

The Credit Cooperative System in Spain

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Abstract Like other European countries, Spain has a long tradition of cooperative banks. Although some credit unions existed previously, essentially they date from the early twentieth century, originating as institutions founded by medium and small-sized farmers to improve their access to banking services. However, they occupied a marginal position in the financial system until the legislative reforms of the 1970s. During the two last decades of the twentieth century, Spanish cooperative banks suffered a deep crisis, two changes in their organizational model and the shock of transformation and innovation in the financial system. Currently, the sector is made up of 65 small institutions with a relatively small market share: slightly over 4.4 % of total assets. Their model of organization has been threatened by weak cohesion and by not behaving as a true group. The financial crisis that started in 2007 affected Spanish cooperative banks less than other institutions, especially saving banks, because they held higher levels of capital and their business was retail-oriented. The more competitive environment nowadays could jeopardize the valuable principals which inspire the cooperative movement. Economic viability can and must be compatible with the democratic principle of ‘one member, one vote’, with enhancing ownership participation, with neighbourhood and community, with transparency and with their combination of social and financial objectives.

1 The Establishment and Evolution of the Credit Cooperative System in Spain

Although some credit unions were set up at the end of the nineteenth century, the Spanish credit co-operative movement can be considered to date from the early twentieth century. It followed the French agricultural credit bank model and the basic ideas of Friedrich Wilhelm Raiffeisen, which spread thanks to the social

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doctrine of the Catholic Church. As in the rest of Europe, it was a collective response by small and medium-sized farmers to being sidelined by the big banks. The nascent cooperativism was given strong institutional backing by the 1906 Farmers Union Law (*Ley de Sindicatos Agrícolas*), which gave professional farming organisations important privileges in the form of tax exemptions and other advantages for rural credit cooperatives. This was the first law in Spain to regulate the mutualist principles and cooperative institutions.

The 1906 law encouraged the spread of farmers' unions and a large number of rural cooperative banks (*cajas rurales*): at the beginning of the 1920s there were around 5000. The model was based on setting up small local cooperative banks linked to the Catholic farmers' unions. Nevertheless, their poor ability to organise themselves as a group and develop a farm credit market condemned them to a marginal position within the Spanish financial system, dominated by the big banking status quo.

However, during the 1960s and 1970s a number of factors roused the cooperative banks from their lethargy and triggered a stage of considerable growth. These factors included:

- (a) The beginning of reform in the Spanish financial system, which brought recognition of the rural cooperative banks as credit institutions and a start to harmonising the different monetary financial institutions. The Banking Regulation Law (*Ley de Ordenación Bancaria*) of 1962 expressly stated that *all grades of rural cooperative banks shall be reorganised to strengthen their purposes at the service of agricultural credit. Without prejudice to the discipline to which they are subject at present, the Treasury Ministry shall exercise the inspection and control of the rural cooperative banks to ensure their compliance with their exclusive purposes and coordination with general credit policy*. In 1971 they came under the regulatory control of the Bank of Spain and their credit activities were regulated by the 1978 regulations.
- (b) A period of great economic growth and modernisation in agriculture increased the demand for farm credit. It was met in part by institutions such as the rural cooperative banks that were part of the fabric of the farming world and were particularly well-adapted to the peculiarities of agricultural loans. The slogan *el dinero del campo para el campo* (the countryside's money for the countryside) was a call to place available funds on deposit in the rural cooperative banks, where in part they would be returned to the sector in the form of credit and loans.
- (c) The development of farming was accompanied by the spread of associationism as a way to generate greater value added for the farmers. This led to a proliferation of farming cooperatives, particularly for marketing and processing agricultural products.

As a result of the spread of credit cooperatives, the sector as a whole organised itself around a central body, Caja Rural Nacional. This was set up in 1957 and acted as the interlocutor between government and the rural cooperative banks with more limited geographical scope. In turn, provincial rural cooperative banks formed

through the conglomeration of smaller-scale ones became consolidated as the model throughout most of Spain. In this way, local- or district-level cooperatives disappeared from most of the country except in the East and South, where, in response to their marginalisation by the central body, they created a separate, independent organisation of their own.

The 1970s also saw a proliferation of non-farming credit cooperatives in urban areas. As a result of the advantages offered for setting up cooperatives and the difficulties in establishing private banks, around 40 'urban' credit cooperatives were born during this period, linked to professional bodies or to cooperative company groups. Nevertheless, bad management in many cases and the deregulation of the banking sector led to the disappearance of practically half of these. The Mondragón group's *Caja Laboral Popular*, set up in 1959, deserves a special mention as an example of the dynamic role that a credit cooperative can play in the leadership of a group of industrial and commercial cooperative companies in the Basque country.

In response to the greater presence of credit cooperatives, specific regulations were drawn up to govern them. Three major provisions of Royal Decree 2860/78 aimed to make these institutions take part in the transformation of the Spanish financial system: making the organic and functional characteristics of the different credit and savings institutions at the same time more homogenous and more flexible; establishing disciplinary rules to ensure their financial solidity; and making the governing bodies of financial institutions more democratic.

