, four rural savings banks set up the first SIP in Spain, the Grupo Cooperativo Cajamar. It is a soft SIP, with no mutualisation of profits. Since then a number of mergers have taken place, new SIPs have been set up and existing ones have grown as new credit cooperatives have joined them.

Since the first of these, the Bank of Spain is now only authorizing SIPs that mutualise all their profits and give each other unlimited support.

To date, the SIPs set up by credit cooperatives have either made an existing credit cooperative their central institution or have formed a second-tier cooperative, but it would also be possible for them to create SIPs based around banks and transfer their business to these, as the savings banks have done.

22.- On the application of these systems to credit cooperatives see PALOMO and SANCHIS (2010) "Los Sistemas Institucionales de Protección (SIP) en las entidades financieras de economía social: su aplicación en las cooperativas de crédito" in *Creando clientes en mercados globales: Building client relationships in global markets* (coord. Redondo López).

23.- Among the reasons mentioned for this failure are that consolidation of the accounts was more demanding as it required solidarity and involved setting up a central body to control the solvency of the institutions, with the power to issue binding instructions, and that neither Cajamar nor DZBank (both large BCE shareholders) took part in the initiative to consolidate the accounts.

7.- ‘Bankization’ or converting credit cooperatives into banks

The rules discussed earlier have led most of the savings banks to set up banks and obliged them to transfer their entire business to these, which in the medium term could bring about the disappearance of savings banks as a legal form of company. This process, which has been justified by the need to recapitalize, has been termed the bankization of the savings banks.

As the credit cooperatives have no solvency, liquidity or bad debt problems, do not use the international wholesale markets for funding and have share capital that can be acquired by members and others, for the time being they have not found themselves compelled to become banks or to set up banks and transfer their business to them.

Owing to their size, however, they do find themselves obliged to undertake integration, and while these processes do not require them to become banks it is certainly possible for them to merge with banks or to set up a bank to head the Institutional Protection System group and transfer their business to it.

These risks of bankization have been joined by a new rule, approved on the grounds that the equity of the credit institutions needs to be reinforced, which constitutes an incentive to convert credit cooperatives into banks. Law 3/2009 on structural modifications in commercial companies has modified credit cooperative law by introducing the rule that when a credit cooperative is converted into a different type of credit institution (a bank), its Obligatory Reserve Fund becomes part of the share capital of the resulting institution.

The main question this raises is who owns the shares that correspond to the fund which has become part of the share capital. In the Spanish Parliament it was argued that these shares should be distributed among the cooperative members turned shareholders. We argue that the ownership of these shares belongs to those who would be the assignees of these funds in the event of conversion of the cooperative in accordance with cooperative law and the articles of association of the cooperative²⁴.

Subsequently, Law 2/2011 on the Sustainable Economy has extended the possibility of assigning the Obligatory Reserve Fund to share capital to cases in which a credit cooperative has already been converted into a bank, irrespective of how this fund had been assigned. This is a retroactive rule and its interpretation and application may create serious problems.

24.- FAJARDO (2010) "Aspectos de la transformación de las cooperativas de crédito tras la ley de modificaciones estructurales de 2009" in *Estudios de Derecho del Mercado Financiero. Homenaje al Profesor Vicente Cuñat, Universitat de Valencia, p. 91. As the European Commission says, asset-stripping and 'de-mutualisations' must be avoided and on conversion of a cooperative, its assets should be distributed according to the principle of disinterested distribution (Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions on the Promotion of Co-operative Societies, 2004).*

8.- Conclusions

There have been credit cooperatives in Spain since the end of the 19th century. They have been regulated by special laws that are common to all of them (despite the plurality of Spain's cooperative legislation). These laws have respected the cooperative principles (although they have allowed voting rights in proportion to capital) and have allowed credit cooperatives a tax regime of their own in accordance with their characteristics.

As credit institutions, credit cooperatives are subject to the control and supervision of the Bank of Spain and like banks and savings banks, they can conduct all kinds of banking activities.

According to Spanish law, credit cooperatives should be encouraged, because they are cooperatives (Spanish Constitution, article 129.2) and because they belong to the Social Economy sector (Law 5/2011).

Over the past three years, major reforms have been approved in Spain in order to restructure the banking sector.

The purpose of these reforms has been to reinforce the solvency of credit institutions through recapitalization and integration into larger organizations.

The credit cooperatives have not presented any solvency problems which would justify these measures being applied to them. The problem that the financial authorities see in their case is their limited size.

As a result, the credit cooperatives are immersed in an integration process which is not revolving around the Banco Cooperativo Español (BCE) or the Spanish Association of Rural Savings Banks, as might be expected, but is taking place through mergers between individual institutions and the setting up of various cooperative groups.

While the credit cooperatives have not been channelled into bankization (conversion into banks) like the savings banks, ways to become banks have been opened up to them.

Time will tell whether these reforms will help to strengthen the cooperative credit sector or will hinder its growth.

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