All these measures helped to increase the presence of the credit cooperatives in the financial system. Nevertheless, strong growth without the consolidation of sufficient reserves, the lack of professionalism in their management and the effects of an agricultural crisis halted their expansion and led to a number of serious problems that hindered their consolidation and cast the rural cooperative banks into deep crisis in the 1980s. As a result, around forty rural cooperative banks disappeared between 1984 and 1990, the disarray of their existing organisation led to the liquidation of *Caja Rural Nacional* and a new structure had to be created for this sector.

The crisis of the 1980s was influenced by the difficulties that the farming sector was going through and, above all, by managers who ignored the rules of prudence, concentrated risks without due control and operated in sectors where they did not have sufficient information or experience. This slack management was compounded by scanty observance of the cooperative principles as regards the openness of their relations with the members. The absence of external checks on the central organisations and poor group cohesion are further factors that made it difficult to prevent the crisis and to adopt appropriate measures to tackle it.

The resulting situation made it necessary for the authorities to intervene to re-establish confidence in these cooperative institutions and in the reorganisation of the sector. The reorganisation plans that were drawn up in 1984 provided for a series of measures to restructure the assets of the crisis-hit cooperative banks. At the same time, the coordination needs of the credit cooperatives were met by the creation of *Grupo Asociado BCA-CRA*, following the model of the French *Credit*

Agricole. Although this Associated Group did not last long, it deserves at least some attention. On the one hand, *Banco de Crédito Agrícola* (BCA), a state-owned bank entrusted with channelling official credit to farming, assumed the leadership of the group and acted as its controller. On the other hand, the associated rural cooperative banks (*cajas rurales asociadas*—CRA) placed at its disposal a dense network of branches throughout Spain, channelled a large part of their cash to the public bank and submitted to certain directives from it. The new logotype created at that time to relaunch the group, the yellow ears of wheat on a green background, have remained as the symbol of the rural cooperative banks.

However, later developments showed up major cracks that led to the breakdown of the Associated Group in 1988, only 4 years after the agreement had been signed, as a result of the imbalance of power in the governing bodies and the attitude of the authorities towards the disappearance of some rural cooperative banks. For instance, officials encouraged the absorption of rural cooperative banks by savings banks while *Banco de Crédito Agrícola* stood by and did nothing.

In view of this situation, the Spanish cooperative credit institutions looked for an alternative form of organisation. In 1990, they set up *Banco Cooperativo Español*, S.A. Its shareholders were the rural cooperative banks that voluntarily joined it and the German cooperative group *Deutsche Genossenschaftsbank* (DG Bank). *Banco Cooperativo Español* tries to provide banking services to its members which they would be unable to access individually, owing to their small size, and to take on the role of the central body of the rural cooperative banks group, using the rural cooperative banks' association (*Asociación Española de Cajas Rurales*—AECR) and specialist companies such as its IT and insurance arms (*Rural Informática* and *Rural Grupo Asegurador*—RGA). The result is a decentralised system with voluntary integration.

Since then, the consolidation of this model of organisation has been threatened by weak cohesion and by not behaving as a true group, leading to significant pull-outs by some rural cooperative banks. This was the situation when the international financial crisis struck in 2007, although its effects on the Spanish credit cooperatives were relatively minor. Because of their smaller size, they were not as badly affected by the liquidity strains on the international markets, they had not taken extraordinary risks in large property developments and they kept their business close to what has been being called for since then: *back to basics*. As a result, they have not suffered major solvency problems, although the low general efficiency of the sector still needs to be remedied.

Consequently, strong sector concentration is being encouraged, both by conventional mergers or through what are known as Institutional Protection Systems (SIP), in which the associated institutions retain a certain degree of management independence.

Although in general the crisis did not damage the solvency of cooperatives as much as that of other institutions, the government proposed strict regulations for them, similar to Law 26/2013 for saving banks and banking foundations. Finally it was put off because of the cooperatives' opposition and the proximity of elections in 2015 (Table 1).

Table 1 Historical data on number of banks, branches, employees and total assets of credit cooperatives in Spain

	Number of institutions	% of banking system	Number of branches	% of operative system	% of banking system	Number of employees	% of banking system	Total Assets (10 ⁶ €)	% of banking system
1945	29								
1950	41								
1960	58								
1970	169								
1980	155	42.8	2668		10.3	9731	4.0	3371	3.5
1981	147	41.2	2841		10.3	10,347	4.1	4241	3.6
1982	154	40.7	3048		10.3	10,866	4.3	5060	3.7
1983	153	40.7	3197		10.3	10,880	4.4	5801	3.7
1984	149	40.4	3315		10.4	10,896	4.5	6091	3.3
1985	146	40.1	3350		10.3	10,823	4.4	7352	3.6
1986	138	38.9	3388		10.4	10,225	4.2	8406	3.2
1987	129	37.3	3248		9.8	10,153	4.2	9439	3.2
1988	117	35.0	3029		9.0	9674	4.0	10,072	3.1
1989	110	33.0	2890		8.4	9592	3.9	10,839	2.8
1990	107	32.7	2919		8.3	9968	4.0	12,321	2.9
1991	106	32.8	3018		8.7	10,643	4.2	14,154	3.0
1992	101	31.7	3080		8.7	11,016	4.4	15,548	3.0
1993	100	31.6	3072		8.7	11,225	4.5	17,938	2.9
1994	99	31.3	3107		8.7	11,195	4.5	20,151	3.0
1995	97	30.5	3195		8.8	11,626	4.7	23,399	3.2
1996	97	31.0	3311		8.9	12,024	5.0	25,983	3.4
1997	97	31.6	3468		9.2	12,804	5.3	28,551	3.5
1998	97	32.3	3607		9.3	13,292	5.5	31,721	3.6
1999	94	32.4	3744		9.6	13,855	5.8	34,811	3.6

(continued)

Table 1 (continued)

	Number of institutions	% of banking system	Number of banking branches	% of operative system	% of banking system	Number of employees	% of banking system	Total Assets (10 ⁶ €)	% of banking system
2000	92	32.7	3888		10.0	14,495	6.1	39,601	3.7
2001	89	31.7	4091		10.6	15,580	6.5	46,069	3.9
2002	85	30.9	4275		11.1	16,414	6.9	50,485	3.9
2003	84	31.2	4460		11.3	17,067	7.1	56,162	3.9
2004	83	31.2	4563		11.3	17,650	7.3	65,132	3.9
2005	83	30.9	4657		11.2	18,395	7.4	82,180	4.0
2006	83	30.5	4771		11.0	19,382	7.6	98,123	4.1
2007	83	29.6	4953		11.0	20,429	7.6	110,765	3.9
2008	81	28.3	5097		11.2	20,940	7.7	115,846	3.7
2009	81	28.9	5043		11.4	20,757	7.9	122,933	3.9
2010	80	29.0	5018		11.7	20,545	8.0	125,702	4.0
2011	74	30.2	4928		12.4	20,036	8.2	126,891	4.0
2012	68	29.6	4832		12.4	19,674	8.4	131,649	4.2
2013	65	27.0	4651		13.9	18,910	8.9	125,593	4.4

Source: Up to 1980, Martín Mesa (1988). From 1980, Bank of Spain and UNACC

2 The Current Model

Credit cooperatives are governed by Law 13/1989¹ (LCC), by the Regulations pursuant thereto (adopted by Royal Decree 84/1993² (RLCC) and, secondarily, by the national Cooperatives Act, Law 27/1999³ (LC). The Spanish Constitution (CE) orders the authorities to encourage cooperatives through appropriate legislation (CE art. 129.2). Additionally, cooperatives are subject to special fiscal legislation (LRFCA, Law 20/1990⁴) and to accounting rules adapted to their peculiarities (Order EHA/3360/2010⁵).

2.1 *Governance and the Mutual Spirit: The Reasons for the Creation of Cooperative Banks*

The Spanish credit cooperatives were set up to meet the financial needs of their members, who were united by a common bond. The rural cooperative banks were created to address the financial needs of farmers and farm cooperatives, essentially, and the professional credit cooperatives, which arose at a later date, were associated with professional bodies such as the official colleges of engineers, architects, pharmacists or lawyers.

Apart from these cases, most credit cooperatives have resulted from mergers or reorganisation processes among other cooperatives.

Depending on how they were formed, the credit cooperatives can be classified into:

- (a) Rural cooperative banks set up by farmers and farmers' cooperatives to meet their financial needs
- (b) Local rural cooperative banks formed by splitting off the credit section of a farmers' cooperative
- (c) District, provincial or regional level rural cooperative banks, formed by the amalgamation of farmers' cooperative credit sections and/or local rural cooperative banks or set up on the initiative of federations of farmers' cooperatives at these levels.
- (d) Credit cooperatives founded by professional bodies such as the official colleges of engineers, architects, pharmacists or lawyers. The only remaining ones of this type are those of the engineers and architects, as the others have changed their form or been absorbed by other credit institutions.

¹ <http://www.boe.es/buscar/act.php?id=BOE-A-1989-12296>

² <http://www.boe.es/buscar/act.php?id=BOE-A-1993-4684>

³ <http://www.boe.es/buscar/act.php?id=BOE-A-1999-15681>

⁴ <http://www.boe.es/buscar/act.php?id=BOE-A-1990-30735>

⁵ <http://www.boe.es/buscar/act.php?id=BOE-A-2010-20034>

- (e) Credit cooperatives set up as the financial instrument of a cooperative company group in the industrial, commercial or service sector. This is the case of Mondragón's *Caja Laboral Popular* and of *Caixa Popular*.

In every case, initially the founders and members of the credit cooperatives shared much the same background, but over time, as the cooperatives have grown and extended their membership to other more heterogeneous and urban groups, the common bond has weakened. Nevertheless, permission to establish a new credit cooperative can be refused if the members have no shared interests or financial needs (RLCC art. 5.2).

The governance of credit cooperatives is shared between the membership (general meeting and board of directors) and the management.

The cooperative principle of participatory democracy is reflected in the voting rights that every member possesses; in the principle of 'one member, one vote' in most credit cooperatives; and in the legal limits on the number of votes that may be cast by any one member (not more than 2.5 % for an individual and 20 % for a legal person) and by legal persons that are not cooperatives (not more than 50 % in total). However, multiple voting rights, and even rights proportionate to capital, are possible in first and second tier cooperatives, and member participation in general assemblies is more restricted than in the case of bank shareholders (LCC arts. 9.2 and 7.3).

Firstly, the General Meeting need only be convened 15 days before it is held, compared to month for a bank. Secondly, if it is the Annual General Meeting it is advertised on the a notice boards in the headquarters and branches, though if the cooperative has over 500 members it must also be advertised in one of the highest-circulation newspapers in the province (LC art. 24.1), whereas notices of bank general meetings have to be published in the Official Gazette of the Company Register and the bank's web page or, if it does not have one, in a newspaper with a province-wide circulation.

In the larger cooperatives, preparatory meetings are often held locally in order to facilitate participation by their geographically scattered membership. However, it is not necessary to have held all the preparatory meetings before the meeting of delegates can take place, as 75 % is sufficient, nor do all the delegates elected at the preparatory meetings need to be present, as the quorum for holding the meeting of delegates and for the agreements it adopts to be valid is 40 %. Holding preparatory assemblies does not really make it easier for cooperative members to take part. Cooperative law has not yet provided for telematic attendance at meetings, as is allowed for commercial companies. Using the new information and communication technologies would undoubtedly facilitate democratic participation by credit cooperative members.

The data on member attendance and participation in the cooperatives' meetings could lead to the conclusion that there is a democratic deficit. However, it has been shown that when the members internalise the decisions as being important they mobilise, and they can even reject decisions that had been taken by the management and the board of directors, as has been seen recently on various occasions.

The general meeting elects the board of directors, which is normally made up of 12 members, mostly prominent members of the cooperative (68 %) or directors of other associated cooperatives (20 %); independent directors are infrequent (1.7 %). The system by which the credit cooperative directors are elected makes it difficult for the members to take part democratically. Firstly, the directors are elected through closed lists. Secondly, candidacies can be presented by members of the board of directors or by members with high percentages of representation (5 % of the members, 250 members or 25 % of the share capital). Removal of credit cooperative directors is subject to more conditions than in the case of a bank director, and two-thirds of the votes are required to hold them to account, compared to the simple majority that is required in a bank.

Although the general manager of a credit cooperative is not an organ of the cooperative but an employee, he or she is subject to conditions as regards incompatibilities, prohibitions and limitations in the performance of his or her functions that are similar to those for the directors. The general manager's powers are essentially concerned with the management and administration of the business, but include convening the board of directors and deciding on transactions with third parties, a decision which in other types of cooperatives lies with the members and must be allowed by the cooperative's statutes.

In recent years the credit cooperatives have made great efforts to improve the qualifications and professionalism of their managers, but some shortcomings are still apparent. The long service of the managers, around 20 years, gives an indication of their considerable independence from the governing bodies.

The European rules on assessing the suitability of members of the management bodies and those responsible for key functions were transposed to the RLCC by Royal Decree 256/2013. One of the requirements for obtaining and conserving authorisation as a credit cooperative is that the directors must be persons of recognised commercial and professional probity who have the adequate knowledge and experience to fulfil their functions and are in a position to exercise good governance of the institution. These requirements also apply to the general manager or similar positions and to those responsible for internal control functions and other key posts for the daily conduct of the institution's business. Information on all the above must be recorded in the Bank of Spain's Register of Senior Officers (*Registro de Altos Cargos*).

A natural or legal person may become a member by requesting membership and meeting the conditions laid down in the cooperative's statutes, which usually require ownership of at least one registered share documenting a contribution to capital of no less than 60 Euro (LCC art. 7). This contribution may be remunerated within the limits provided in law in the event of there being sufficient net income or freely-distributable reserves (RLCC art. 10).

Reimbursement of capital when a member leaves the cooperative has been limited since 2004, when Spain extended the obligation to draw up annual accounts in accordance with International Accounting Standards (IAS) to all credit institutions. Contributions to capital are reimbursed in the conditions set out in RLCC art. 10, and only if authorised by the board of directors. In no case may reimbursement

be authorised if this would lead to shortfalls in the mandatory capital requirement, reserve or solvency ratio cover (LCC art. 7.4).

2.2 *The Bank's Activities with Members and Non-members*

The corporate object of Spanish credit cooperatives is to serve the financial needs of their members and others by pursuing the activities proper to credit institutions (LCC art. 1). Consequently, they operate with their members for preference but can engage in credit operations with non-members with up to 50 % of their total assets (not including operations with members of member cooperatives, the investment of spare cash or the purchase of shares).

In practice, the credit cooperatives have universalised their clientele far beyond their agricultural origins by accepting new customers in two main ways: accepting them directly as members through a small contribution to the share capital (normally 60 €) or accepting members of an associated cooperative (agricultural, industrial or, less frequently, service or retail, in which case the initial contribution tends to be even smaller). In this way, the membership of Spanish credit cooperatives, around 2.5 million, approximately matches the number of customers involved in loan operations. This is because the credit cooperatives usually make membership one of the conditions for granting a credit or loan. However, the clientele of the cooperative banks as deposit takers is over ten million, as their customers include their members' families, among others.

Lastly, it should be pointed out that in their business activities, the credit cooperatives do not normally make a distinction in the treatment of their member and non-member customers.

2.3 *Other Services: Insurance, Stockbroking, Etc.*

Credit cooperatives are considered credit establishments (Royal Decree 1298/1986) and may engage in all the types of lending, borrowing and service operations that other credit institutions are permitted to undertake, laid out in Directive 2006/48/EC (article 3 of the credit cooperatives law). Those that require a certain scale are normally provided by the central organisations (*Banco Cooperativo Español* or its specialist companies).

Credit institutions are also allowed to compete with stockbroking companies, so the credit cooperatives can operate directly on the stock exchange. Grupo Caja Rural has an on-line stockbroking service, RuralBols@, which can undertake all types of stock market operations and also provides information to help its customers to optimise their stock market investments.

However, the cooperative credit institutions account for a relatively small proportion of stock or securities market issues, both because of their relatively

small individual size and because they have less need of wholesale capital market funding. The members' contributions to the share capital of the cooperatives cannot be traded on the Spanish stock market and their issues of quoted securities are very small: between subordinate bonds, securitised assets and mortgage debentures, they make up no more than 1 % of the total securities issued by credit institutions.

Other products and services that the credit cooperatives normally offer in addition to traditional banking and stock broking include on-line banking, credit and debit cards, mutual funds, the *Telepeaje* toll tag system, renting, insurance, pension plans, a property portal or ticket sales for shows, exhibitions, sporting events, etc.

2.4 The Relation Between Local, Regional and Central Banks

The Spanish financial system is currently undergoing an extraordinary transformation and the credit cooperatives are no exception in this respect. All the credit cooperatives belong to the National Union of Credit Cooperatives (*Unión Nacional de Cooperativas de Crédito*), which advises its members and publishes the most important information on its sector. Most of them also belong to the Spanish Association of Rural Cooperative Banks (*Asociación Española de Cajas Rurales*) and form the *Grupo Caja Rural*, which is headed by *Banco Cooperativo Español, S. A.* This bank provides financial services to its associates and is complemented by other companies in the group such as the IT company *Rural Servicios Informáticos*, the fund manager *GesCooperativo*, the insurance company *Seguros RGA*, or the property company *Rural Inmobiliaria*. The German cooperative groups *DZ Bank* (formed by the acquisition of GZ Bank by DG Bank in 2001) and *R + V Insurance* have holdings in all of these. This setup follows a federated bank model inspired by decentralisation, subsidiaries, solidarity, cooperation and territoriality.

Despite having been set up in the 1990s, the *Grupo Caja Rural* structure is not completely consolidated. *Caja Laboral Popular*, associated with the Mondragón cooperative group, has always remained aloof, while *Cajamar*, the largest of the originally rural cooperative banks, split off because of management disagreements and created an alternative group called *Banco Social y Cooperativo* (Social and Co-operative Bank), which accounts for over the 44 % of the total assets of credit cooperatives in Spain.

The Bank of Spain's aim to set up a single Institutional Protection System under the umbrella of *Banco Cooperativo Español* has not so far come into being and the direction that the group is taking at the moment is to consolidate a number of regional cooperative groups with relatively weak links to the central organisation.

As a result, totally independent local, district and regional institutions currently coexist, although the smaller ones are likely to join higher-tier cooperatives,

whether by being absorbed or with a certain degree of autonomy, constituting a hybrid system.

2.5 The Minimum Capital for the Establishment and Functioning of a Cooperative Bank

Spanish law, in application of European directives, requires certain minimum levels of capital, fully subscribed and paid up, in order to engage in banking activities. The general level of 5 million euros can be lower when the institution only operates in a limited sphere. For instance, the minimum for credit cooperatives that operate in municipalities with 100,000 or fewer inhabitants is 1.05 million euros of equity, while for a sphere not exceeding the autonomous region it is 3.6 million euros and 4.8 million euros if it exceeds this sphere.

The credit cooperatives are also subject to the latest financial regulations adopted after the crisis in Spain, following the criteria of the European Union and the Basle III accords. The most important achievement has been the implementation of the framework for cooperation in the control of supervision and solvency within the Single Supervisory Mechanism (SSM) [*Regulation (EU) No 468/2014 (ECB/2014/17) of 16 April 2014*]. This includes setting minimum reserves, updating the deposit guarantee systems, uniform rules and procedures for the restructuring and resolution of credit institutions with problems, measures against market abuse, fiscal considerations and strengthening investor protection. The institutions supervised, which can receive assistance under the European Stability Mechanism, are classed as ‘significant’ or ‘less significant’ institutions. The second group, the ‘less significant’ institutions, are almost all Spanish credit cooperatives and are supervised directly by the Bank of Spain. Only one credit cooperative, *Cajamar*, is considered ‘significant’ and is therefore supervised by the European Central Bank (ECB). This new legal framework for credit institutions is reflected in Law 10/2014 of 26 June 2014 and Royal Decree 84/2015, which completed the transposition of Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, and other European regulations.

Since the financial crisis, increased emphasis has been placed on monitoring compliance with the equity requirements in relation to risky assets. In general, the Spanish credit cooperatives show greater ease in meeting the 9 % minimum requirement (increased in January 2013) and the instruments that make up their equity are also of better quality. In fact, Spanish cooperative banks typically hold around 2–2.5 % more capital than commercial or savings banks. Moreover, tier 1 common equity or core capital (common equity and reserves) make up 88 % of the total equity of the credit cooperatives, compared to 73 % for the banks and

savings banks. The excess solvency of the Spanish credit cooperatives is largely due to their policy of retaining between 65 and 80 % of their annual profits.

2.6 The Guarantees System in Cooperative Banks

The credit cooperatives, like other credit establishments, are subject to a complex system of guarantees to ensure their liquidity and solvency, over and above the capital requirements referred to in the previous section.

On the one hand, they are governed by a special administrative supervision system (Law 26/1988 for individual institutions and Law 5/2005 for financial conglomerates). On the other hand, like the banks and savings banks before them, the credit cooperatives have had to set up a specific deposit guarantee fund (required by Royal Decree Law 18/1982) to guarantee the deposits placed with them and the restructuring and refloating of credit institutions in difficulties. If a credit cooperative or any other credit institution became insolvent, the respective fund could offer financial assistance such as non-refundable grants, guarantees, loans on favourable terms, subordinate financing, or the acquisition of damaged or unprofitable assets; it could also help to restructure the institution's capital by subscribing capital increases.

Royal Decree-Law 16/2011 of 14 October 2011 created the new Credit Institution Deposit Guarantee Fund through fusion of the three above-mentioned specific funds. Its purpose and function is limited to guaranteeing deposits held by credit institutions and its old function of strengthening their solvency has been taken over by the Fund for Orderly Bank Restructuring (FROB, the abbreviation of its Spanish name). The Guarantee Fund is made up of contributions from the credit institutions. It is governed by the rules of Directive 2009/14/EC, Directive 2014/49/EU and Law 10/2014 (mentioned in Sect. 2.5).

In addition, *Grupo Caja Rural* has voluntarily set up a Solidarity Fund to forestall and, if necessary, solve insolvency or mandatory equity cover requirement situations among its members.

To address the 2008 crisis, following the programme of assistance to Spain for recapitalising its financial system agreed in the Memorandum of Understanding of 20 July 2012, the Spanish government took extraordinary measures which included setting up the above-mentioned Fund for Orderly Bank Restructuring (FROB—*Fondo de Reestructuración Ordenada Bancaria*) through Royal Decree Law 9/2009. The purpose of this fund is to manage credit institution reorganization processes and help to reinforce their equity. The fund can be employed to restructure institutions with weaknesses in their economic and financial situation, and also to reinforce the equity of institutions without any weaknesses or solvency problems.

Should a credit cooperative undergo a banking reorganization process, the FROB could contribute to its funds by subscribing or acquiring contributions to its capital. Furthermore, Law 9/2012 also created the Company for the Management of Assets Resulting from Bank Restructuring (SAREB, the abbreviation of its

Spanish name, *Sociedad de gestión de activos procedentes de la reestructuración bancaria*, also known as the ‘bad bank’). This company can receive the assets and liabilities arising from the restructuring process. However, as already mentioned, so far the credit cooperatives have not presented solvency problems and have not been involved in restructuring processes for this reason.

What they are engaged in, however, are integration processes to increase their size. This integration can take place through mergers, general assignment of assets and liabilities, the creation of second-tier cooperatives or cooperative groups, or Institutional Protection Systems (SIP). At all events, the measures introduced by the government to confront this crisis are available to the credit cooperatives just as they are to the other credit institutions.

A peculiarity of the Spanish system is that while the supervision of the credit institutions’ solvency falls to the Bank of Spain, the Autonomous Communities (regions) also possess prudential supervision powers, cooperating with the Bank of Spain in this respect.

2.7 Profit Distribution in Credit Cooperatives

Spanish credit cooperatives differ widely in their distribution of surpluses. Once the balance has been determined, including the proceeds of lending to non-members and capital gains or extraordinary income of all kinds, the losses from previous years, tax liabilities and interest on paid-up capital are deducted.

Interest may be paid on the capital contributed by members if this is allowed by the cooperative’s statutes. Such returns are limited to a rate no higher than six points above the statutory rate of interest and conditional on the cooperative’s meeting the solvency ratios and minimum equity requirements and on there being no losses carried over. They may not be counted as operating costs or expenses.

Out of any available surplus, at least 20 % must be assigned to provisioning the mandatory reserve fund and at least 10 % to the education and promotion fund (this provision is tax-deductible up to a maximum of 30 %). Both of these funds are non-distributable except in the event of the cooperative’s changing its form and the latter is also not attachable (with the exception of the immovable property of the cooperative).

The data from the years previous to the financial crisis give a general picture of the accounting profit’s being distributed to taxes (around 15 %), interest on capital contributions (10 %) when allowed, and the remaining 75 % constituting the available surplus. The available surplus is mainly assigned to mandatory and voluntary reserves (80 %), the education and promotion fund (12 %) and dividends to cooperative members and other purposes (8 %).

2.8 Tax Policy for the Credit Cooperative System

Like other cooperatives, credit cooperatives are subject to a special tax system under the Cooperative Tax Regime Law (Law 20/1990) and, in the Basque Country, the region's autonomous rules (*normas forales*), and by Decree 1345/1992 which regulates the tax on the consolidated profits of cooperative society groups.

Under Law 20/1990, the credit cooperatives' profits are liable to company tax. Those obtained in the course of their ordinary activities are taxed at 25 % and their extraordinary profits at the general rate of 30 %. The Basque country's tax legislation generally applies lower company tax rates. As a result, credit cooperatives pay company tax on all their profits at 28 %.

Credit cooperatives enjoy other tax benefits under Spanish and Basque law, such as in the capital transfer tax and stamp duty on acts of establishment, capital increase, merger, split, award and cancellation of loans, in the acquisition of goods and rights for the education and promotion fund and in the economic activities tax (95 % tax relief).

2.9 Credit Cooperatives Mainly Act as Deposit-Takers

Because of their size and operative limitations, the credit cooperatives have traditionally behaved mainly as deposit-takers in a system in which the private commercial banks have obtained inter-bank funding from saving banks and credit cooperatives.

This situation changed considerably with the extraordinary expansion of credit between 2001 and 2007, when the credit extended to resident sectors of the Spanish economy grew far more than deposits. The resident private sector deposit-to-loan ratio of the cooperative banks fell from 119 % in the year 2000 to 94 % in 2010, while the ratios for the banking system as a whole were respectively 93 % and 80 %. As a result, credit cooperatives have been relatively well-insulated from the liquidity problems that the Spanish banking system has experienced during the financial crisis.

2.10 Margins and Interest Rate Policy

Because of their retail banking orientation and dense network of branches, particularly in places that other credit institutions do not reach, the profit and loss accounts of Spanish credit cooperatives present certain peculiarities. On the one hand, credit cooperatives obtain higher interest margins than banks and savings bank, but on the other hand, their operating costs are higher. As a result, their pre-tax profits (measured as a percentage of average total assets) are slightly lower

Table 2 Interest margin and pre-tax profits as a percentage of average total assets

	2005	2007	2010	2013
Interest margin				
– Private banks	1.04	0.98	1.10	1.98
– Savings banks	1.64	1.51	1.12	
– Credit co-operatives	2.31	2.30	1.56	1.58
Pre-tax profits				
– Private banks	0.91	1.13	0.50	0.42
– Savings banks	0.80	1.15	0.13	
– Credit co-operatives	1.07	0.97	0.28	0.30

Source: Bank of Spain, AEB, UNACC

than the average for the financial system as a whole. These high operating costs and consequently lower efficiency are one of the main weaknesses of the Spanish credit cooperatives in view of the likelihood of a more competitive future (Table 2).

3 The Importance of Credit Cooperatives in the National Banking Market

The cooperative credit system in Spain has a relatively low market share: around 4.4 % of the total assets of the banking system at the end of 2013. Nevertheless, in recent years its relative weight has increased, although moderately, following a slight decline during the years when the property boom was at its height (Table 3).

The growth of credit cooperative branches has been greater than in the banking system overall, reaching 11.7 % of the total. This share is considerably higher in rural areas, where the credit cooperatives play an important role in the financial integration of districts that are neglected by other intermediaries. Thanks to this network, they take around 6.5 % of resident private sector deposits, although this percentage varies widely in different parts of Spain. The cooperatives take more than 15 % of the deposits in Navarre, the Basque Country, Castile-La Mancha, Andalusia and Murcia, but under 2 % in Madrid, Catalonia and Galicia. In spite of the progress that has been made, the branch network of most cooperative banks in Spain is weak in the main cities and in tourist and commercial areas.

The proportion of deposits in the private sector is higher in relative terms than those of loans and total assets. This is the result of the retail banking character of the credit cooperatives, close to the customer and possessing a dense network of branches. Their lower unit size and links with the geographical areas in which they operate lead to a relatively greater weighting of funding to agriculture and to families. In spite of having diversified their credit operations in recent decades, because their origins lie in rural areas the Spanish credit cooperatives assign a significantly higher proportion of their loans to funding farmers. Around 12 % of the cooperative banks' loans for productive activities goes to the primary sector, compared to 2 % for the banking system as a whole. Equally, the credit

Table 3 Share of the credit cooperative system in the Spanish banking market

	2000	2010
Branches	10.0	11.7
Employees	6.1	8.0
Total assets	3.7	4.0
Liabilities. Resident private sector	7.3	6.4
Lending. Resident private sector	4.9	5.4
Lending. Agriculture	26.7	21.5
Lending. Industry	3.4	4.6
Lending. Construction	2.8	3.6
Lending. Households	5.4	6.6

Source: Bank of Spain

cooperatives' presence in the retail banking sector leads to greater specialisation in funding housing purchases by families, which make up 43 % of their total loans compared to 35 % for the banking system in general.

The changes in the business model have affected their financial performance. Spanish credit cooperatives base their resources on traditional deposit-taking. As mentioned above, their strong local orientation and neighbourhood bank character has allowed them to obtain higher financial margins than the rest of the banking system. Because of this, despite their efficiency problems they have presented higher return on assets (ROA) rates than the banks and savings banks. Nevertheless, because their equity is significantly greater, their return on equity (ROE) ratios have been slightly lower.

The current international financial crisis has affected the Spanish credit cooperatives to a significant degree, as the squeeze on their profit margins has increased and so have bad debts. However, Spanish credit cooperatives are generally encountering fewer problems than other banking institutions, owing to a series of circumstances.

Firstly, while they did take part in the excessive growth of credit in the years running up to the crisis, their expansion slowed during the years of maximum euphoria, when they lost market share (Table 1) to larger institutions that inflated the bubble by resorting to wholesale funding markets. Consequently, the barrier of their smaller size urged them to greater prudence and their comparative disadvantage in accessing international financial markets provided relative isolation from the credit euphoria.

Secondly, the initial impact of the crisis, between 2007 and 2009, was essentially financial and essentially affected international liquidity, so its impact on Spanish institutions, particularly cooperatives, was not very strong. However, from 2009 onwards the crisis affected the real economy badly, severely accentuating the basic imbalances. It was at that point that it hit the Spanish banks' balance sheets hard, through a combination of greater bad debt levels and an accumulation of devalued assets in Spain's heavily indebted economy. As a result, equity was eroded and confidence was lost.

To avoid insolvencies, in June 2009 the Bank of Spain set up the Fund for Orderly Bank Restructuring (FROB), as mentioned in Sect. 2.6, to help any bank in difficulties, encourage their integration, adjust oversized branch networks and ensure healthy balance sheets. The assessments and stress tests that have been carried out have proved satisfactory for the credit cooperatives: unlike some other institutions, no Spanish credit cooperative has needed recapitalisation and their solvency levels are more than adequate (only one small local cooperative, the *Caja Rural de Mota del Cuervo*, needed an ‘early intervention’ in January 2014, and its problems were solved by its merger with the regional credit cooperative, without any public-sector support). Despite this, the Bank of Spain is persistently calling for sector concentration, not so much on the grounds of solvency problems as of reasons of size and efficiency. In fact, the efficiency ratio of the credit cooperatives, defined as operating costs in relation to financial products, was 43.5 % in 2010 compared to 38 % for the system as a whole.

Nonetheless, strong concentration is indeed taking place among credit cooperatives, both through conventional mergers, splits and assignment of assets and liabilities (RLCC art. 20) and through Institutional Protection Systems (SIPs), as defined by European directives.

4 The Future of the System

In these times of change it is difficult to forecast the definitive future shape of the cooperative credit system in Spain, although a few possibilities may be ventured:

- The number of institutions will be considerably smaller, as they will unite with other cooperatives or join institutional groups. As a result, the major references in credit cooperatives will be *Laboral Kutxa*, which has a strong base in the North, *Cajamar*, which will be joined by other smaller institutions and consolidate into the largest Spanish rural cooperative bank, and all the other cooperatives, which will organise more or less cohesively in a two- or three-tier pyramid structure.
- If the savings banks (which have suffered the crisis more intensely) lose part of their social and local/regional character, as seems likely, the credit cooperatives can reinforce their neighbourhood bank philosophy, based on the cooperative identity, identified with the area where they operate, and on supporting the social economy of which they are a part. The credit cooperatives’ role in financial integration in Spain, especially in the rural areas, has grown with the disappearance of the savings banks.
- Their greater solvency and moderation during the ‘bubble’ has made the Spanish credit cooperatives more crisis-resistant. In principle, this could encourage greater growth than among other financial institutions. However, the predicted lengthy period of sluggish banking credit operations and adjustment in the real

economy would indicate that any progress is likely to be modest and limited by branch network and staffing level resizing to improve efficiency.

- Credit cooperatives are social institutions that have won a significant share of financial activity. The financial crisis has generated a dangerous concentration in a small number of institutions and an excessive homogeneity within the bank system. This combination is the main threat to competition and financial stability. Consequently, one of the cooperatives' challenges is to enhance competitiveness and biodiversity in the financial sector and avoid oligopolies. To live up to their potential, credit cooperatives must strengthen their transparency, their ethical behaviour and their governance values.
- The main weaknesses of the Spanish credit cooperatives are their high operating costs and their efficiency ratios. Greater integration could help to overcome these drawbacks and provide economies of scale that would allow them to undertake all types of banking business.
- At all events, the search for solutions in a changing climate could lead to redefining the structure of the cooperative credit system. Progress in the direction of greater integration and global cohesion would be desirable even if a two- or three-tier structure were retained.

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